COMMONWEALTH OF AUSTRALIA

JOINT COMMITTEE

of

PUBLIC ACCOUNTS

Reference: Review of Reports of the Auditor-General

CANBERRA

Monday, 12 August 1996

OFFICIAL HANSARD REPORT

CANBERRA

JOINT COMMITTEE OF PUBLIC ACCOUNTS

Members

Mr Somlyay (Chair)

Senator Crowley	Mr Anthony
Senator Macdonald	Mr Beddall
Senator Mackay	Mr Broadbent
Senator Watson	Mr Laurie Ferguson
Senator Woods	Mr Fitzgibbon
	Mr Georgiou
	Mr Griffin
	Mrs Stone
	Mr Vaile

The matter referred -

Review of reports of the Auditor-General.

WITNESSES

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JOINT COMMITTEE OF PUBLIC ACCOUNTS

Review of Auditor-General's reports 1995-96

CANBERRA

Monday, 12 August 1996

Present

Mr Somlyay (Chair)

Mr Beddall

Mr Griffin

Mr Vaile

The committee met at 9.32 a.m.

Mr Somlyay took the chair.

CHAIR—Before we commence proceedings, we need some resolutions on procedural matters.

Mr GRIFFIN—I move:

That the committee authorise publication, including the release of the proof transcript of the parliamentary database of the evidence given before it at the public hearing today, excluding any evidence taken in camera.

CHAIR—There being no objection, it is so resolved.

Mr GRIFFIN—I move:

That the following submissions be accepted as evidence to the Auditor-General's sectional committee review of 1995-96 reports of the Auditor-General and authorised for publication: Submission No. 7 of 1995-96 from the Department of Finance dated 1 August 1996; submission No. 8 of 1995-1996 from the ANAO dated 1 August 1996; submission No. 9 from Department of Foreign Affairs and Trade dated 12 August 1996; and, submission No. 10 from Austrade dated 12 August 1996.

CHAIR—There being no objection, it is so resolved. I now open today's public hearing, which is the second in this parliament, to review Auditor-General's reports using the new review procedures announced by the committee. We will be running these hearings in a round table format, which means that all relevant participants will be present to hear what the others are saying about an Auditor-General's report.

I would like to remind witnesses of three key features of this format. First, during the general discussion periods, committee members will first have the opportunity to ask questions, and any subsequent questioning or discussion between participants will need to be directed through the chairman. Secondly, for the benefit of *Hansard*, witnesses should identify themselves whenever they wish to make a comment. Thirdly, given the length of the program, statements and comments by witnesses should be kept as brief and succinct as possible.

I also remind witnesses that the hearings today are legal proceedings of the parliament and warrant the same respect as proceedings of the House itself. The giving of false or misleading evidence is a serious matter and may be regarded as a contempt of parliament. The evidence given today will be recorded by *Hansard* and will attract parliamentary privilege.

I refer any members of the press who are present to a committee statement about the broadcasting of proceedings. In particular, I draw the media's attention to the need to report fairly and accurately the proceedings of the committee. Copies of the committee statement are available from the secretariat staff present at this hearing.

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Audit Report No. 19 of 1995-96, The Management of Small and Medium-Sized Overseas Posts

CHAIR—We have convened this public hearing to examine the main issues raised in the Auditor-General's report entitled *The management of small and medium-sized overseas posts*. The Auditor-General has raised accountability questions relating to the management by DFAT and Austrade of Australian overseas posts, especially in regard to delivery of client services, financial control and improved management.

The JCPA will take evidence today on the deficiencies identified in the Auditor-General's report. We have the initial responses from the audited agencies. For this reason, we propose to dispense with lengthy opening statements. However, the committee would be interested to learn if any action has been taken, or is planned, to address the problems raised in the report. Mr Jones, would you like to make an opening statement?

Mr Jones—Thank you, Mr Chairman, and thank you for the invitation to appear. We in DFAT welcome the opportunity provided by the outside review by the ANAO of our overseas activities to enable us to improve our methods and to sharpen our focus. We worked very closely with ANAO in this audit and with Austrade, and we had a very collaborative relationship with them in the process. We are pleased with the generally favourable tone of the ANAO report and we are working on the implementation of the recommendations.

I would just like to make a couple of preliminary comments before moving to reporting to you on the implementation. To start off with, I would like to underline the difficult conditions under which many overseas posts operate, particularly the small and medium ones. A number of factors contribute to that. Firstly, they are very small work units by their nature and that means they have very limited flexibility in terms of deploying resources both financial and personnel.

Secondly, their workload is not under their control; it is driven by circumstances and developments in the country of accreditation or by tasking from Australia or other sources. So they have to adapt very rapidly to peaks and troughs in demand and try to balance their workload. There is a lot of judgment of priorities.

Thirdly, they are working in often quite difficult environments, certainly different environments, in which business conditions and standards are different from those we are used to here. The quality of locally engaged staff available is quite variable. Utilities are not as reliable as we are accustomed to and, of course, if your power goes off, many of your office systems these days go down—and we face that all the time.

Law and order and personal security questions are often quite difficult in the environments in which they work, not to mention problems for families: children, education, climate, health and so on. So these factors are part of the backdrop in which the posts operate. Generally speaking, in these difficult conditions the posts do a very professional job.

Another preliminary comment I would like to make relates to the figure used by the ANAO as the cost for maintaining an Australia based officer overseas. The figure contained in the report is $536,000 per annum. We have some doubts about the validity of the premises on which the calculation of that figure was based. The figure that we use for the cost to our portfolio of supporting an officer overseas is $228,000, and that includes the indirect costs—that is, the support costs in Australia. If you add the property costs which are the responsibility of the Overseas Property Group, which is not in our portfolio, that brings the figure to $375,000 a year.

It seems to us that some of the factors which were taken into account in calculating the $500,000-odd figure are not really justified. One seems to be that the cost of locally engaged staff in a post needs to be factored into the cost of the A-based officers, but it is not the case really that the role of locally engaged staff is essentially to support Australian based officers. In fact, as we try to reduce costs and streamline our operations, we are handing over to locally engaged staff functions which have in the past been performed by Australian based officers in order to try to reduce overall costs.

In addition, the figure is based on a calculation across all the agencies with Australian based staff overseas. It may be that the calculation of costs related to agencies other than DFAT has had an influence on the outcome as far as the ANAO figure is concerned.

My third comment is in relation to the costs of the head office operation. Again, it does not seem to us that factoring in virtually all the running costs of head office across the number of staff supported overseas is necessarily a sound basis of calculation given that home office operations are going to continue even if we do make changes to the number of A-based staff overseas. So we do have a difference with ANAO about the basis of calculating that figure.

Turning to implementation, I would just like to group the recommendations into three categories. As I say, we do not have major difficulties with the recommendations of the report. The first group would be procedures which the department has had in place for some time but which the ANAO recommends would usefully be sharpened in some way. We are happy with those recommendations. This includes the recommendations about establishing post objectives and observing the requirements related to diplomatic immunities and privileges.

The second category is those recommendations relating to processes which the department has under review or consideration, in some cases before the ANAO report, but which are taking time to make progress with because of the complexity of the subject matter. That set would include the recommendations about the role of the senior admin officer at posts, recommendations about regionalisation of administration and recommendations about the introduction of automated decision making procedures.

The third group of recommendations are those where implementation is directly affected by resource constraints. That would include on-line accounting links between posts and head office and language training for senior admin officers. I will just touch very briefly on the recommendations individually and the state of implementation.

The first recommendation was about establishing specific written post objectives prior to the opening of a new post. We do not have trouble with the principle of that one. We have not opened any new posts since the ANAO report, but I do want to flag that there are already in existence mechanisms for the establishment of objectives for posts. This takes two forms. One is the head of mission directive: every head of mission is given by our ministers a directive setting out the tasks to be accomplished while head of mission at the particular post. This is a comprehensive review of the tasking of the head of mission and the post for the time the head of mission is in charge.

The second mechanism is the post evaluation report, which is an annual review of the work of the post. There are three components to this: one is a review of performance for the previous year against established performance indicators; the second component is the establishment of a set of objectives for the post for the coming year; and the third component is the establishment of performance indicators for those objectives for the coming year. This is a process which is very comprehensive, which establishes agreed objectives for the post between the post and headquarters and which involves consultation with a wide range of clients of the post beyond DFAT.

The second recommendation related to the responsibilities of the senior admin officer positions and said that they were very demanding and perhaps difficult for an individual to manage. We agree with that. It is an issue we have been grappling with for some time, and we are making some progress with redistributing duties in a way that eases the burden on the SAO. This includes looking at whether all the functions are really necessary. We are looking at process re-engineering for the processes that the SAO oversights, we are looking at distributing some functions to locally engaged staff and we are looking at regionalisation or transfer of functions back to Australia. Recently we have transferred the responsibility for security arrangements at posts away from senior admin officers, and that has reduced their duties to some extent.

The work on the role of the SAO is being overseen by the department’s Review of Administrative Procedures, which has been operating now for about 15 months and which, as the ANAO report notes, is reviewing the full range of administrative functions carried out within DFAT. Its first focus was on the administrative load at smaller posts. So the work of the Review of Administrative Procedures fits quite neatly into the recommendations of the ANAO report.

The third recommendation was a regionalised approach to administrative processes. To a degree, we are already doing this in some areas. For example, technical officer support—that is, support by technical officers for our classified communications network—is handled on a regional basis by regional technical officers. Information technology support, to a lesser extent, is looked after by Paris and Washington for Europe and the Americas respectively. Some of our accounting mechanisms support is provided regionally from posts which have a particularly strong base in that area. Training, to a degree, we do on a regional basis by bringing staff together from other posts into one centre.

As the IT systems we are introducing are more extensively established, we will be able to increase the regionalisation of administrative functions. In some cases, where it is a question of sending data down a wire, it may be better to bring that function back to Canberra rather than do it on a regional basis because it is here that we gain best economies of scale and have staff costs which are relatively low.

The fourth recommendation was that as part of the Review of Administrative Processes we look at automated decision making procedures. Again, this is going to be dependent in part on the further extension of our non-national secure IT system. We are introducing that steadily now and are certainly looking very hard at finding ways of introducing automatic decision making procedures for such areas as leave, travel, salary calculations, overseas living allowances and other entitlements. We fully agree with the desirability of automated decision making procedures in these areas.

The fifth one was the introduction of on-line links between posts and headquarters for processing budget data and so on. As you probably know, Finance is introducing a requirement for direct lodgement of financial data by 1 July next year, and we will have e-mail links to all our posts established by then through our non-national secure system which will enable that data to be lodged. We will be extending those e-mail links to other functions which will enable a broader range of data to be introduced. One of the limitations here is the limitation on bandwidth to certain countries which makes it difficult to get access for data flows for a full range of categories of data.

The next recommendation was language training for senior admin officers. We do not have difficulty with the desirability of language capability for senior admin officers. It comes down, in the end, to resources and priorities and, certainly, we are doing what we can to extend that capability.

The next one related to compliance with the rules relating to the Vienna Conventions on Diplomatic and Consular Relations. We agree, again, that it is important to make sure that posts in their operations work consistently with these requirements. We have had a mechanism in place to draw this to the attention of officers since 1987, and in 1993 we upgraded our mechanisms for this. We require all staff on arrival to read the material setting out the rules and to sign a document stating that they have read and understood it and will apply it. We check that in our internal audit operations, and we are finding quite a high compliance rate, as we would expect. But we need to keep reminding people of this requirement, and we will do so.

The second last recommendation related to making that material available to officers at post as part of the induction kit issued to new arrivals. As I said, we are requiring new arrivals to read the material and sign a certificate stating that they have read it. So they do have access to it—it is provided to them when they arrive at posts. In some cases it is part of the induction kit provided to them, and in other cases it is part of a formal sit-down briefing.

The last recommendation related to the introduction of the international administrative system and the refinements to be introduced for the next version of it. We agree with those recommendations. We are working with other agencies towards the introduction of the second version of it.

A number of things we are doing which will help us prepare for the second version include working on refinement of clauses, which have been the subject of some debate or which have attracted attention for one reason or another; setting out, when a question has arisen about application of some part of the IAS provisions, the reasons for a particular outcome or decision; working on circulating best practice details to posts, where we find a mechanism which works particularly well; notifying central agencies of other departments of any problems that have arisen and of approaches we recommend; and asking both posts and agencies working in the system to give us a review at the end of the first year of areas where problems have occurred so that we can take account of those in the second version. So that is where we are with the implementation of those recommendations. Thank you for listening to these opening remarks.

CHAIR—Thank you, Mr Jones. For the record, could you please define what you mean by a small post and a medium post? Could you give us some examples?

Mr Jones—It may be better for the ANAO to speak on that because it is, essentially, their definition.

Dr Nicoll—Our definition was an evolving one and, essentially, we consulted with DFAT and Austrade about it. In practice, it meant that posts were considered as small to medium sized if they had less than 20,000 financial transactions and no more than about 100 staff.

CHAIR—Thank you. Mr Langhorne, would you like to make your opening statement?

Mr Langhorne—Yes. Austrade also welcomes the opportunity to participate in this hearing on the review of Audit Report No. 19. While the report identified a number of areas for Austrade to address, we were pleased that the report acknowledged the considerable effort and priority given to administrative reforms and the adoption of best practice management processes within Austrade itself.

Partly as a result of this audit, Austrade has developed a corporate government's training package, which is progressively being delivered in overseas regions and in Australia. The package aims to develop for staff an awareness of the key accountabilities in their role; an understanding of the critical importance of accountability for individual and collective actions, judgments and the use of resources; and the ability to exercise an appropriate balance between the front-end export impact work and the administrative side of what Austrade does. I would like to take the opportunity, if you agree, to tender a copy of that package to the committee, perhaps at the end of this particular hearing.

In relation to the recommendations and encouragement of Audit Report No. 19, Austrade is undertaking remedial and reinforcing action, as appropriate, to ensure that the Auditor-General's concerns are fully addressed. We have tabled a copy of our responses to the recommendations separately.

Austrade has made particular efforts to address the need to ensure that senior managers, particularly those appointed from the private sector, are fully appraised of their responsibilities in respect of post management and people management, public accountability and consular responsibilities where they are applicable.

The need to formalise agreements with agencies for whom Austrade provides administrative services at sole post is also recognised. There is also a need to formalise some of the linkages within the portfolio and ensure that communication lines are in place between DFAT and Austrade for the delivery of accurate and unambiguous information and, importantly, to ensure that both agencies are aware of where those contact points are. There is also the continuing need for review of administrative processes throughout the organisation via a combination of internal review, and internal and external audit.

I would just like to emphasise that the Austrade board makes sure that Austrade operates within an accountability framework that includes everyone in Austrade, from senior executives to junior staff. We in management and the board recognise that our achievements in maximising export impact of Australian exporters need to go hand-in-hand with public accountability for our actions and judgments and for the public resources entrusted to us. In that regard, we welcome the recommendations of the Auditor-General's report. As stated in the report, we agree with them all and we are in the process of implementation now.

CHAIR—Thank you. I will call on Mr Barrett to respond to those statements. Mr Barrett, you might like to address the discrepancy in the cost of maintaining an officer at an overseas post. The audit office's estimate seems to be about more than double that of DFAT's.

Mr Barrett—Thank you, Mr Chairman. I will just reiterate the basic reason for this audit first and re-emphasise that the management of Australia's overseas posts had not been previously scrutinised by the ANAO from a performance perspective. It was envisaged that this audit would form part of a broader review of Australia's representation abroad, focusing particularly on the Department of Foreign Affairs and Trade and Austrade as the agencies responsible for managing virtually all overseas posts.

The objective of the audit was to ascertain the extent to which DFAT and Austrade have made management of overseas posts conform to the models of good public administration that have been promulgated over some period of years, as you are well aware. In particular, the audit focused on the extent to which management of small and medium posts reflects best practice as set out in the Australian government guidelines and policies and other international comparisons.

The audit also focused on the extent to which certain administrative reforms have been implemented and on the quality of service provision from both agencies providing corporate support services to other agencies at posts and by those agencies acting as agents for the delivery of program services on behalf of other agencies. The overall conclusion, as you are aware, was that the evidence of good practice in both the agencies concerned should be recognised. As both have indicated in evidence this morning, they basically agree with the thrust of the recommendations and the areas in which improvements can be made and they are taking action accordingly.

In relation to the specific point you raised about the cost, before I ask the auditors concerned—Paul Nicoll and Helen McKenna—to respond on the detail of that figure, it is important to recognise the purpose of doing that. The purpose was for the agencies to get a better handle on what it was actually costing to maintain Australia based staff overseas. It was clear that no-one really had a firm handle on the total cost of so doing.

As to the nitty-gritty, these things can be worked out. I am confident about that. Even though there may be some difference after this morning's hearing, I am sure we can work with the agencies concerned to get a better feel for the figure. The figure Mr Jones said was in the order of $375,000 including an allowance for property. I can recall that the rule of thumb figure for a Finance officer overseas which included none of those costs—property costs, costs for head office, et cetera—was about $¼ million. So that just gives you another feel for the costs associated with maintaining overseas representation.

The notion was not simply comparing the two agencies concerned, but to really get across to agencies exactly what it was costing, including support from head office and, obviously, importantly property expenses. One should recognise—and it has been clear from the definition that has been provided about these offices, in particular—that the costs of our people abroad are the major cost.

We should be quite concerned at establishing what it does cost us to do this, particularly if we are establishing new posts or servicing posts that may not require the same A-based assistance as might have been felt to have been required in the past. So it really is having a finger on the costs and having that as part of the decision making at the time when you are considering new posts, changes to existing posts, amalgamations, et cetera. On that note, I will ask either Paul or Helen to respond on the detail.

Dr Nicoll—I would like to reiterate what the Auditor-General has said. What we were doing in the report in part was putting more data into the public arena about the true cost of our overseas representation. Often the information which floats around in different arenas refers to agency specific costs so we were trying to put all of the agency specific costs together for, as far as we know, the first ever total cost figures. That is the motivation.

In terms of the figures which Mr Jones mentioned a little earlier, the figure we quoted was for all government agencies; it was not for DFAT in particular. It was for agencies such as Defence, Immigration, DEETYA, Austrade and DFAT. Mr Jones was referring to the DFAT figure and we have no fundamental problem with that. If anything, our costs for DFAT would come out perhaps a little lower than the figures which he quoted.

That is the major explanation of what may appear to be a discrepancy. In practice, I do not think there is too much at all. Our figure refers to the cost to government as a whole, while the DFAT figure refers to DFAT in particular. Our actual estimate for that is fairly close to what Mr Jones was saying. It is about $323,000 per A-based officer per year, which is actually a little less.

Mr GRIFFIN—If you could take us through that a bit further, does that mean that officers from Defence and Immigration are costing us about $1 million?

Dr Nicoll—Yes.

Mr GRIFFIN—Do you want to run through that? That sounds interesting.

Dr Nicoll—One of the key drivers is the ratio of A-based to LES staff. If an Australian government agency employs a very high proportion of locally engaged staff, that is going to drive the figures in one way. DFAT did not have as many locally engaged staff as some of the other agencies so, therefore, its cost was certainly lower than the average figure which we reported in the report.

Mr GRIFFIN—So it basically relates to the ratio of locally engaged staff to Australian based?

Dr Nicoll—Yes. In the report we were very careful not to make any statement about whether any particular ratio is good or bad. It is up to the agencies themselves to make a decision on that. They are far better placed to do that than we are.

Mr GRIFFIN—Is ANAO looking at examining the operation of posts of other departments—Immigration, Defence and so on?

Dr Nicoll—Only so far as in this report we were trying to get a figure of what the total cost to government as a whole was. We did not go right into the costing for those other agencies. Our focus was principally on DFAT and Austrade with a little bit of data on the other ones.

Mr GRIFFIN—It may well be worth while having a look at other departments and instrumentalities operating within posts if there is such a great variation. Would Foreign Affairs and Trade like to comment on what the ANAO said on that matter?

Mr Jones—It is just a question, again, of methodology, I guess. From what Dr Nicoll says, one could be excused for inferring that there is an encouragement built in not to employ locally engaged staff because it drives up your total cost. Of course, in reality, locally engaged staff are a cheaper resource and we should use a system which encourages agencies, where possible, to transfer work to locally engaged staff as a cheaper staff resource than A-based staff. It seems to me that it is a bit misleading to leave the impression that agencies which have a lower share of locally engaged staff somehow are operating on a more expensive basis. Basically, these days we are trying to handle as much of our work as we can through locally engaged staff whose salaries tend to be low—because of the allowance factor, et cetera, and accommodation costs for A-based staff—and we think that transferring functions to locally engaged staff involves reducing the total cost of overseas representation, not increasing it.

Mr GRIFFIN—Would you like to comment on that?

Mr Barrett—I think that is a fair point. I would say that this was to try to give parliament a better idea about the representation costs and put it in terms of A-based officers to show that, if we have so many hundred A-based officers, the representation cost in total is of this order. I certainly agree that, if you were looking at the economic provision of services, it may well make a heck of a lot of sense to have one A-based officer with nine locally engaged staff rather than having three A-based and whatever trade-off between the two groups. The international interest in parliaments is what it is costing to have representation abroad, and this was a figure. I accept the comments that Mr Jones makes, but I think it is important that, from an overall point of view, we do have some better idea about not just the cost of having X number of people overseas; there are a lot of other costs associated with it and, on average, it is costing this amount.

Mr GRIFFIN—Mr Jones.

Mr Jones—We agree that it is important to know the costs. It is important for the parliament to know the costs and it is important for us, in managing our resources, to know the costs. The difference between us goes to the basis of calculation. That is perhaps something that our various accounting specialists should get to work on.

Mr GRIFFIN—It would be nice if we could agree on the costs.

CHAIR—Are you talking about accrual accounting and reporting in this context?

Mr Barrett—We would be.

Mr Peirce—Yes, they are accrual accounting costs that are put together in the $375,000. If you took an analysis of the financial statements, I think for the whole portfolio we looked at about $585 million as expenditure for last year. That included all resources received free of charge from all other providers and the analysis was based on that information.

CHAIR—Is there any international comparison? Can DFAT determine, at one of these posts, whether or not another foreign post in the same country has similar costs? Are there international comparisons?

Mr Jones—The ANAO may want to make some comment on that. It is the sort of thing we have looked at. It proves to be extremely difficult, because each country works on a completely different administrative system and trying to find comparisons we have found almost impossible. We carried out a major review of our overseas operations last year. We wanted to get some comparative data from other agencies and we talked to other foreign services but found that acquiring a meaningful figure that could be comparable was virtually impossible.

Dr Nicoll—As part of this exercise, we certainly talked with the equivalents of the Department of Foreign Affairs and Trade elsewhere, but not about this particular dimension of costs. It was more to do with other dimensions in the study like administrative practices. So we have nothing to add in terms of international comparison.

Dr McKenna—We would agree with DFAT: it is very hard to establish an international comparator that will hold up.

Mr BEDDALL—In a broader context, it was very pleasing to see that all the recommendations had been agreed and we are working towards it. Is it possible to give us a time frame of when you will implement the recommendations and, if so, could you advise the committee as each recommendation is implemented rather than just leaving it up to saying that it is all a good idea and down the track you will have it all implemented? Could you set out a time frame for us and, as each recommendation is implemented, advise us that that is the case?

Mr Jones—Yes, we are happy to advise you when they are implemented, although it comes down to a question of definition about the point of implementation, but we agree with the principle. The time frame will be different for each recommendation, of course. I do not know whether you want me to go through all of that now.

Mr BEDDALL—No. We would like to make sure that we get a follow-up rather than just everyone agreeing.

Mr Jones—Sure. There is no difficulty with that. Some of them will be conditioned by the introduction of the IT-wide area network linking all the posts. Some will require that before they are fully implemented. Others have a built-in time factor, like the introduction of the next stage of the international administrative system, which is to be introduced for 1997-98. When that is in place, we can. Yes, we are happy with the principle of your proposition.

Mr BEDDALL—Perhaps we could do it with on particular recommendation, that is, recommendation 1 in relation to a written set of post objectives. You advised that this was quite good because you had not opened a post since the recommendation; therefore, it was not required. Surely, by now, there would be a draft set of written post objectives, if we could please have a copy of that. What posts are due to be open within the next six to 12 months?

Mr Jones—Not many, I am afraid, for the moment. It is a difficult budgetary environment and if we were looking at anything it is probably in the opposite direction.

Mr GRIFFIN—So where are you looking at closing then?

Mr Jones—We have to await the outcome of the budget and then we will take stock. But yes, we are happy to give you a look at a conceptual list of post objectives. Could I just flag again the point I made earlier that we do have an objective setting system for posts. It is quite a sophisticated one. It involves establishing objectives, performance indicators and a review of performance against objectives for each post each year. This recommendation related specifically to opening new posts and to the period prior to the first annual post evaluation review for that post.

CHAIR—Could you please explain how the user pay pro rata is determined when apportioning cost charges to client agencies?

Mr Jones—This is under the IAS, I take it?

CHAIR—Yes.

Mr Jones—John Rigg, perhaps, can speak to this.

Mr Rigg—Are you referring to the fee that is charged each agency?

CHAIR—Yes.

Mr Rigg—That was determined by looking at each post and establishing which of the local staff provided services to all agencies in a common services sense. To the wage costs of those employees was added a margin for on-costs and other relevant costs of providing services such as medical costs of those employees; the costs of the community liaison officer at the post were added; and that was divided by the number of employees at the post to determine a post fee and that amount was devolved to each agency. The fee per person was devolved to each agency for the number of employees they had. That transfer of money, which totalled $8 million for all agencies, was part of the 1995-96 budget.

CHAIR—And the agencies were happy with that arrangement?

Mr Rigg—That was part of the negotiation process. We held a series of meetings between January 1994 and June 1995. Some 20-odd meetings were held with a working group which comprised the major agencies overseas in terms of numbers of people. The Department of Finance was also represented on that committee and the Department of the Treasury represented the smaller agencies. That fee and the quantum of money that was devolved to the agencies came out of that negotiation process.

CHAIR—I will put the same question to Austrade. The report states that Austrade calculates its charges for service provision at posts on a case by case basis. What aspects were taken into account in determining these charges?

Mr Langhorne—In the past, we have had a case by case approach to charging for services provided where we were actually managing the post. We are now moving to a process which is aligned with the approach that DFAT has taken in regard to working out what the cost of services are. In other words, taking into account in a more standard way across the board the nature of the services that we provide to departments that are working within posts, that we manage the cost of those services, including on-costs, and we are looking at wrapping that up into a formal standardised agreement with those agencies so that the whole process is transparent. It is standard across the world.

We believe that we will have that process completed by the end of this calendar year and agreements entered into with various agencies. We have drafted an MOU, a memorandum of understanding, to that extent. We are also looking at a similar arrangement with the department of immigration so that we should have all agencies that are in our posts covered.

As far as the user pays principles that were put in place by the department over the last 12 months are concerned, I can say that Austrade is completely happy with that arrangement. It seems to be working out well in practice in the field and will form a good base for future costings, in our view.

CHAIR—As a rule, trade commissioners are not career public servants, are they?

Mr Rigg—Sorry?

CHAIR—Trade commissioners are not usually career public servants, on the whole, so your problem would be different from DFAT from the point of view of training appointees so that they have an understanding of post objectives and responsibilities in public accountability?

Mr Langhorne—Austrade staff are employed under the Austrade act rather than the Public Service Act. There are some ties back into that process but, basically, we are covered by the same requirements for accountability for financial control and employment as the balance of the public sector. It is just that we happen to have our own act. Our costing arrangements and so on are very much aligned to those that would apply in a standard Public Service organisation. And we of course have to ensure accountability through our minister to the parliament.

CHAIR—Because many of your trade commissioners are not career public servants, do you have a difficulty or a special task in training them in terms of accountability requirements that DFAT, for instance, would not have to do?

Mr Langhorne—Yes. There is an issue here because the people that we do post overseas are a mix of what we would call career public servants—in other words, people who are in Austrade and are making a career out of the process—and those that we engage from the private sector under contract. This is one of the issues that was recognised in the ANAO report. We recognise that difference. About 20 per cent of our Australian-based staff overseas would be on contract from the private sector.

Since this report came out we have been introducing—it has been introduced now in full—a very detailed training package as part of our corporate governance process on accountability, so that people coming in from the private sector who are going to work for us for, say, three years and then go back into the private sector have a very good understanding of their obligations under our act and their obligations under the process of public accountability. That is not only, I might add, in the area of financial accountability, but also in the area of the way we handle our human resources, equal opportunity aspects and so on.

CHAIR—What consultation will take place now between Austrade, DFAT and the Auditor-General's office regarding agreement on estimated cost of officers posted overseas? Will we get a benchmark figure that the parliament can use as being an accurate estimate of the cost of establishing an officer overseas?

Mr Barrett—The first point I would make is that we will supply to the JCPA the calculations leading to the figure of $536,000, just for your information. What we can do is, I would suggest, look at the figures for DFAT as the major organisation concerned and get agreement on that. It may well be that Austrade might be in a similar position because of their particular program responsibilities. I stress that while we describe this as a performance audit it is more in the nature of a project audit in my terminology because we really have not looked at what we are getting for what it is costing us.

We have stipulated that there needs to be better specification of the objectives. People need to understand those objectives. What we are hoping is that people will focus on the full accrued costs as part of determining the efficiency and effectiveness in meeting those objectives. So it is important to have a fair handle on costs. Certainly, I would believe, it is important for parliament to understand the costs of representation. I think it is a fair point, as I said to Mr Jones, in relation to DFAT and to Austrade. If we can work out with them what are, for their particular programs, the costs of their representation over the next few weeks or so, we will certainly do that and we will come back to this committee. That is my suggestion.

Mr Jones—We are certainly happy to work on the cost analysis and the committee is welcome to have our figures as we have them at the moment. I think, from Dr Nicoll's comments earlier, there is not a significant distance between ANAO and us on the DFAT costs. In response to the Auditor-General in relation to objectives, I underline what I said before. That is, we do have an elaborate system of establishing objectives with performance indicators and reviewing performance each year against those performance indicators for all our posts. It is not as if there is not a system in place. The issue raised by the ANAO related to the establishment of new posts. As I said earlier, that covers the period before the first head of mission directive and the first annual post evaluation report. But there is a major process in place for all posts which establishes objectives for them and assesses performance against the objectives.

If I could just finish off here by answering the question you asked right at the beginning, which was what posts were covered in the audit, there is quite a wide range, but the largest was Hong Kong, which has 32 Australia based and 77 locally engaged staff—a total of 109. That is a post with a number of agencies represented from different branches of government, of course, and with a very big Immigration presence. The smallest DFAT post was Nauru with two A-based and four locally engaged staff—a total of six. There were some smaller Austrade posts covered because a number of Austrade posts are very small.

We have two other posts which were smaller than Nauru, but they are not fully self-supporting. One is Bridgetown, which has two A-based and two locally engaged staff—a total of four, but that is co-located with the Canadian mission which provides support for them, a formula which has proved to be quite successful and which we are looking for other opportunities to implement. The other one is the Holy See, which has one A-based and one locally engaged, for a total of two. Again, that is a mission that is supported by the embassy in Rome for other purposes.

Mr BEDDALL—I have actually had some dealings with places like Nagoya, which was, from memory, an Austrade post but doing consular work. Has that been a growing trend? Particularly Nagoya—I spent a couple of days there—was a very well run local office with the Austrade person very fluent in Japanese, very integrated into the Japanese culture. Has that been a trend developing in the smaller centres?

Mr Jones—Yes, it is indeed a trend. There are a number of posts where Austrade has established a very small Australian presence which picks up consular work as well. Peter Langhorne might want to say something about that.

CHAIR—Also, Mr Langhorne, do you want to say anything on the costs of establishing officers from Austrade? The figures you have quoted are DFAT only and do not involve Austrade.

Mr Langhorne—Austrade would be interested in being involved in any negotiations or discussions between the ANAO and the department on costs of overseas posts. We believe that we do have a good handle on costs of our posts. On average, our figure comes out very close to the department's at about $350,000 per A-based person. We would like to be involved in that. I would just emphasise that certainly within Austrade—I know it is happening within the department too—there is an increased emphasis on using professional locally engaged staff overseas as a substitute for Australian based staff. The methodology of costing has to be looked at very closely. That fact has to be recognised when you are loading costs on only to A-based staff, for example.

The other point I would make on costing is that we believe that the global network is just that. It includes the back end of the network, which is here in Australia. Some people would call it the front end of the network. The importance of the people working in Australia in their own right also needs to be taken into account. We would like the opportunity to contribute to that process.

In regard to the question of overseas posts and posts managed by Austrade, off the top of my head, Austrade runs about 17 posts as joint consulates and trade promotion type activities. We have an arrangement with the department whereby we look at the establishment of posts overseas. Japan is a good example; we have established a number of very small posts outside Tokyo and Osaka and also provide consulate services in those posts. That works extremely well in that we can provide a service at a reasonably low cost to Australian citizens from a consulate point of view and also provide the key activity at that particular location, recognised as the trade promotions side of the work.

Mr BEDDALL—Would they handle visa applications at those smaller places in Japan?

Mr Langhorne—No. In the case of those small posts, most of what we would call the processing type activity—visas, passports, et cetera—is either handled from Osaka or Tokyo. The same does not apply in some of our other posts where, again, it has been determined by the department and ourselves that the prime activity at the location is trade promotion related. In that case, our senior trade commissioner is also the consul-general at that location. In some of those locations the department provides the consular officer. Also in some cases the department of immigration provides immigration officers to assist in that process. We believe it works extremely well.

There is a need from our side to watch that we do not place these joint post activities in locations that have a very heavy consular workload—for example, in a place such as Hong Kong, where the representation and public diplomacy aspects of the work are very high. Therefore, if our senior trade commissioner was also consul-general, the person would be absolutely swamped with work. We try to limit the senior trade commissioner's time taken on consular work to around 20 per cent. The balance of the time is then spent on trade.

CHAIR—I am not yet clear on the question of costs. An average cost is $536,000. DFAT's costs are about $300,000-odd. Austrade's are about $300,000 odd. If $536,000 is an average cost, somebody is pretty high. Which agency is causing that?

Dr Nicoll—The data is on page 12, table 3. The figures suggest that DFAT was actually on the lower side of things. As I mentioned earlier, we are at pains not to make any value judgment about whether the ratio of A-based to locally engaged staff is good or bad; it is up to the agencies. There are some there which do suggest that the figure is a little higher. The Austrade one actually does come out a little on the high side. There are also one or two others there which show up like that.

We were less concerned about calculating the per agency cost than the total cost because the total costs to government have been increasing. By putting up more information in the public arena to the government and the parliament, both the government and the parliament will be better able to make decisions on where it wants to go with its overseas representation.

CHAIR—Are there any future plans to look at the larger foreign posts?

Mr Barrett—Discussion is currently going on about that.

CHAIR—Mr Jones, did you want to say something?

Mr Jones—The moment has probably passed, but I wished to say something in relation to this issue of small Austrade posts doing consular work. It is certainly useful for us where there is no requirement for DFAT to have a presence. If Austrade judges it is important for trade promotion purposes to have a presence, for them to be able to take on consular work extends our consular network very usefully in terms of services to Australian citizens overseas. It is something we welcome and it works well between us, as Peter Langhorne said.

CHAIR—On balance, there seems to have been good cooperation and response to the Auditor-General's report. Do my colleagues have any further questions?

Mr GRIFFIN—I have just another question on the matter of cost. Looking at the table on page 12, I take it that the total agency staff number is the total number of staff all up who are in these posts from the various agencies. I am still a bit intrigued. From that, it would appear that over 1,300 of the 1,800 staff are from Austrade and DFAT. The costs in those circumstances have been said to be well below the average which ANAO was working on. I just find the differences amazing; that is all.

Dr Nicoll—The data largely came from all of the agencies involved. We can have another look at those, but they are the data which came out of the exercise.

Mr Jones—In my mind, it raises a question about methodology, really. I doubt whether with these other agencies it costs so much more to maintain somebody in the post. It is a question, I think, of what is included in the figures. It suggests to me that really we ought to look at the methodology lying behind that figure.

Mr GRIFFIN—I would certainly be interested in seeing some comparisons. Can you show me in that table where I would establish that DFAT was at the 300,000 or so mark that DFAT talked about?

Dr Nicoll—The DFAT line—dividing 301 into $97,098,000—will come out at a figure a bit greater than $300,000 there.

Mr GRIFFIN—You are taking the A-based figure—the Australian based figure—and dividing that?

Dr Nicoll—Yes.

Mr GRIFFIN—So you are not taking into account the local staff at all. Is that right?

Dr Nicoll—The figure we have reported here represents the total average annual cost of an A-based staff member. There are other data, other indicators which can be calculated from here.

Mr GRIFFIN—So you are taking the A-based staff figure and dividing that into the total expenditure of the department.

Dr Nicoll—That is right, yes.

Mr Barrett—That is on the basis that locally based staff are supporting or providing the support for A-based staff. There is not a one for one translation necessarily, as most of the people in this room would know. I think that is another issue that really needs to be examined.

The fact is that, from the point of view of internal controls and ensuring that government policies are followed, et cetera, the extent to which both DFAT and Austrade are talking about the kinds of systems may allow better translation between locally engaged staff and A-based staff—and thus lower the cost which, as has been suggested by DFAT, might be the way to go.

But at the moment there are a certain number of staff who are deemed to be important to be A-based staff. In this total cost of representation, that basis is reflected in the figure that has been provided.

Mr GRIFFIN—I think I have a handle on that now. I wonder the worth of such a comparison in terms of the operation of a post. Unless what it actually represented was very clearly understood, the danger is there that it could be seen as a very misleading statistic in terms of working out effective utilisation of resources. Further, it could lead to situations in which, going by that stat, a department was looking quite effective when, in fact, in real costs in terms of locally based staff it was an entirely different picture. I just mention that in passing.

Dr Nicoll—We would agree with that. In fact, the caveats we place around the figures in the relevant chapter very much say that. What we were trying to do was add to the marginal cost figure, which is often talked about, and pull out the average cost figure. There are other indicators as well. But at present there is so little information which comes out about the costs of our overseas representation that this was one small step in putting out a little bit more. There are other ways in which this can be put.

Mr GRIFFIN—I understand that. Just to draw, I suppose, an analogy with my colleagues, there was some recent reporting on how much politicians cost. Very bizarre accounting practices were used in that case—misleading. Sometimes people, members of the press or some private sector organisations will take those sorts of things, latch on to a figure and run with it. When you go to the detail it may in fact mean something different. That can be quite irritating and misleading in the circumstances. But I take your point.

Mr BEDDALL—I have just a query. When you go through the list of your small to medium agencies, there is a rationale that you would have to look through. The one that intrigues me—and on which perhaps you can provide me with some details at a later date—is the very large number of staff we have in Islamabad. There are 72 staff in total: 15 Australian engaged staff and 57 locally engaged staff. I just wonder, in terms of a trade portfolio there, or whatever, why we would possibly have 72 staff in total in Islamabad. Perhaps I could get some information on that.

Mr Jones—We can give you that information. It is a post that has quite a few non-DFAT agencies represented; Defence and AFP are there. Also I think you will find that the locally engaged staff component includes quite a large number of very low cost locally engaged staff with static security duties, and so on. The salary factor is something one always needs to look at in assessing locally engaged staff. Their costs are very different according to location, and also the effectiveness varies widely too.

Mr GRIFFIN—There would be quite a large Immigration and Multicultural Affairs presence there too, wouldn't there?

Mr Jones—Yes.

CHAIR—Would anyone like to make a brief concluding comment?

Mr Jones—Thank you for this discussion, which we found very useful and interesting. I thank the ANAO for the report, which was helpful to us. We look forward to keeping in touch with the committee.

Mr Langhorne—Thank you, Mr Chairman. Again, we found the process useful. We will be participating with the department in follow-up with the ANAO.

[10.52 a.m.]

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Audit Report No. 27 of 1995-96, Asset Management

CHAIR—We welcome officers from Finance and Administrative Services. We now come to the second report for today's public hearing. Again, we will run this hearing as a round table format.

I must ask participants to observe strictly a number of procedural rules. First, only members of the committee can put questions to witnesses if this hearing is to constitute a formal proceeding of the parliament and to attract parliamentary privilege. If other participants wish to raise issues for discussion, I would ask them to direct their comments to the committee and I will decide if the committee wishes to pursue the matter. It will not be possible for participants to respond directly to each other.

Secondly, to assist *Hansard* witnesses should identify themselves whenever they wish to make a comment. Thirdly, given the length of the program, statements and comments by witnesses should be kept as brief and succinct as possible.

Audit report No. 27 is the first financial control and administration audit, and it raises some serious concerns about asset management by Commonwealth agencies. I would like to provide an opportunity at the outset of the hearing for brief opening statements. First, would the Auditor-General like to make an opening statement about the significance of this audit?

Mr Barrett—Thanks, Mr Chair. We appreciate again the opportunity to talk about this particular report, report No. 27, on asset management. I consider this report, which does set a benchmark for future audits of financial control and administration, to have been very successful. The reason I say it has been very successful is that there has been general agreement that it was the right product at the right time. It established a very cooperative framework from all the agencies concerned for which we would like to register our thanks.

As you would know from our brief to the JCPA last August on the introduction of this particular product, the financial control and administration audits are concerned with improving the quality of public administration by assisting and encouraging agencies to achieve better practices. They are intended to assist managers in the public sector with meeting their responsibilities and will inform parliament about aspects of financial control and public administration which fall outside the boundaries of financial statement and performance audit products.

The main output at the end of an FCA audit is the publication of a report, the report to parliament and an *Asset Management—Better Practice Guide*. That was the intent, as we indicated to the JCPA last year. The approach provides a benchmark against which government agencies service wide will be able to compare their respective performances and to implement improvements, if considered necessary. FCA audits are undertaken across a selection of agencies. The number of agencies will vary but it is generally between 15 and 20. It was a little higher on this occasion, but that is broadly the number we would be aiming to cover.

What we have done, as we have indicated to the JCPA, is to adopt a whole of government view. The reporting therefore is generic in nature, so we have not included the names of particular agencies involved unless in particular areas they represented best practice. By indicating that they were engaged in best practice, that gave other agencies the opportunity to contact them and to indicate the nature of the approaches that they had taken.

In short, we concluded that the sound principles of asset management dealing with strategic planning, acquisition, operation and disposal need to be applied in most agencies to improve performance and, even where they are applied, they can be significantly improved. In relation to management control and monitoring of assets, agencies have generally developed basic asset policies and procedures and implemented adequate asset accounting systems. However, the most significant progress observed to date has been made as a result of the adoption of accrual reporting in the annual financial statements by 1994-95.

I would stress again that there may be variations in the approaches that we take to these particular types of audits. In this case, we have produced an operational handbook that may not be practical or necessary in more specific audits. In this case, I think it was a major output of this particular audit and one that we hope will be of value to the agencies, not only the ones that were covered within the audit but the 400-odd agencies outside. On that basis, I mention that Colin McPherson and Andrew Greaves, who are at the table, were two of the major participants, from our point of view. Bill Nelson and Edward Hay have got overriding responsibility for these types of audits.

Mr Bowen—At the outset, we in Finance would like to applaud our colleagues in the audit office for the initiative they have taken in proceeding with this series of financial control and administration audits. We believe that these audits will significantly boost the ability of agencies to continuously improve their management practices in a range of areas. The best practice guide and asset management handbook that the audit office has produced will be, in our view, very useful to agencies in reviewing their asset management practices, updating their procedures manuals and their management information systems, as they come to do that.

The audit report notes that the Commonwealth, unlike the states, has not promulgated a central policy on asset management. Understandably, the management of physical assets is a very high priority in the states because of their responsibility for extensive physical infrastructure. In the Commonwealth's case, some 70 per cent of the Commonwealth's annual budget is in the area of grants and transfer payments—many of which go to the states—rather than in the form of direct expenditure on assets. Nonetheless, asset management is important to the Commonwealth and we agree with the Auditor-General that the principles in the ANAO report, the best practice guide and the asset management handbook will provide a good basis for strategic guidance to agencies.

We accept that in addition to our role in Finance for the financial management framework setting, we have an educational role at the strategic level. Equally, however, agencies have responsibility for the day-to-day management of their resources, including for the management of their assets. Agencies are responsible for ensuring that they have appropriate procedures, undertake proper investment analysis, have adequately trained and professional staff and appropriate management information systems. The proposed FMA legislation, which we are very confident about proceeding with shortly, will make explicit the responsibility of chief executives for the efficient, effective and ethical management of their resources. I am not telling you anything when I say that, Mr Chairman, I am sure.

Devolution of management decision making and the running cost arrangements have required agencies to focus more on the management of their total resources with the exception of major capital items, which are not included in the running costs arrangements. I think we could argue about how effective the running costs arrangements have been, but I do not think there would be any disputing the fact that they have been a major step forward in the direction of better management of total resources.

Major capital items are treated separately from running costs at this stage. However, new policy proposals involving asset acquisitions are subject to Finance scrutiny in the usual budget process. Information technology proposals which, for most departments, account for more than 50 per cent of their asset bases, are subject to rigorous acquisition council processes and cost-benefit analysis based on life cycle costings. Provision is also made in the running costs arrangements for long-term resource agreements between departments and Finance to cover major asset acquisition and replacements. I think it is fair to say that these arrangements have not been widely used to date, but we do have some recent examples, such as the Customs' recent 16-year resource agreement covering the acquisition and replacement of its marine fleet.

Finally, if the government decides to move beyond annual accrual reporting—which I think it is generally recognised has had a beneficial effect, even though it has been in place for only a fairly short time—and adopt a full accrual budgeting, accounting and reporting framework, this would place increased focus on the need for agencies to manage the performance of their total assets. That is one of the important thrusts of the audit report. This is particularly so, I believe, if such a framework were to include the setting of explicit financial performance targets for agencies at the departmental or program level. In fact, the adoption of such a framework would permit the setting of those targets on a systematic basis, which is quite difficult to do under the current arrangements.

Further initiatives to improve the strategic management of asset performance, such as the possible implementation of a capital use charge, which is canvassed in the audit report, should in our view be considered within the context of any initiatives the government takes to place its financial management framework on a more businesslike footing.

Mr Palywoda—The Department of Administrative Services supports the thrust and finding of the Australian National Audit Office report on asset management and believes that the best practice guide and asset management handbook will be valuable tools for departments and agencies in long-term strategic asset management. DAS, through its policy roles in procurement in public works and its expertise in the practical application of property related asset management, can and does play a role in developing and implementing strategic asset management principles.

In the Commonwealth procurement guidelines referenced in the ANAO report, which are about to be re-issued, buyers are asked to take whole of life considerations in assessing purchasing decisions and determining value for money. Value for money encompasses a range of considerations, not the lowest price, as the capital cost of many up-front acquisitions can be in part less significant than the total cost of operating an asset.

DAS represents the Commonwealth in the National Public Works Council and participated in the formulation of a set of principles of total asset management in 1993. These principles are consistent with the views expressed in the audit report and have been incorporated in the frameworks adopted by most state governments. DAS business units have been using these principles in developing strategies for their customers in the use of asset management.

Mr GRIFFIN—I have a question for the Auditor-General for a start. The report talks about the need for provision of central guidance on the application of asset management principles. Whom would you see taking that role? How much further should that role go than where it has gone so far?

Mr Barrett—Traditionally, and I cannot see any reason to depart from this, from a financial management point of view it has been the Department of Finance. We would stress that, while obviously our friends in the Department of Administrative Services have a lot of practical hands-on experience in terms of asset management principles and purchasing assets and the like, the framework has been developed by the Department of Finance.

When you look at the whole issue Mr Bowen referred to concerning the likely move to accrual accounting and managing and budgeting in the accrual format, I would think that—certainly as they would in concert with related departments—they would at least discuss the general approach to be taken by the Commonwealth as a whole. I would think the Department of Finance would be the appropriate department to coordinate, given the broad financial resource management framework that it is responsible for.

Clearly, if there are any other factors that can be gleaned from this audit, we could input into those guidelines and certainly we would be happy to do so. On the specific issue of the guidelines, I ask Colin McPherson if he has any comments about what specific areas we might want to see from the point of view of general guidance.

Mr McPherson—As we said in the audit, there is a need for some central prescription to guide agencies at the highest level with the strategies that are inherent or should be inherent in their asset management. The Auditor-General has said that probably resides in Finance, and I would agree with that. From our audit and the way we looked at what agencies are doing, there is a need for a central prescription that comes down from government through Finance, or whomever, to guide agencies in the broadest way in the strategies that need to be applied in asset acquisition, asset maintenance and asset disposal.

Mr Barrett—I will just add to that, Mr Griffin. Clearly, it is a question of who would take that forward to cabinet if they wanted to get government endorsement. It seems to me that the Minister for Finance would be responsible for the relevant legislation and, therefore, I would have thought that it would be the Minister for Finance who would take it. Therefore, it follows that the Department of Finance as the adviser would in fact be the proponent.

Mr GRIFFIN—Given what Finance said earlier, Mr Bowen, with respect to developments you saw as probably occurring down the track, would you like to make some further comments on those issues in relation to what has been said by the Auditor-General?

Mr Bowen—I guess the first comment I would make is to agree with our audit colleagues that I think the executive responsibility for providing high level strategic policy level guidance does rest with Finance. It always has. Finance, while not necessarily going as far as some people might wish, has provided such guidance in the past through Finance directions, circulars and things of that nature with the backing of the financial management legislation.

Over recent years there has been a deliberate push to devolve more and more responsibility to agencies. That has not been simply to take the workload off Finance but to place a greater degree of responsibility and accountability on the managers, who actually have the resources within their control, to manage them efficiently and effectively. I do not see anything that has been said today or in the audit report which would change that, neither do I think it should.

Just to follow that line a little further, the proposed financial management and accountability legislation is currently drafted on the basis that it will be less prescriptive in many areas than the current Audit Act. That, again, is consistent with ensuring that agencies work within broad guidance but actually take responsibility for the detailed day-to-day management of what they have within their control. I do not think we want to change that. Nonetheless, I think the sort of guidance that has been provided here, particularly in this *Asset Management Handbook*, is excellent at a very high level. I am sure it would be of tremendous use to agencies when they come to sit down and work out in detail what they need to do within their own agencies.

Mr GRIFFIN—That is an interesting point that Mr Bowen has raised in relation to the financial management and accountability legislation. Can I get a comment from the Auditor-General regarding that? The suggestion, as I take it, from ANAO is that there needs to be a greater role than has been the case for Finance in terms of directing and providing advice with respect to asset management. Mr Bowen is saying that the actual act that is coming down is principally making a situation where agencies will have responsibility in themselves. We have two competing principles, if you like, there: the question of agencies being responsible for their own expenditure, which we probably all support, versus the question of ensuring that information, best practice and directives make it down the line. Can I get a comment on that?

Mr Barrett—I do not think there is a contradiction there, Mr Griffin. I think what is being said, as I was trying to connote with the notion of resource management framework, is that while there is an essential element of that framework—and certainly from the mid-1980s there has been a devolution of authority to agencies to manage—the fact is that we are still the Commonwealth of Australia and we still need to have consistency in approaches, particularly when we are talking now of whole of government reporting. One of the areas where there is a problem of consistency is, of course, in asset valuations.

But if you go beyond that and look at things like life cycle costing and aspects of charging, which is really a policy issue for the government but is endemic in the nature of the way in which countries such as New Zealand have moved when they have gone for accrual based systems, these are not issues that individual agencies can take their decisions on. They need a framework. My colleagues might want to embellish on that.

Mr BEDDALL—It seems to me that there is a contradiction in the principle in the application, particularly with the Department of Finance. The Department of Finance has a role that is twofold: one is to make sure that it brings in the lowest possible budget deficit and the other is managing. Quite often that will lead to a situation where I think bad practices are adopted. Purchases are made of government assets and they are done basically on a time payment basis rather than purchasing the assets because the capital cost would add to that year's budget.

Without a full accrual accounting system, that pushes us not to best practice but to worst practice. I have practical examples where I have seen vast amounts of money wasted because what you are doing is paying for an asset on a recurrent basis rather than purchasing the asset and being able to write that off over a period of time. So there is a contradiction there with the Department of Finance taking its role as the manager and also its role in the ERC process where it has to crunch ministers on a blow by blow basis so that they do not spend too much to push the budget up.

Mr Bowen—Could I just comment on that? I think there is some truth in what you are saying. At times there can be a conflict between living within a financial envelope or a fiscal envelope and the most efficient practice. However, I think I phrased my reference to adoption of an accrual framework in terms of putting the government's accounting and management on a more businesslike footing. That is not to say that we will not have fiscal constraints, but there will be a much greater focus on the right areas of decision making when it comes to asset acquisition, which will have an impact on cash requirements in the government's budget but which would not have an impact on the government's budgetary bottom line under an accrual framework.

Mr BEDDALL—Not under an accrual framework, but we do not have a full accrual framework.

Mr Bowen—We do not have a full accrual framework. The later bits of my comments were really aimed at saying that much of the future reforms would need to be looked at in the context of the adoption of the full accrual framework.

Mr BEDDALL—If you have a look at, say, asset purchase, in many instances it is quite legitimate for a business to lease a product rather than purchase, but it is also very legitimate for it to purchase rather than lease. If you have a bent in the system that makes the decision making process enforced by the circumstance rather than the right business decision then you get the outcome I am talking about.

Mr Barrett—I totally understand the point that Mr Beddall is making. We have looked at the cost—and it is a cost versus cash situation, and accrual accounting is taking us down the cost route. The question is: if we have to report to parliament in accrual terms then these kinds of issues will come out. But the point I want to stress is that even here there needs to be a central direction, for instance, on this issue of taxation treatment.

In the past, you have heard me talk about the fact that if I, as a departmental manager, went out and went into a buy-lease environment, no doubt, on a tax basis, from time to time I could get cheaper lease arrangements. But, in fact, for the Commonwealth it is a Peter and Paul argument. The question is whether the government of the day wishes to indicate to departments that it specifically wants that factor taken into account. That needs to be centrally directed, as far as I am concerned; otherwise managers, particularly at low levels in agencies, will simply look at the two cost figures and say, 'Well, that's cheaper.' But, from a Commonwealth point of view, it may well not be cheaper.

CHAIR—Would DAS like to comment on the agency that is affected?

Mr Palywoda—We would make a couple of observations. The first is that we agree that, in terms of the development of service wide guidelines in the area of asset management, clearly the executive responsibility rests with the Department of Finance. The DAS business units, in fact, operate on a full accrual accounting basis now. Therefore, the true cost of asset acquisitions is an important part of the decision making process. We have internal guidelines which require that, as part of the business planning process, each business has to identify asset acquisitions of $250,000 or more. They cannot unilaterally proceed with the acquisition of any asset of that value or more without executive approval. Before the executive approves any acquisition of that magnitude, it does an independent analysis to satisfy itself that, from a whole of life cost, that makes the best sense.

I am also very conscious of the points the Auditor-General was making that, from a whole of government perspective, certainly when you are dealing with major property acquisitions, the taxation effect on the Commonwealth needs to be factored into those decisions on long-term lease versus construction or buy options. That is because of the tax advantages in the leasing arrangements, which flow back to the private sector owner.

CHAIR—What exactly do you mean by 'executive approval'?

Mr Palywoda—The executive committee in the department, which comprises the secretary and the three deputies, has to consider and endorse all acquisitions over $250,000.

Mr GRIFFIN—Mr Bowen, you mentioned earlier in your initial comments that states have a formal promulgation of asset management principles under law, and we do not in the Commonwealth. You made the point that, given the nature of their asset base, that was understandable to an extent in their circumstances. Can we just talk about that and whether, in fact, that should go ahead on the Commonwealth basis. Does this current legislation that is coming up take care of that, or do things need to go a bit further to do that?

Mr Bowen—I think you understood the basis for my comment, as to why it is of such importance to the states. Having said that, it is important, and I agree with the other comments that have been made around the table—

Mr GRIFFIN—You mentioned the states. I do not know whether you gave a percentage of the state base that is actually—

Mr Bowen—No, I did not.

Mr GRIFFIN—Is it about 30 per cent of the Commonwealth's assets?

Mr Bowen—The figure I gave was that in the Commonwealth's annual budget, depending on how you measure some of these things, more than 70 per cent is taken up in grants and transfer payments; that is, grants to the states, social welfare payments and things of that nature which do not go directly to the formation or replacement or maintenance of assets. On the other hand, the states—and I do not have a percentage—have a very large interest in the physical infrastructure of roads, hospitals, schools and things of that nature.

Just looking at it, I think that is why, historically, the states have given that a much higher priority than perhaps we have here in the Commonwealth. That is not to say that we should not be doing more. I guess what I am saying, and I agree with the other speakers, is that Finance does have the responsibility for providing central whole of government level strategic guidance, if I can call it that. In my view, it is important that that guidance on asset management be considered in the context of the overall financial management framework. That was the other point I was trying to make.

I think we have to be careful. A report like this is extremely useful to highlight deficiencies, including central guidance at the operating level, the agency level. It is very constructive in its suggestions. It is even more than a suggestion because it has actually produced some guidance, which is very concrete. Having said that, I think we have to be careful that we do not tackle these things on an ad hoc basis and that we do, in fact, look at our overall financial management as a package, as a total framework.

I believe the sorts of issues that Mr Beddall raised are extremely important for the future of the Commonwealth's financial management. If you read carefully the report that the audit office have done, they have focused on the non-commercial elements of the Commonwealth and how they manage assets. The question is: why have they done that? They have done it because the incentives are in the system for the commercial people not to have to worry so much about them. They do have the incentives. They do account on a full accrual basis. They have to take account of their full resource costs when they make their business decisions.

I think that, if we can place the Commonwealth's financial framework on a businesslike basis, decisions will be taken in a similar way. We may still need some guidance on specific aspects of whole of government approaches but I believe that, if there is a greater focus on total resource use by departments, much better asset management will result.

Mr GRIFFIN—On that question of formal promulgation of asset management principles, a la the states, do you see that as being something we should do, we should not do or is it something else?

Mr Bowen—The simple answer is yes, we should do it. I guess I am saying that that is one of our priorities. We would expect that that would be done within the implementation of a new financial management framework or an enhanced financial management framework.

Mr GRIFFIN—The report talks about the fact that most agencies—it is a generalisation—are not managing assets rigorously. Does this suggest that the financial management improvement program has failed in the area of promoting good asset management or does it lead to the question of what else should be done and when should it be done?

CHAIR—And will the FMA Bill when enacted be the answer?

Mr Barrett—Like all programs, they are not meant to wrought miracles. There was a very large campaign run by Finance in the late 1980s on asset management all around Australia, including the ACT. It is not as if there has not been an awareness raising exercise for managers. But it will not happen until managers really have to think about what they are doing. What accrual reporting has done, at least to start off with, is to make managers start to realise that they have these assets that they have to account for in some way.

While I am focusing on the future, quite clearly any move towards full accrual accounting and accrual budgeting will focus that even more. That is going to be the catalyst in my view to managers really starting to address questions. They will start to ask questions, for instance: 'Is the fit-out of a building current expenditure? Should it be capitalised? Under what circumstances should it be capitalised?' It is the same with our computing equipment, 'Do we capitalise our software? Do we take it as a current cost?'

Those are the issues on which I believe some sort of central guidance is necessary so that we are all reasonably consistent in our approaches because at the end of the day, as we said to you before, particularly in whole of government reporting, we do not want to be adding up apples and oranges. It would simply be misleading.

It is misleading even within agencies that are trying to take a whole portfolio approach where they have got several bodies within the agencies—entities, we might call them. Even a minister looking from a portfolio point of view wants to be assured that there is reasonable consistency within the portfolio so that, when figures are being put forward in the budget context, they mean what they say they mean. So that is a concern in a very practical sense.

The premium in the past has been only for the individual managers in so far as they have been switched on, if you like, forward thinking and really thinking about these issues. But the system in itself has not demanded it. Under FMIP the system has raised awareness and said, 'You should be looking at these issues as a matter of course.' But the system did not require it at the end of the day.

What I suggesting to you is that, with a move to accrual accounting, accrual budgeting, then the system will be requiring this. Once the system requires it, then you will need some central guidance. That is one of the reasons why we are pressing for central guidance. In this sort of environment agencies will come forward and ask, ‘What do I do in these particular circumstances?’ We do not want them reinventing the wheel. We do not want them going out and doing their own thing.

We will have enough problems if we do go into whole of government reporting from an audit point of view to come out and make some sensible audit comments on it, let alone from our FSAs where we find these differences of treatment and we bring those to attention. They are all going to be magnified at the end of the day once we start getting into the aggregation consolidation processes.

I do not see it necessarily as a failure. I would have to say in the case of the audit office ‘Mea culpa’ because we still do not have a costing system where we can put our hand over our heart and say, ‘Yes, we are consciously taking into account the full cost as we know it of providing audits.’ We try to do that as best we can, but like a lot of other agencies we do not have the systems in place to be confident about it. So the onus is on us to do something about that, the same as it is on every other agency.

When you look at this report, we are generally saying, ‘Yes, their practices are on average not bad but, given where we are going and the focus that is going to be on total resource cost, we need to do better.’ One element of that is obviously going to be in the systems area again, which has to be addressed, and that is going to cost some money.

CHAIR—Do you want to put that into a time frame?

Mr Barrett—It depends. In terms of the statements that have been made so far in the information technology arena, which have suggested that there will be more use of bureau type operations, particularly for smaller agencies, whether they will be within the Public Service or outside the Public Service remains to be seen. So in essence it really depends, particularly for small to medium sized agencies, as to what time frame that will take to put it in place.

If we are going to be using more centrally provided bureau services and if we are ‘the masters of our own destiny’, it would really depend on resource availability. You would have already heard—and there is much comment in the newspapers—about the tough budgetary situation in the medium term. Therefore, I do not think departments are going to be well placed if they do not get supplementation to be going into these kinds of systems.

In our own particular case for the information of this committee, we have made provision. We have put aside money in the flexible budget situation that has been provided under running costs. Either we will have the facility to put in a system ourselves or we will have at least the ability to be able to go into a bureau based system in probably 12 or 18 months. I say fairly confidently in 12 to 18 months. At the end of the day some very large departments will need some quite significant requirements—

CHAIR—Such as Defence?

Mr Barrett—Social Security, for instance. They have quite a significant system. I do not know where they are at—unless one of my colleagues knows—with their present replacement. In essence, no-one is going to go out in the second or third year of a system and say, 'We're going to replace that overnight,' if they have a five-year depreciation plan in front of them. They will do their costs and their sums and at the end of the day they will say, 'Yes, we'll do our planning and we'll move when the costs and the benefits are better aligned.' For them, it may be two or three years down the track. There will be a bit of horses for courses here, but I think, firstly, it will need a series of government decisions that bear directly on these issues, as I have indicated, and then, as always, it will depend on the resources available in individual agencies concerned.

If we are required to go on to accrual accounting and budgeting on that basis within, say, a medium-term framework, obviously that will be the decision for the government to take, because you cannot have one without the other.

Mr Bowen—Could I comment briefly on Mr Barrett's very comprehensive answer.

CHAIR—I have read those newspaper reports, too.

Mr Bowen—I will not comment on his hint about supplementation. I think there is a recognition, certainly within Finance, and I assume within government as well—

Mr GRIFFIN—You do not sound confident, Mr Bowen.

Mr Bowen—I am not talking supplementation here; I am talking about a need for a phased approach to the implementation of a new financial management framework. The question as to how quickly you can do that does, in large measure, rest on how quickly agencies can gear up. It also rests on how quickly we in Finance can gear up. We also have central accounting system requirements. Currently our central accounting system is a cash based system. It is an extremely good cash based system, I would have to say, and one which has served us and various governments very well over the years. If we are to move to a full accrual budgeting accounting and reporting framework, then we too have to gear up our internal systems and procedures.

Also, all sorts of educational issues arise within Finance with people who currently do what we call the supply work in dealing with agencies on their budgets. There is a very important educational role that we see ourselves having in the way that agencies manage their finances and interface with us. There is probably some educational work to be done at the cabinet level in how we interact in the ERC processes with an additional set of financial information. So there is some lead time.

CHAIR—Does DAS have a comment?

Mr Palywoda—We would agree that the introduction of accrual accounting is something that you cannot do overnight. Leaving alone the systems issues, there are very substantial training and development issues and recasting the culture of an organisation away from a cash based mentality to one where you are looking at the full costs over the life cycle. Our experience in moving all our businesses onto an accrual accounting system invariably means that you are looking at two financial years to put in, bed down and be confident that you are on top of the system issues, as well as the people issues involved.

Mr BEDDALL—I agree it takes some time, but if you do not set a target or an implementation date it could take forever and the agencies which you most want to do it will be the last to do it, unless they are forced. DAS has said a two-year time frame—maybe even a little more generous—but if we had to have a cut-off time to move the whole of the Commonwealth towards that would it be two or three years?

Mr Barrett—As you would appreciate, that is a policy issue, but I talk about it in terms of administrative effectiveness. I think what you say from an administrative effectiveness point of view is apt. What it points up to me is that, when you look up the handbook and you see some agencies are setting a recording threshold on the assets which are valued over a certain amount and are recorded in registers of the agency, you look at the ABS that has a system that they have had in place for some time, the user charger regime for IT equipment and support services. You have the National Library which has adopted an approach for their utilisation and functionality of their photocopies. The Attorney-General’s Department has developed a system which records electronically the IT equipment attached as an automatic asset location and verification, et cetera.

It is these kinds of initiatives that are taking place. It seems to us that, when looking at better practices, if you are looking for central guidance and systems that are now going to be based on this better practice, you need to have that central guidance out sooner rather than later because that is going to impact on the kind of systems that people are going to put in place. If you are going to have a time frame of the type that you have indicated, I think it is as the government of the day decided on accrual reporting. There is no question that, if we had not set a timetable on accrual reporting, agencies would have strong arguments as to why they could not have gone onto accrual reporting. The agencies need to ensure that their ministers have appropriate information on the costs and benefits to them and put that up in the decision making process when it is put forward. Hopefully, that will determine the best time period. As I said, for a planning period I think probably three years is fair enough.

The only comment I would make is, as usual, that it is for large agencies with large systems. If they have just, for instance, put in a new system, you can scarcely ask them. If it is a three-year timetable, the depreciation schedule and the cost benefit of moving them in that time frame might be okay. But it is a very big upheaval.

The DAS experience is really what the rest of us in the Public Service should be looking at—DAS having gone through all the teething problems—not necessarily that that was the appropriate timetable, but to see what issues they had to face and what we would have to do in a similar situation, even though we have had that learning period and the systems are perhaps far better today than they were when DAS started on the move. If all those in that potpourri of factors boil down, it is essential for all agencies to have a sensible time frame that reflects the cost and benefits.

It may well be that some ought to move more quickly. But the only way that that can happen is if there is appropriate central guidance, so that, if we happen to move in the next 12 months, we do not have to change in three years time because the rest of the people have learned other things and they are going to change. We do not want that latter imposed cost. That happens so often to people who have made innovations and get very frustrated because the rules of the game suddenly change on them later.

None of us are going to argue that life stands still and that changes will not impact which we will have to input into our systems, if not cost effectively in the life of those systems, certainly in the next replacement phase. That is just something that we need to bear in mind. It is the old stitch in time problem.

CHAIR—It must be a conscious decision of government to drive this.

Mr Nelson—Yes.

Mr Barrett—Yes.

Mr Bowen—Yes.

Mr BEDDALL—The life cycle costing of assets has been referred to a little bit today already. Is it an appropriate way to go for all government agencies? Is it something that we should be able to implement on a widespread basis in the near future? What does Finance have to do to get that up and running? Is it a desirable option?

Mr Bowen—There is no doubt that decisions about asset management should be based on a life cycle approach. While this may not happen in every case, it certainly does happen in many cases. I quoted the instance of major IT acquisitions which are subject to a specific process called the acquisition council process. Finance is involved in that as is the agency that is putting up the proposal. My understanding is that those proposals are put through a rigorous cost-benefit analysis at the point of acquisition where the total life cycle costs should be included.

It is also fair to say though that possibly some of Mr Beddall's budgetary expedience applies in the case of some assets in the running cost system which may not be subject to quite the same level of rigour when decisions are being made about them. While guidance is important, guidance within a framework which provides the encouragement and incentives is even more important. We want to be very careful we do not just pick off the question of guidance as opposed to an accrual framework, et cetera.

We certainly see Finance having a very central role when the government takes a decision to go down this path, if in fact that is what it does. There does have to be an explicit government decision. We would see ourselves as having a very central role in implementation of that framework and, as part of that, having a high profile at a strategic level in the education process. That includes the setting of specific guidance on a lot of the issues that have been talked about today.

Mr Barrett—Mr Chairman, I have just had a quiet conversation with Mr Nelson here. We both agreed that it is probably down to a small agency/large agency situation. I would not necessarily expect small agencies to have either the value of the assets or the infrastructure and the resources. In a cost-benefit sense, they probably would not go into doing this kind of analysis.

Certainly, Administrative Services and Defence, for instance, would be the ones we would expect to have quite sophisticated life cycle evaluations done, including both the planning and disposal areas. Unfortunately, basically because we have not had to concentrate on better asset management, those are two areas where we in the Commonwealth probably have not given sufficient attention in the past. That is the planning phase, the cost of the planning phase, and the disposal action and making sure we get the best value that we can in a competitive environment, taking these decisions into account, particularly when we are looking at the asset lives and their contribution. We found a number of assets in books that had been written off. That has been a common factor and nothing has been really done about that, in the sense of what was management's view that they had all these assets that were written off.

Mr McPherson—Through the audit we did find a surprising number of cases where agencies were still carrying in their asset registers assets recorded at nil value but still in use. This raises the question: is the cost of the asset really being reflected in the program costs? If the asset has already been depreciated to nil value and is still in use, there is still a cost to the program that is not being shown correctly.

It was indicative of a problem we saw in the audit. We think greater consideration of asset management needs to be imported down to program level. It should not be at corporate level. Corporate would certainly have asset policies and strategies, but they need to be pushed down to program level in agencies. I think that was the very reason we saw a lot of nil value assets sitting on the books of agencies, still being used and of service.

CHAIR—That leads us into the principle of asset cost attribution to program levels. Does Finance support that? If so, how could asset cost attribution to program levels be implemented as a general accounting policy for government?

Mr Bowen—If we are serious about measuring the efficiency with which we deliver programs, then the full costs associated with program delivery need to be allocated to those programs. One large area in most departments which currently is not allocated to program in a management and reporting sense is the corporate services area. This can involve quite large lumps of cost—recurrent and asset cost—which really comes back to a fundamental question of how you design your program structures. If we are going to allocate costs to demonstrate how efficiently and effectively we deliver government programs, we have to first of all work out exactly what it is that we want to measure and what we want to allocate. Having done that, we need to have systems which enable us to do it on a systematic basis.

One of the reasons Finance, in specifying guidelines for reporting by agencies—they are promulgated by the Minister for Finance—has not pushed as hard as it otherwise might the idea of allocating costs to program is that there has been a recognition that many agencies do not have the systems in place at this stage to enable them to do it on a regular, systematic basis. Certainly, most modern accounting systems, if they are implemented properly, can permit you to allocate your costs on a number of different bases, one of which certainly could be to program.

Mr BEDDALL—Zero assets in a registry is one of the problems you have got if you do go to a full accrual accounting system because depreciation rates for assets are often set by a political process rather than a process of the life cycle of an asset. When we get into accelerated depreciations, et cetera, we do end up with lots of assets that technically have no value but have a very large value if you wish to resell them. It is one of the issues you have to address. Sometimes in the private sector that is redressed by re-evaluation of that asset. Something like a Caterpillar D10 bulldozer probably is always worth more than it was ever purchased for, but it depreciates over time rather quickly in times of accelerated depreciation. How do you address those issues with an asset that in a depreciation schedule, even over 10 years, will be depreciated but will always have a life cycle?

Mr Barrett—I would look at that on a life cycle basis and bring it back into the books at a reasonable value. The difference between the public and private sectors, at least for those non-taxpaying agencies, is that we do not pay tax. As you know better than I do, in a lot of these areas it is driven by the taxation advantages that apply. I would hope that our managers, when we are looking particularly at that and discussing this particularly with their ministers and looking at appropriate lives for such assets, would look at what is really the life and the value. If we have taken a conservative point of view to start off with, then I think managers need to consciously look at those assets again and decide what is their value in use.

That comes back to this concept of deprival value, which has been pushed. There has been a lot of criticism about that particular process, but it seems to me that in a public sector model the issue of deprival has a very good in-principle approach because it really does force the manager to say, 'If I did not have this asset, what would I require?' That really is the value to them in that particular program. That really is the discipline in the process that should be exemplified.

I will take this opportunity to raise another point in relation to this issue of disposal. In the handbook we make the point about the DAS guidelines, discussing primary methods of disposal between sale by public auction, tender, sale by private trader, trade-in and write off. However, there is one in relation to this issue of central guidance that has often bemused me a little from the outside looking in, in a sense. That is the absence of some mechanism by which departments and agencies can notify generally, on some kind of bulletin board, that they have assets for sale or assets to be disposed of.

There are a lot of assets in common use across the Commonwealth and one agency might well be in a situation of dearly loving to have those assets rather than having to simply go into the easy way of disposal, saying, 'There is a disposal arrangement out there and we simply get our friendly private sector entrepreneur coming in to dispose of it and that is the end of it.' The opportunity cost from the Commonwealth's point of view could be quite significant in terms of the value and use to the Commonwealth of such assets.

The issue may simply be the cost of maintaining it. In these days of electronic advantages, some bulletin board where agencies can indicate the nature of the disposal of their assets, and have those notified to other potentially interested agencies, does not seem to me to be such a bad idea.

Mr BEDDALL—Mr Barrett, maybe you could notify the relevant state agencies who may wish to purchase Commonwealth assets.

Mr Nelson—In terms of accelerated depreciation and the value of assets, accrual reporting and accounting standards now apply whereby each year each agency must address service life and value and depreciation when preparing their financial statements. In terms of having accelerated depreciation rates and, therefore, assets coming down to nil value, it is less likely to occur now with the move to accrual accounting and application of accounting standards. That does not mean that you will always get it right, because at the end of the day you are making qualitative judgments about service life, which is not easy. But accrual accounting and the application of accounting standards is moving everyone in the right direction in terms of the reporting of those numbers.

Mr Bowen—I wish to support Mr Nelson's comment. We are now seeing quite a significant difference within the Commonwealth. No longer are we simply making our own rules. We still have the right to make some of our own rules, but more and more we are doing our accounting and reporting on the basis of accepted professional standards. I am not suggesting that there is no need for our own internal guidance, but we do have a body of accounting standards which is continually being kept up to date and which professional accountants working within the Commonwealth are required to comply with. Generally speaking, I think I am right in saying that the minister's guidelines on reporting require agencies to comply with Australian accounting standards. So it is a very important point.

CHAIR—One complaint we often get from the private sector is in the area of competitive tendering—when the government and agencies tender against private enterprise. I suppose accrual accounting will require government agencies to go in and tender at a true cost. Would you like to comment on that?

Mr Palywoda—When tendering for that work DAS businesses do tender on the basis of their full accrued costs. They have been operating on accrual accounting for some time now. That full accrued cost, certainly for non-government work, includes bringing to account the tax equivalents that they would have to pay.

CHAIR—I hope you encourage local government to do the same thing. In its report No. 341 on financial reporting, dated November 1995, this committee recommended that the Department of Finance and the ANAO should develop an asset valuation framework to ensure that Commonwealth agencies have consistent asset recognition and valuation policies. Has any work been done on standardising asset valuation for Commonwealth agencies?

Mr Bowen—Under the accounting standards there is no requirement on agencies, or commercial entities for that matter, to revalue their assets at any particular point in time. There are requirements that once having done so they must revalue all assets in a class within a particular period of time. Some of the states have certainly gone beyond that point. The departments and entities within their control have specified particular valuation regimes. That has not been done in the Commonwealth, except that we have no more than encouragement—George, you might be able to comment in more detail—for agencies to adopt the deprival value approach to valuation of their assets. That does not of itself overcome the problem of different agencies being at different points in time with their valuations. That is something that we still have to address.

Mr Carter—There is probably not much that I can add, except that the deprival methodology was developed by the Commonwealth and states over a period of time for the purpose of government trading enterprises. It has also been found to be relevant to departments and budget funded bodies. The guidelines are set out in this red booklet, which has been distributed amongst Commonwealth authorities. Having made that available to them and having presented a large number of seminars to the departments and authorities to explain the methodology, that has now been placed in the minister's financial statement guidelines to encourage departments to use it, but it is not mandatory at this stage.

Mr Palywoda—I wish to plug the services of one of the DAS businesses—the Australian Valuation Office. It has a significant body of expertise not only in relation to property valuation, but certainly asset valuation and plant and equipment and is available to assist departments and agencies in putting in place valuation arrangements.

CHAIR—DAS has published guidelines for surplus asset disposal. What role has DAS had in advising agency managers about asset disposal?

Mr Palywoda—Through Purchasing Australia, we provide a policy framework for the management disposal of assets and that is reflected in the Commonwealth procurement guidelines. But more generally, through both Purchasing Australia and the domestic property group on a consultancy basis, we do provide departments and agencies with assistance in managing their disposal programs, be it property, fixed assets or plant and equipment. That goes through the whole range of looking at the best disposal strategy, the timing, how that should be managed, and agreeing with the department or agency a timetable.

CHAIR—Is that binding on the agencies?

Mr Palywoda—No. The departments and agencies are responsible and accountable for the management of their own assets and make their own decisions. We can provide guidance and help.

CHAIR—Do they have to pay you for that guidance?

Mr Palywoda—The guidance, in terms of the Commonwealth procurement guidelines, is provided as part of our policy role. But in terms of actual consultancy assistance, it is on a fee for service basis.

CHAIR—Finance: incentives provided to agency managers for better asset management. Do you want to comment on what incentives a good asset management is provided with under the running cost arrangements?

Mr Bowen—Just briefly—and Mary Venner may be able to provide more detail, if required—under the running cost arrangements, I guess there are two elements. One is those items which are encompassed within running costs, which include the minor capital items up to, I think it is, $250,000, on the one hand; the other is something I mentioned earlier, which is the ability to enter into resource agreements with agencies on replacement of major capital items.

But in particular, on the minor items, given that this is part of the total resource base which agencies have to manage, there should be incentives in there for them to manage that resource base as efficiently as possible. They do have efficiency dividends payable on their running costs base. So there is an incentive for them to see which elements of their running costs are important to them and which are not.

The system as it currently stands does not provide the same focus for agencies on their total resources that a full accrual budgeting and accounting system would. Under that system, it would be very transparent to agencies and managers just what their total annualised costs were, including the annualised costs of their major capital. That is a lack, at the moment, in the current system. Do you want to add to that, Mary?

Ms Venner—I do not think so. You covered that very well.

Mr GRIFFIN—The House of Representatives Standing Committee on Banking, Finance and Public Administration recommended at the end of 1995 that the limit on 'minor capital' items in running costs be increased from $250,000 to $750,000. Is it proposed to increase the limit for minor capital items; what effect, if any, could this be expected to have on asset management by government agencies; or does the increased limit simply compensate for changes in real costs?

Mr Bowen—I think the issue of, effectively, what goes into bill 2 as opposed to what is covered in running costs is a matter for the government and the parliament to decide. I think there are advantages in having more rather than fewer assets within the running costs base, if you accept the logic that, by having them there, managers will exercise more management control, if you like, over the priorities of what they are dealing with.

Under a full accrual budgeting and accounting system, of course, I am not sure that it is so important where the source of the funding for those assets comes from, whether it is part of running costs or whether it is part of something else, because there will be a very clear shooting home of the costs of those assets into the operating statement of that department. Hence, decisions will be made on the basis of the budgeted operating statement almost irrespective of the source of the funding for the asset concerned.

Mr Barrett—If I can just add to that: I think it is important to do the separation that Mr Bowen has referred to in terms of costing the asset and funding it. What I would not like to have is that, if there is an absence of central guidance, a notion of any increase in minor capital be regarded as current simply because it is minor.

Mr Bowen—No, I agree with that.

Mr Barrett—That would be something I would be concerned about.

Mr Bowen—I agree. I think it is very important to have a clear distinction in the accounts between what is capital and what is recurrent to be able to manage effectively. That is, of course, what a full accrual system would do for you.

Mr GRIFFIN—Audit report 27 raises the question of the need for external mechanisms—incentives or penalties—to encourage performance in asset management, particularly by budget dependent agencies. We understand that the Heads of Treasuries forum is examining the potential for introducing a 'capital charge' for government agencies acquiring assets.

There is a recommendation from this committee in report 338 on accrual accounting: that Finance should consider levying capital charges for the use of public assets. What is your attitude to that now; have you any knowledge of overseas experience in that—particularly, say, in New Zealand; or are there other, perhaps better, mechanisms than the capital charge for making the costs of asset ownership transparent to agencies?

Mr Bowen—That is a fairly wide question. I think there are some attractions, certainly, in the concept of a capital charge in that it does very clearly overcome concerns that in certain circumstances departments may consider their capital as a free good. The capital charge makes it very clear that the capital is not a free good. In terms of overseas experience and what we are doing here currently I may ask Mr Carter to comment. He is a member of the committee of heads of Treasuries which is looking at this issue.

Mr Carter—The Commonwealth, along with the states, is currently looking at options for the capital charge. It is a matter of interest to the states as well. Victoria has introduced a capital charge. None of the other states have yet, but they are considering it. The heads of treasuries requested this committee to provide a number of options. At the moment a paper is being finalised which sets out various ways that the capital charge could operate. At this stage the range of methods that have been provided do not really suit the Commonwealth very well mainly because our financial structure is so different from that of the states.

In New Zealand the capital charge is levied on the net assets or the equity component of the balance sheet. The proposal which is favoured by the Commonwealth-state committee would be based on total assets less interest bearing debt. We would not find that very helpful in the Commonwealth because departments—except for the Treasury—do not borrow, so they do not have interest bearing debt. Departments also have major liabilities for accrued long service leave so their net equity position is generally negative. So a capital charge would not work on that basis. This is not the case in the states. Most of them have positive equity because the way they arrange their finances is different. It is a very complex area, but once these options are settled the Department of Finance, I think, will need to examine which suits the Commonwealth best.

Mr GRIFFIN—You seem to suggest that there may be options being considered which would suit the Commonwealth. Is there a favoured option at the moment or one that is being pursued in discussions?

Mr Carter—If we go to a full accrual accounting framework, the Commonwealth balance sheets will become more like private sector balance sheets, in which case a model like the New Zealand model would probably be sensible, which is a charge on net assets. At the moment our balance sheets are quite unusual in comparison with the private sector. But if departments were funded differently I think we could adopt the New Zealand model.

Mr Barrett—I might make a gratuitous comment. Again this comes down to central guidance because clearly it does very much depend on what arrangements are made for departments and agencies to retain depreciation. In relation to a depreciated asset if it is an unders and overs arrangement and the Commonwealth is prepared to wear that on its budget—and this is the age old problem of conflicts, as Mr Beddall was talking before about; the budget versus devolved management, et cetera—what agencies and obviously what departmental managers want is the certainty of being to able replace assets from the depreciation charge they have. They are prepared to wear a charge to do so, but in essence, as we know in the past, and particularly in the computing area, where you may have bought quite an expensive computer five years ago, today that computer may be able to be purchased for half the cost.

The Department of Finance and maybe the government of the day may not be so generous in that situation as to say, 'Yes, you can retain and replace whatever assets', which in fact only represent 50 per cent of the depreciated cost and which means that the agency would then have that other 50 per cent to do whatever it liked with. It is this kind of issue that we need some indication on from a central point of view in terms of being able to manage in an operational way.

CHAIR—What can Finance do to make sure that agencies are across this asset management in future training programs, or do you leave it up to the agency to provide a private training scheme for their managers?

Mr Bowen—Our view would be that we have a very important educational role at a fairly high, if I can use that term in its proper use, strategic level. I guess that level will vary from time to time. At the point of moving to a phased introduction of a full accrual accounting system of management it might be at a higher plane. I would like to make a distinction between our role as an educator and a framework setter as opposed to a trainer. I do not believe that in this day and age of devolved management Finance should necessarily be getting into the detail of training, which we would see far more as a responsibility of individual departments and managers within departments. It is terribly important that we ensure that they have the right framework, the right guidance, within which to develop and conduct their own training programs.

But being very practical about this, which you have to be with training, I would also question whether Finance is qualified to get into the nitty-gritty of training for some of the aspects of DAS's operation, for instance, or the Department of Defence's operations, which are quite massive. Detailed in-house knowledge is required. It is important that the training which is conducted and resourced by departments for which they are responsible is conducted with the right strategic guidance. That is where our role really lies.

CHAIR—Finally, Mr Kennedy or Mr Bowen, when do you expect the FMA bills to come back to the House?

Mr Bowen—I will ask Mr Kennedy to be accountable for that question.

Mr Kennedy—It is, of course, a matter for government decision. But the expectation within the department—and we do not speak for the government—is that the forthcoming budget sittings will see the reintroduction of the bills.

Mr BEDDALL—Has the government determined priorities for bills yet or is that process still going on?

Mr Kennedy—No.

Mr BEDDALL—It depends where it sits in that list.

Mr Kennedy—Yes, it has a place on that list.

Mr BEDDALL—Every bill has a place on the list.

Mr Kennedy—Since both Mr Griffin and Mr Beddall raised the question of the legislation in a number of contexts, I would say that you cannot ever legislate for good management. We can provide a framework—and we are providing a framework—through the FMA and its subsidiary legislation. That will provide the platform, which is a vast improvement over what we have now under the Audit Act and its subsidiary legislation. But the only way that you are going to be able to change managers' behaviour is by making their performance visible. The accrual accounting and reporting and, ultimately, budgeting framework is what is going to do that. The advances on those fronts will be well accommodated within the legislative framework that the FMA will offer.

CHAIR—Does anybody care to make a concluding remark?

Mr Barrett—Just a quick comment. You might be interested to know that, on the training and awareness front, there are three areas that we will be involved in: a seminar for the Government Accounting Group and the Victorian and ACT branches of the Australian Society of CPAs; a presentation seminar to the Institute of Internal Auditors;

and an asset management workshop at the Australian National Audit Office for representatives of the actual auditees from this particular audit.

As I said to you last year, we intend to follow up, in all our financial statement audits, the timetable and the approaches being taken by individual agencies against our better practice guidelines. From the point of view of the development of audit related services about which I spoke to you earlier this year, we will be seeking to assist, where we can, those agencies to implement these better practices. We certainly will be commenting as to the extent to which they have or have not in the financial statement audits, as we undertook to do to you last year. We would also be contemplating, in the light of the changes that are being contemplated and that may well be implemented in the next 12 months or so, the need for a follow-up of this particular audit in about 18 months or two years time.

CHAIR—Thank you very much. I adjourn the meeting to 1.30 p.m.

Luncheon adjournment

[1.36 p.m.]

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BARRETT, Mr Patrick Joseph, AM, Auditor-General for Australia, Australian National Audit Office, GPO Box 707, Canberra, Australian Capital Territory 2600

BOWDEN, Mr John Arthur, Executive Director, Performance Audit Business Unit, Australian National Audit Office, 19 National Circuit, Barton, Australian Capital Territory 2600

MEERT, Mr John, Group Director, Australian National Audit Office, GPO Box 707, Canberra, Australian Capital Territory

McCAUSLAND, Dr Ian Phillip, Managing Director, Meat Research Corporation, Level 6, 26 College Street, Sydney, New South Wales 2000

MENZ, Mr John Edward, Corporation Secretary, Meat Research Corporation, Level 6, 26 College Street, Sydney, New South Wales 2000

PERRY, Mr Michael Charles Richard, Business Manager, Meat Research Corporation, Level 6, 26 College Street, Sydney, New South Wales 2000

Audit Report No. 21 of 1995-96, The Meat Research Corporation: Management of Project Fututech

CHAIR—I welcome representatives from the Australian National Audit Office and the Meat Research Corporation. We now come to the third report for the day's hearing. We will be running this in a round table format, and I ask participants to observe a number of procedural rules.

First, only members of the committee can put questions to the witnesses if this hearing is to constitute a formal proceeding of the parliament and attract parliamentary privilege. If other participants wish to raise issues for discussion, I ask them to direct their comments to me and the committee will decide if it wishes to pursue the matter further. It will not be possible for participants to directly respond to each other; please do that through the chair.

Second, witnesses should, to assist Hansard, identify themselves whenever they wish to make a comment. Third, given the length of the program and the late arrival of some of the committee members, witnesses should keep their comments as brief and succinct as possible.

The Auditor-General's views, as well as the initial responses of the audited agencies, have been set out in the report. For this reason we are proposing to dispense with lengthy opening addresses. However, I would like to provide an opportunity at the outset of the hearing for the Meat Research Corporation to inform the committee of any action that has already been taken. Dr McCausland, do you want to make a few brief comments?

Dr McCausland—Yes. I would like to make a few brief comments, Mr Chairman. Thank you. I would like to use some of my five minutes to put the Fututech project into context with all the other projects that the Meat Research Corporation does. The Fututech project was clearly very ambitious. It was risky but we would maintain still that it was worth doing. The project actually began with the CSIRO before the Meat Research Corporation began. When the Meat Research Corporation was formed in 1985, the industry requested that we take this project on as a high priority and accelerate it.

You may be aware that meat processing in Australia was then and is now substantially less efficient than our main overseas competitors. This is of great importance to the nation because Australia is, surprising to some, the biggest beef exporter in the world. So we are competing on an open market and half of our production, even more than that, goes overseas yet we have a processing sector which is less efficient than our competitors.

So the project aimed to improve efficiency by semi-automating a whole abattoir. That was important because it was believed that by automating or doing one little bit of an abattoir the efficiency would not be achieved—it needed to be a whole abattoir. This was exactly the sort of project the MRC was set up to do. It was clearly not within the capacity of any Australian processing company to attack this project.

I would like to take you back to 1985 when the industry requested this be taken on as a high priority and with urgency. At that time the MRC had just started. It had 11 board members and five staff, of which one was a technical staff member and all the rest were administrative people—accountants and so on. It made sense at that time that the most important and largest of our projects should be handled by the board direct—that is, managed by the board directly.

With the wisdom of hindsight, it is clear to see that the board should have held the industry back and said, 'We cannot start this thing yet. We need to take on appropriate staff,' because when staff manage a project they have to answer to the board but when the board itself manages a project, or a subsidiary company reports directly to that board, there are no such checks and balances. That is a fundamental issue that I would like to get across with this project.

Very few projects have been managed directly by the MRC board, and certainly none are today. The MRC acknowledges now that this was an inappropriate method of project management and that failures in project management did occur, and they have been shown in the ANAO report. It is significant that in February 1995, before the ANAO started their investigation and shortly after the MRC had itself stopped the project, the MRC board met, decided and resolved that this must never happen again, that all projects must be managed through the managing director and that none would be handled directly by the board ever again.

I should say too that strict project management procedures have long existed for all other MRC projects and a series of written mandatory requirements have been in existence since at least 1991, and that is referred to in the ANAO report at summary point No. 20. Most importantly, the MRC agrees with all of the ANAO recommendations. We have examined them carefully and have put in place for all of them procedures which address all of those recommendations.

Finally, I would just like to say that the Fututech project is not without some merit. Fututech spin-offs—bits of equipment which have come from the major effort that was Fututech, the team that we put together—are now on the market. No fewer than three bits of equipment which have been designed for conventional abattoirs are now on the market, and two of them came on the market only recently and are already selling.

I will not go into details except to say that they are: a bunging machine to stop faecal contamination onto the carcase—which is one of the major causes of food poisoning; so it is very important in today's meat industry—a head meat removal machine and a head transfer machine; and there are further bits of equipment about to come onto the market as well. While it is a matter of record that the major Fututech project was a failure and we stopped it, there are spin-offs that have come from it and are continuing to come.

CHAIR—Mr Barrett, have you any opening remarks?

Mr Barrett—If I could just explain again the reason for the audit, the Fututech project was selected for audit because it was one of the largest projects conducted by any of the rural research and development corporations. The ANAO planned to identify possible improvements based on risk management principles which would assist not only the MRC but also other R&D corporations.

I want to stress the point that this was not an exercise in criticising what has been—and agreed just now to be—a risky project, but there were elements to substantiate why it should have been done. That was not the concern of the audit. The concern of the audit was basically to look at what lessons could be learnt for the future for these kinds of projects. Quite rightly, the emphasis was on project management and the use of risk management principles, which have received a lot of attention, as you know, in the last year or so.

The objective of the audit was to examine the efficiency and effectiveness of the management of the Fututech project, including MRC's decision to develop a commercial prototype, the tendering procedures employed, the contracts negotiated during the project and the project management of Fututech. As has been agreed, there were areas where in hindsight—and I agree with that—management practices could have been improved in relation to decision making processes, contractual and tendering arrangements and project management. As you have also heard, the Meat Research Corporation has agreed with all 10 recommendations and is now in the process of implementing them.

I point again to the issues for the future, one being project management. One issue—it goes beyond our colleagues in these particular corporations, as we discussed the last time we spoke—is this whole problem of contract management and trying to ascertain what reasonable approaches should be taken in more commercial environments. We do not pretend to be technical experts, and certainly we accept the advice of the technical experts, particularly in the Meat Research Corporation, but this was a commercial prototype. Contractual obligations for the operation of the slaughterline were based on fully commercial criteria and included guaranteed performance rates of 99.6 per cent.

As the report pointed out—and it is not a blinding insight—this was a very exacting requirement for a prototype of whatever kind, particularly given the lack of operational data that was obtained from the research prototype at Cannon Hill. In those sorts of situations you have to ask yourself what kind of risk management guidelines should you have in place when you are making commitments—not inconsiderable moneys—even for risky projects, what are the sensitivities associated with those risks, what are the likely chances of this particular thing happening or not happening and have periodic reviews, particularly in the areas which are of agreed high risk.

That sounds all very fundamental—as I said, it is not a blinding insight—but it does point to the fact that, as we are getting into more and more commercial type operations, we need to borrow from the experience of the more commercially oriented elements of the Commonwealth public sector for those not so commercially oriented. We expect to learn some lessons from those that are commercially oriented. So the issue for this one is not just for the MRC and for its future project management, as we have heard Dr McCausland talk about, but what lessons does this have for other elements of the public sector.

The two senior auditors associated with this were John Bowden and Diane Barr, and they would be happy to answer any questions that the committee wants to put.

CHAIR—For the benefit of the committee, where does the Meat Research Corporation gets its funds from and how much comes from the budget?

Dr McCausland—Half of its funds comes from the budget. It is part of the rural industry research corporations where a levy is collected from all producers of beef and sheep meat, and then as that money is expended the federal government matches it dollar for dollar.

CHAIR—How much of public funds was at risk in this project? What is the bottom line?

Dr McCausland—If we say that the totality of the project from beginning to end was $40 million, there was $20 million of public money.

Mr BEDDALL—You indicated that the board had made the decision to run this project itself. Do any members of that board still continue to serve on the board and, if so, why?

Dr McCausland—No, none of the original board is still on the board. The decision was really taken before I joined it as the managing director, but I was part of the board that continued with Fututech.

Mr BEDDALL—I suppose a lot of issues arise but, in essence, it would appear that right from the start the management practices have left a lot to be desired. Can you enlighten us about how BHP Engineering was the successful tenderer? It had no experience in this type of operation, whereas I understand that some of the other tenderers, in fact, had expertise in the abattoir industry.

Dr McCausland—I will ask Mr Perry to answer that question.

Mr Perry—BHP Engineering were chosen primarily for their project management expertise rather than for their experience in the meat industry which, quite clearly, they did not have. However, they did have access to people in CSIRO who provided much of the original research and, of course, it was always envisaged that BHP Engineering would be subcontracting virtually all of the design and construction work to relevant specialist organisations. So, to sum up, they were chosen for their management experience in handling large and complex projects.

Mr BEDDALL—When problems became apparent and the management regime was identified as being faulty, you still, I understand, took some time for remedial practice to take place. Is that correct?

Dr McCausland—Yes, I do not think that the management group recognised that it was faulty itself. Certainly there were men of great experience in the meat processing industry involved in that. It was a frontier type project. We did not expect to have no difficulties, so when difficulties arose that was expected to some extent.

Mr BEDDALL—The Auditor-General has indicated that, whilst it was a very futuristic research project, the spec was very tight, which seemed to be contradictory. We were asking you for something very specific. In this type of research, obviously you may get a different outcome to the original specification, but that original outcome may have been beneficial anyway.

Dr McCausland—There was a catch-22 involved here. You really could not go too far with a straight prototype which did not have the capacity to process a lot of animals. You can imagine trying to process a lot of animals in a research laboratory type arrangement. Eventually we had to take the prototype to a commercial works to see whether this machinery could stand up to the day in, day out working by disinterested parties, not research scientists. We could not effectively replicate that in a research laboratory. We had to take the research into the commercial works. The only way we could do that was to guarantee to the owner of the works that we would either get to 99.6 or take it away.

So there was a real catch-22 there—unlike with other sorts of manufacturing gear—because of the dynamics of having to kill live animals and having to deal with all of the waste and everything else. Hopefully, the meat from the 3,000 or 4,000 cattle put through during the day would be sold at the end of the day rather than be thrown away. Of course, without having it in a registered works, you cannot get AQIS approval, so you cannot sell the meat.

Mr BEDDALL—You cannot sell it on the export market, but you could have had inspection for domestic consumption.

Dr McCausland—It would still need to be inspected and, of course, domestic inspection requires a very high standard as well.

Mr BEDDALL—But $40 million is a lot of experimentation. I am just trying to come to terms with the fact that we are not talking about $4,000 or $400,000. Forty million dollars is a lot of prototype. When did BHP identify problems? Did they get out of the contract too easily?

Dr McCausland—We think that we did the right thing in regard of BHP in that we did get them to do a scope of works. We paid a considerable sum of money, half a million dollars, for them to do a very thorough scope of works before they proceeded. We proceeded on the basis of their reputation, as they themselves put it to us. In hindsight, it was probably more than they knew, too. We were going into completely unknown territory and, basically, it was a bigger ask than they could see or we could see.

To be able to get something like this working in a commercial abattoir—and before we decided to stop it, we got it to work at about 80 per cent of effectiveness—costs a lot of money if you are going to automate these things. We were consulting with the industry all of the time. The industry itself—in terms of the meat processing industry, the Cattle Council, the Sheepmeat Council, et cetera—was giving us full support. We decided to stop it. They did not ask us to. They gave us full support right up until the last day.

Mr BEDDALL—When everyone pleads guilty, it is hard to pursue it. There are lessons to be learnt. Having had some responsibilities for some of the research corporations, I know some of the thinking that goes on.

Mr GRIFFIN—So what have you actually done to correct the problems that occurred? I read somewhere that you have accepted the recommendations, but I think a comment was made that they were largely what you were already doing, yet that did not occur on this occasion. When we look at this question of Fututech and what happened, was there a change in procedure that occurred for Fututech? Was it the situation that that was the way things were done prior to this event and that what makes this one different is that it was so big and so different?

Dr McCausland—We make the case that there was a real difference in the Fututech process in that it was conducted for good reasons to start out with but continued to be conducted and managed directly by our board. There were two or three other projects which carried on for a little while and then stopped under that form of management. The Fututech project kept on going until it was eventually handed back to me as managing director in mid-1994, and at that point I stopped it.

There are no other projects that were managed that way. We maintain that all other projects already fit within the recommendations that the ANOA recommended to us. It was and is a major disappointment to the corporation. You do not have that sort of failure and not be changed by it. When we had the ANOA recommendations we examined them very closely. We examined everything that we were doing.

The board put into quite a complex formal resolution that these things must be followed in the future. We took on three marketing managers to deal with the commercialisation and marketing of research results. In addition to the original board resolution, we put forward a complete commercialisation policy which embodied all of the ANOA recommendations. That was passed by the board and that is now mandatory within the corporation.

We have now formed a small group of experienced private sector senior people which make up the Commercialisation Advisory and Management Group. They are on a retainer to the corporation. We seek their advice before we go down commercialisation routes.

Since the ANOA report, we have instituted a weekly contracts meeting so that all new contracts being offered by the corporation have to go before all senior staff. All the objectives and the commercialisation policy have to be outlined. All of their peers are there to check every week. It is quite a rigorous peer group that every single contract has to go before now.

Mr BEDDALL—I notice in the original contract there was a cost-plus exercise which, therefore, puts no incentive on BHP Engineering to provide anything because everything they do is just added on. Are any of your current contracts cost-plus or are they all now performance based?

Dr McCausland—In certain cases there would be some cost-plus.

Mr Perry—I am not aware of any major cost-plus contracts. There would be some small ones where we are paying for services on a per diem basis.

Mr GRIFFIN—What do you call small?

Mr Perry—Probably nothing over 40,000 or 50,000 at the outside. I am guessing, I have to say.

Dr McCausland—Could I take that question back and say that, wherever we have a project which is of such complexity that we are not sure what is going to be required, our procedure now is to phase it. At the end of each phase there is a stop-go point. That is very seriously taken and examined before we go ahead. In that way we make sure that we do not go beyond what is prudent.

CHAIR—The Auditor-General's report makes very plain what the shortcomings were. It is very easy with 20-20 hindsight. It is fairly unusual that you would not conduct a risk analysis before the commencement of the project, isn't it?

Dr McCausland—Yes, I think it really does come back again to the way the project was managed. It was a carry on. Always with this project there was a feeling of great urgency. There was a feeling that we could not divulge too much because, if the industry saw in great detail what was coming and if we got the industry in terms of the work force involved in this, that—

CHAIR—By 'the industry' you mean the abattoirs and the meatworks?

Dr McCausland—The abattoir workers and so on. So another lesson we learnt was that, no matter what the reason, you cannot proceed with these things without having the end users involved intimately. We were talking to the owners of the abattoirs all of the time in the form of the Australian Meat Council, but we had almost no contact with the abattoir workers. With hindsight, we should have said to the industry owners, 'We cannot proceed with this unless we have the abattoir workers involved in it.' That would have taken one of the big risks out of it.

The procedures that should have taken place were reviews, right at the beginning, of the objectives that we were attempting to undertake. I think there are a few places—and the ANOA have picked them out—where, with the benefit of hindsight, we should have said, ‘Let us stop this. Even though we are under great pressure, we should stop it and have a look.’ That did not happen and the project went on.

Mr BEDDALL—You put out that you have sold some of the technology even though it is spin-off technology. Optimistically, how much recovery do you think could come out of that?

Dr McCausland—When we closed the project, we estimated that, if we got about half a dozen spin-offs from that, it would be valued by the industry at about $15 million a year. I would say that is probably about right. Some of these things are very hard to put a price on. For example, to combat a Japanese lunch box type problem which could arise when faeces get onto the meat—that is, the bugs get onto the meat via the faeces—we have developed an automated method, which is superior to the manual method, of blocking off the anus and putting a bag over it to make sure there is no spillage.

Mr BEDDALL—I am glad you did not bring slides.

Dr McCausland—We have not decided which minister we are going to ask to—

Mr GRIFFIN—He used to work in an abattoir. You could tell them we do not want to do an inspection on that.

Dr McCausland—It is very hard to put a dollar value on that. You cannot say, ‘Every animal, you are saving this much.’ It may save us from having a major scandal such as the Garibaldi thing. The other bits of equipment I think you could put a value on but, as I say, we made an estimate which we would stick to. If we can get six of these—we have three and almost four out now—it would be about $15 million a year. It is not a good investment, but $40 million is not totally wasted by any means.

CHAIR—Who owns the intellectual property rights?

Dr McCausland—CSIRO has some of those, with us in part, and a couple of them we own entirely.

Mr GRIFFIN—I have three questions for the ANAO. You heard the MRC talk about the fact that they have picked up on the recommendations, et cetera. Are you satisfied that that is the case and that this should not happen again?

Mr Barrett—We cannot say that at the moment. In any follow-up audits we would ask questions to ascertain that, but at this time I cannot say to you that we are satisfied. At the end of the day, I think Dr McCausland would agree with me that the proof of the pudding is in the eating. In essence, I suppose what we would be looking for—and this is a comment I was going to make—in a genuine evaluation of the project, for instance, would be whether BHP Engineering had indicated what it would have wanted had it operated more efficiently, what suggestions would have come forward considering that it did not, on the face of it, end up in exactly a happy circumstance. I would assume that they would have had some fairly forthright suggestions and comments to make. I would be interested in what they were and what action might be taken on them.

From the point of view of an outsider and a non-technical person, bearing in mind that there were known difficulties with key elements of the machinery, particularly the sensor equipment, in retrospect for similar kinds of projects, what is better to do from a cost-effective point of view? Do you take the chance that you will resolve the known technical problems when you are producing the prototype, or do you spend the effort prior to it? Obviously, it is how important are the elements in terms of the whole. That risk assessment has to be made.

Some of these things, of course, can be done in parallel. It is an issue whether or not, in this case, it would have been possible to do them in parallel, or are they sequential? On the face of it, particularly with the result, it may have been, if they were approached sequentially that they would not have spent $40 million. They may have spent $5 million and then said, ‘It’s not going to work because the main elements of the thing are not going to work,’ or, at the end of the day, do you go for broke? I know there is a different answer for every kind of project but I am wondering, when looking at that project and experience, what came out of it. If we were doing the follow-up audit, we would be asking those kinds of questions.

Mr GRIFFIN—This particular audit has raised a range of issues about similar sorts of projects that might be done through other R&D corporations. How valuable are those lessons, do you think, given that there is an element of case-by-case basis, as you just mentioned? Secondly, how successful have you been, or have you been able to pass these views on to other similar organisations to ensure that we do not get any repeats?

Mr Barrett—I will ask my colleagues the second part of that question because, up to now, given this is the aftermath, we are still looking at what is coming out of it. We do try to find opportunities for doing the sorts of things you are indicating. It has done two things for me. It has reinforced the requirement for a much tighter commercial approach than we have generally been used to in the public sector and a hard headed approach as well. We have prided ourselves in this country with the enormous amount of basic research that we have done. The criticisms that have been made of us are about the operational research and getting the thing to market. We have done tremendous work, as you all know, in identifying principles, ideas and things, but where we have not succeeded so well is getting them out into the marketplace. That requires another group of skills. Quite clearly, the MRC tried to do that by hiring BHP Engineering which, on the face of it, should have had project management skills to get that thing done, to market.

Mr BEDDALL—There is a real question here about boards of any research corporations. Ministers are told, ‘You can’t pick boards. It’s done by a selection process,’ and the selection process will pick those which have commercial expertise. In this round and round we go scenario, we had a board in place picked by a selection process that is obviously wanting. I have had a great deal of difficulty on a number of occasions with the selection process that was gone through. It seemed to me that, once you got on the A list, you stayed on it and went from one government authority to another and the pre-requisite for getting onto a board was the fact that you had served on another one, rather than going out into the commercial field. All these research boards were set up at arm's length from the minister of the day. Maybe that needs to be questioned as well.

Mr Barrett—You can understand why I will let that sit there. You do not have to be an expert. I think everyone in this room would agree that you do not have to be an expert in the particular area to be a good manager in this sense, and the same for the board. They are providing the corporate direction. At the end of the day, they are going to get the funding, they are going to demand performance and, hopefully, they are going to produce an outcome. They are going to get other people to manage and be the experts.

In this particular case, as we have heard, there were obviously problems because of uncertainties in the project. There was high risk. In terms of management they thought they had done the right thing by getting the right sort of experts in place, which is about all you could genuinely expect. Of course, clearly the minute that the board took itself out of that cosy area where it should have had expertise to do the things it was set up to do, the minute it stepped outside that, it was in trouble. I think that is one obvious lesson which is not lost obviously on the MRC or anyone else.

Coming back to Mr Griffin's point about project management and contractual arrangements, what we need to do, as we accumulate this kind of experience under the broad corporate governance heading, is set down these and make sure, through Finance in terms of the overall corporate governance for the Commonwealth, that we bring these forward and that awareness is raised in the usual ways which were described this morning.

What it is re-emphasising is that, as we move into the more commercial environment, we continually seem to underestimate what is involved in these contractual arrangements to get the product we want at the end of the day at the price that we want to pay.

Mr GRIFFIN—Why do you think that is so?

Mr Barrett—Basically, because we lack expertise and we have got a different mind-set. I am not talking about MRC but the rest of the Public Service. That is not what we were recruited for. It is not the environment that most people who have been around for a few years have been brought up into.

I suppose the other element, of course, is the extent to which the parliament is going to be prepared to accept the risk taking that is involved in some of these commercial type decisions. Quite clearly, public servants have always had in the back of their minds that they are going to get a fair sort of welting if in fact they make mistakes, and there has been a premium on that. I do not think anyone would deny that. You are watching your backsides, so to speak, on these projects to make sure that the downside is as small as you could get it. And, by definition, the upside is not too smart because you are concentrating more on the downside than the upside.

Is parliament—and we talked about this before in previous JCPAs under the risk management heading—going to be prepared to accept the kind of judgments that are involved? From an Auditor-General point of view, I can say that I support risk management on the basis that boards of management, managers and ministers clearly articulate the risks involved, the judgments involved and how much Commonwealth money is at risk so that, at the end of the day, the parliament would have this information. At the end of the day they might say that that was a silly decision. But at least they could say, 'Yes, we can understand why you took that decision,' et cetera.

We will not get it right all the time but this is the discipline of being in the public sector. I do not want to go on to tell you to suck eggs but in this case it is a hell of a lot different to the private sector. It is not just a case of pulling someone out of the private sector, sticking them into the public sector and saying, 'Go for it', because they have to learn that they are now in the public sector. There are certain constraints on them as managers and entrepreneurs et cetera to achieve outcomes that relate not only to a taxpayer who is interested in value for money but also to other issues that are relevant to the parliament of the day. I think you can understand why public servants have been reserved about this whole question of risk management and what it means for them in practice. At the end of the day, they cannot afford to come along to the JCPA and say, 'I'm very sorry: I've lost $40 million worth of taxpayers' money; it won't happen again.'

Mr BEDDALL—That is why I understood we set up boards that were supposed to be not Public Service boards overlooking all of the research and development corporations. They were supposed to bring the necessary commercial expertise. Maybe we should have gone one step further and made the directors liable like in the private sector. That might have concentrated their minds more.

The fact is that we have that structure in place. Because of the innate conservatism of the public sector, that it is risk averse, the boards were supposed to be there to give direction. Obviously, what we have here is a failure of the board, because it took a management role rather than an overview role. That is one of the lessons for the future.

Perhaps one of the problems that the Auditor-General's office may have to face down the track is that if that is a culture that exists in one board of the R&D corps, then that culture may be endemic right through them. I do not know how many projects there would be of this scale. I would think very few, from my experience.

Mr Barrett—I think it was one of the largest at the time.

Mr BEDDALL—Yes. R&D tends to be $2 million to $5 million, or maybe at the top, $7 million or $8 million. I would have thought that, in most of the primary industry research and development corporations, the exposure in this was much bigger than any of the others. Again, that is probably a management thing, that it was so big that you lose sight of things. Perhaps the people who did the audit may have something to say.

Mr Bowden—To respond to Mr Griffin's second point, yes, we wrote personally to the chief executives of all the R&D corporations enclosing a copy of this report, drawing it to their attention, to their particular line of industry. We also gave notice that we would be coming back in the future to follow up an earlier audit that we had done on rural research and development corporations. We looked broadly across their project management, but only in broad terms. Most of them seemed to have the basic principles in place, but we were going to come back to look specifically at the lessons learned from this exercise.

CHAIR—Was the legal work on this project done in-house or was it done by outside lawyers—public sector or the private sector?

Mr Perry—We used outside lawyers, a large firm of solicitors in Sydney.

CHAIR—Is the MRC happy that their position was protected by their contracts adequately?

Mr Perry—We certainly take note of what the ANAO has said. Our response to the ANAO comments on the contracts was that the corporation worked very hard, and its lawyers did too, to protect its position. Pivotal to the contractual conditions was the fact—this is already noted in the report—that the field was very narrow. In the case of Kilcoy, there was no other contender. Even though it was widely known that the corporation was seeking a site for the prototype abattoir, there was no other contender. So it was a question of doing the best deal possible with Kilcoy.

CHAIR—Why was there no other contender?

Mr Perry—I can only guess at the reasons for that. It would be reasonably unusual for any company to require a complete new slaughterline, bearing in mind that Fututech was a complete slaughterline from lead-up race to carcass splitting. So that would cut it down. It happened that Kilcoy required to update its facilities in a fairly major way. I think the only alternative type of contender would be someone putting in a greenfield operation, of which there are not many. I guess we are dealing with a very risk averse industry where there was plenty of interest, but they all wanted to be No. 2 rather than No. 1. So Kilcoy was the only one that put its hand up.

CHAIR—The others were not prepared to take the risk?

Mr Perry—That would be correct, I would believe.

Mr GRIFFIN—You heard the comments by the ANAO a minute ago about that whole question of risk taking by public sector managers, boards and so on. Do you have any comment on that? Do I take it from the fact that you have accepted and embraced the recommendations from the report that you basically agree with what the ANAO has been saying today about that sort of issue?

Dr McCausland—Yes. The MRC generally thinks that the fundamental error here was the issue of corporate governance, that the board went down into management and then had no effective checking and balancing. I think that is the major message. It has certainly been taken on by the MRC. I have given a public address to all of the other managing directors of all of the other R&D corporations indicating the dangers of boards getting involved in management. Research and development is of great interest to many people. They love to dabble in it, but I think the lesson is to keep them out of managing so that they can stand back and be the dispassionate jury on whether things are going right or wrong. That is the major message, we believe.

Mr BEDDALL—What is the composition of the board now? I am not necessarily after names, but disciplines.

Dr McCausland—As you would be aware, boards have to be selected against criteria. There has to be someone experienced in research and development, someone involved in public administration—that is usually the government member—someone involved in production, someone involved in processing and someone involved in finance. I believe the selection process has for MRC worked very well and that has been the only real anomaly that has happened.

Mr BEDDALL—You wouldn’t want too many anomalies like that, though.

Dr McCausland—You would not, no.

CHAIR—As there are no further questions, I thank you for coming today.

[2.35 p.m.]

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Audit Report No. 719 of 1995-96, Department of Veterans' Affairs, Financial Audit

CHAIR—This is the final report for today's public hearing. For the benefit of those who are new, we will conduct this hearing in a round table format. I ask participants to observe a number of procedural rules. First, only members of the committee can put questions to witnesses—that is, if this hearing is to constitute formal proceedings of the parliament and attract privilege. If other participants wish to raise issues for discussion, I would ask them to direct their comments to me and the committee will decide if it wishes to pursue the matter. It will not be possible for participants to respond directly to each other. Secondly, to assist Hansard, witnesses should identify themselves whenever they wish to make a comment. Thirdly, given the length of the program, statements and comments by the witnesses should be kept as succinct as possible.

The Auditor-General's views have been set out in the report, as well as the initial responses of the audited agencies. For this reason we are proposing to dispense with the lengthy opening addresses. However, I would like to provide an opportunity at the outset of the hearing for the Department of Veterans' Affairs to inform the committee of any action that has already been taken to implement the recommendations in the Auditor-General's report. Do you wish to make a brief opening statement to the committee before we proceed to questions?

Dr Johnston—Yes, thank you, Mr Chairman. I will keep my comments very brief. As the Auditor-General has indicated in his document—for example, on the bottom of page 9 of the introductory summary remarks—the decision to undertake this audit came at a time when we were implementing significant organisational changes in the department and moving to a more devolved management structure. At the time we realised that we needed to significantly improve and address the way we were addressing financial management in the department. We were reasonably well advanced in thinking through some of those issues ourselves when the proposal for the audit came forward. We were very pleased to cooperate with the Audit Office and have found the audit process helpful to the work we are doing as a department.

From our perspective, the report certainly served the useful purpose of identifying further areas which we needed to address as a department. It certainly re-enforced the need for change in the department, and that is always helpful when dealing with one's own management and staff. Finally, it certainly validated the financial management changes we were already contemplating as a department.

In all, there are 16 recommendations in the report. I can report to your committee that eight have been fully implemented. Three, which involve IT systems development, are in the final pre-implementation stage, with implementation currently scheduled for the end of this month. Two, which involve the assessment of financial training needs and the development of appropriate training modules, are well advanced, with completion on target for the end of September—that is, the end of next month. One requires a decision from the Office of Government Information Technology on whole of government financial management information systems. On that front we are awaiting decisions and expecting them within a few months. Finally, the two remaining recommendations require analysis of financial data from the department's new cost centre structure, which is a major innovation for our financial management as a department.

We need to get that data before we can progress on those recommendations. But, Mr Chairman, I think it will be evident that we have found this report well attuned to our needs as a department, and I think we have made good progress in implementing its recommendations.

CHAIR—Thank you. I now invite Mr Barrett to address us.

Mr Barrett—I think this is, again, another audit where there was, maybe fortuitously, a congruence of interests. The result is that it was a very productive audit from the point of view of the department, as you have just heard from Dr Johnston. I do believe that this genuinely has met our requirement to add value in public administration.

More importantly, in my view, the outcome of this audit is not just for this department; it has quite clear implications for all departments in this arena.

As the committee would have noted, under appendix C there is a framework for financial management in programs as an overlying indication to departments and agencies of what one would expect to see as constituents of that program. More importantly in many ways, I think the check list for financial management is derived from the real life experience and the principles that generally are accepted in both public and private sectors of good financial management.

There were certain issues. In particular, this is a very large expenditure and a department with considerable client numbers coupled with a wide-ranging nature of departmental services and forms of service delivery. Of course, clearly, they do have an enormous administrative task. An added dimension to these challenges was the move by the department from direct supplying to purchasing health services. Clearly, this is something we are likely to be hearing more of in the public sector in the future.

In past audits, the experience we have had has suggested that there is a degree of uncertainty regarding the role and relevance of financial management in program administration. Probably this is the area where I would pick up on a couple of the key findings—and, to my mind, I am not saying that these are necessarily the most important. But just for the committee's sake, one of the key findings was that financial management in program administration was not rated a high priority by staff. That is not endemic simply to DVA; that is a factor that is of general relevance around a number of agencies.

The other point associated with that and which is perhaps also part of that point is that managers were not sufficiently trained in management-oriented financial administration or analyses. In essence, for the reasons we have been discussing earlier this afternoon and this morning, that also has been the situation generally in the Public Service, despite the attention of, as we have discussed, the financial management improvement program, and the like.

As Dr Johnston has said, we saw this audit as helping us to better understand the practical problems that that department had in developing a more robust and user oriented financial management framework to effectively support program management and administration in its new structure. We saw that as having an advantage to us in terms of us dealing generally with other agencies. So the objective, succinctly put, was to ascertain the extent to which financial management arrangements had helped the department to achieve its objectives efficiently and effectively and the way that these arrangements could be improved in the light of the department's own management reforms.

I will not repeat the recommendations except to say that we have probably had one of the best responses to reports we have done so far in terms of commitment that is made and has already been made to implementing those recommendations. On my right are Alan

Greenslade and Jim Grenfell, who were the senior audit staff involved with this audit and who are happy to answer any questions the committee would like to ask.

CHAIR—Dr Johnston, you said you were waiting for decisions. Do you want to elaborate on that?

Dr Johnston—I turn to recommendation No. 9:

The ANAO recommends that the department undertake a review of the costs and benefits of integrating its financial systems to avoid the current duplication of effort in the use of reporting systems.

The government is currently reviewing a government-wide provision of IT systems for both staff management and financial management purposes, two separate exercises. We are waiting on the conclusion of that exercise before we make decisions on our systems in that area.

Mr GRIFFIN—In terms of training courses, you mentioned a couple of recommendations related to that issue. Can you go through where you are up to with implementing training courses for your senior managers?

Dr Johnston—Yes, I can give you some details and possibly ask one of my colleagues to flesh that out if that is required. The task of improved financial management training for our staff has been well identified and well scoped but we are now in the process of more detailed specification of needs and structures for those training programs. It takes some months to finish that work.

Mr GRIFFIN—Are you developing those in-house? Has there been any assistance from Finance or anywhere else in the service?

Dr Johnston—My expectation is that we will make use of whatever good training is available, but I should ask my colleague if he could answer that in more detail.

Mr Mackrell—Yes, that is correct. We are looking at all resources possible. We have done this initial scoping exercise, in-house obviously, and we will develop the package for DVA and subsequently, I guess, with one eye towards migrating that package to other parts of the Commonwealth service that may be inclined to take it up. We will certainly be looking at modules from places such as the Department of Finance where appropriate.

Mr GRIFFIN—But you are still in the development stage?

Mr Mackrell—We have finished the scoping. The recommendation asks us to identify the needs and the types of financial information relevant to program managers and we are doing that. We are now developing a course that will meet those specific needs at the various levels of need that have been identified.

Mr GRIFFIN—Has the department integrated its financial systems so that there is less duplication of effort in generating financial reports?

Mr Mackrell—The problem at the moment is that to do that comprehensively we really need to either significantly re-engineer our existing system or move to a new financial management information system. We are currently waiting on the Office of Government Information Technology to come up with a panel of new systems and there is currently a prohibition on significant changes to existing systems while that is going on. As a short-term measure we have developed a data warehouse approach whereby information is downloaded from our various systems into a pool, I guess, and we have built a relatively simple system to access and report on that data. Once this is fully implemented that will be updated on a daily basis and is a very good and relatively modest cost interim solution.

Mr GRIFFIN—You mentioned that eight recommendations have been fully implemented so far. Could you flick through those?

Dr Johnston—Did you mean list them?

Mr GRIFFIN—Just mention them and explain what has been done about them, I guess. That will be self-explanatory.

Dr Johnston—Recommendations Nos 1, 2, 3 and 4 have all been implemented. I think at least two of those, recommendations Nos 2 and 3, relate to approaches to planning and business management and to business planning as a department. Work has been under way in the department now for a good 18 months. A lot of excellent work has been done in that area. It is now expected that each year we will develop an agreed corporate plan and that will inform development of business plans by all the operational units in the department.

Recommendation No. 4 relates to improving coordination across the department. In the most recent restructuring, which dates from just several months ago, both Mr Mackrell's branch and Mr Callioni's branch are now key coordination points in the financial management and planning of the department's activities. Recommendation No. 6 has been implemented and recommendation No. 7 has been implemented. Mr Mackrell may want to speak to the detail of those two. They are probably a little more familiar to him.

Mr Mackrell—Recommendation No. 6 stated:

. . . that the department develop comprehensive guidelines to enable estimates to be prepared on a consistent basis.

Between the period when the audit was undertaken and the report was presented, we had developed what we call a budget survival kit—

Mr GRIFFIN—We could all use one of those, I suspect.

Mr Mackrell—Which is a set of guidelines and a process matrix to enable those staff involved in the budget process to take a uniform approach to costing, looking at departmental policy determinants, et cetera. We have provided information on the standards of documentation and pro forma documents on disk. So we have gone a long way towards standardising that process. In addition, we are also reviewing our estimates process and our estimating models with regard to program estimates to ensure that they reflect the current situation of our veteran population.

With regard to recommendation No. 7, we have improved the allocation of funds, including its priorities and timeliness. However, because we have currently moved from a May to an August budget, that has caused us some difficulties this year. But, with the move back to a May budget next year, we will be back in line and continuing to improve the timeliness of those allocations. So we believe that one is implemented.

Mr Johnston—If I can move on then to recommendation No. 11, it reads:

The ANAO recommends that the needs and types of financial information relevant to program managers be identified and reflected in the management reporting framework. The department should pay particular attention to this concept in designing new management information systems.

That has been implemented. This approach has been reflected in the development of a new front end to our financial management system called FILM. It is intended to enable managers to articulate quicker the key reporting items that they want to address in managing their affairs. There is extensive work going on at the moment with working groups not only in each of the program areas but also across the department looking at the performance information which we are using as a department.

We are making reasonable progress on that front, but in my experience that task never ends. You are forever reviewing the appropriateness of your indicators as your business environment changes from year to year. I think that, as managers, we often find it difficult to identify the few critical indicators that should have the highest priority from the whole and wide range of indicators that we can articulate using the sophisticated systems we have available these days. I am not sure, to be frank, that we have that balance right yet. Indeed, I am having discussions with the managers at the moment in which they are telling me where they do not think we have that right yet. So it is something we need to continue working at.

I guess that also relates to recommendation No. 15, which is closely related. It reads:

The ANAO recommends that, as an initial step, the department use its management information systems to develop a performance measurement framework.

That is very much the same area of work. I think that runs through the eight recommendations that at this point we would consider having been acted on and implemented.

Mr GRIFFIN—With respect to this issue, and ANAO may want to respond to this as well, how typical do you think Veterans' Affairs is in needing these sorts of changes? Was it a situation where the work that you do made you different from most other departments or was it a situation where the lessons from this would be applicable elsewhere? Where would Veterans' Affairs be in a scale from one to 10 in actually being on top of these sorts of issues? And, given that you were part way through a review when the audit occurred and that review is continuing—so you were looking to make some of the changes which have come through the audit anyway—does that put you in front of most departments, about the same or behind?

Mr Johnston—That is a hard question to answer. As a secretary, I would want to say we are well in front.

Mr GRIFFIN—You are a relatively new secretary, so you can do what they do and say, 'It was not my fault.'

Mr Johnston—You would not believe me, Mr Griffin. You might want to ask Mr Barrett for some comments, but I can give you some perceptions of the issues that the department has been having to work through. I think in previous years it gave considerable priority to a program structure perspective to management, and that program approach permeated right down through the organisation, including through into the state office management structures.

The department worked very hard to make that work, but in the end management came to the conclusion that there needed to be somewhat more of a compromise between the program management perspective and the customer service front-end perspective. So that is the change we have been implementing. Necessarily, we have had to work as a department to get everybody to lift their eyes a little and look across the department at the coordination of financial management and at how better to integrate service delivery to veterans. I think we have made good progress on that score.

I do not know that other departments would have had the same history or the same recent experience. The other significant feature for this department is that, for program managers, many of the programs are intended to provide quality service to veterans that generally meet all their legitimate needs as veterans in compensation for their service to the country. What that means is that there is not always the same pressure to live within a fixed budget resource. They are what public servants refer to at times as demand driven programs. I think that possibly in the past we have not given enough attention to strategies for cost containment within programs which will be possible while meeting all the legitimate expectations of veterans.

The department has taken some quite excellent initiatives in the last couple of years in the health program area. It is working very hard at evaluating veterans' use of health services and pharmaceuticals and providing feedback to institutions and doctors where significant improvements in outcomes can be achieved with less expense. So it is a matter of developing those sorts of strategies right across the department.

Mr BEDDALL—In the broader context, it has often been said that there is a certain time frame in the curve for veterans' affairs because of the age of World War II veterans, in particular. How long before you reach that peak in cost, or have you reached that peak? A lot of us do not tend to realise that the older these people get the more expenses there are.

Dr Johnston—Indeed. Not only is it more expensive but more services are required, particularly in health and accommodation areas. Transport becomes a problem for them. It is true that the unit cost of services to veterans is likely to continue to rise in the foreseeable future.

The department at the moment is undertaking a comprehensive review of the network structure of the organisation—the requirements of the veteran community and the changes that are occurring there as veterans' needs change with age, location and so on. We expect that the minister will be releasing a discussion paper on those issues within a month or two. That will present some statistical information on that very issue. The work that we have done suggests that the demands on the department are still to peak. They will probably peak within the next few years and will not drop off all that sharply for quite some time. That increased demand for services really does carry a lot of weight as the community ages.

Mr GRIFFIN—Mr Barrett, would you like to comment on that?

Mr Barrett—We are happy from the financial audit point of view to give the committee, as we do, an analysis of where Veterans' Affairs sits in relation to other areas. I think the most telling observation was the comment made by Dr Johnston, where the previous secretary—and this was shared, as I understand it, by senior management in DVA—thought that something needed to be done in this area. I think that is indicative of what the perception was as to where they were and where they had to be.

I really do underline the importance of recommendation 11. Program management, budgeting and information systems have probably not attracted the support that they should have had from managers generally in the Public Service because we have never really ascertained from those managers exactly what it was they needed to manage their programs. That is what is being done under that recommendation, and we will have lessons for other agencies in that respect.

The other thing that we have not done well—any of us really—is to link the provision of the information that managers regard essential to their day-to-day management with the performance information; that is, directly linking that information so they have in mind all the time what performance they are aiming to achieve at the end of the day, and they can link the two together. That is something that the new systems that are coming on the market have the potential to do.

Quite clearly, as we discussed earlier in the day and it has now been reiterated, we are in a state of hold because these systems—such as rationalising, the issue of central bureaus, et cetera—have to be looked at. There is a government requirement to put a hold on any new system until such time as they have a chance to report and the government has a chance to decide what they are going to do about that.

Nevertheless, the points I was making earlier are fundamental to any system regardless of who does it. If you have an outside supplier who has a very good financial management information system, they will come in and ask you the same questions. In essence, we have to do this base homework that most of us have not done in the past in order to ensure that any systems that we do implement are going to deliver to program managers the ability to provide information necessary for them to manage their programs—and, more particularly, the ability to stand up and be counted in front of Senate estimates committees and functional committees and be able to link that information—

Mr GRIFFIN—We do not mind if you have problems at Senate estimates now; it is okay.

CHAIR—We cannot all agree with that, of course. I think we have covered all the areas of the recommendations in the report. There seems to be a harmony between DVA and the audit office, and we are pleased to see that.

Mr GRIFFIN—I have one question for Mr Barrett. How many reports would you have had since you have been Auditor-General where the department has accepted every recommendation?

Mr Barrett—I cannot remember any, quite frankly. We will have a check and get back to you, but I doubt if there has been any where we have had 100 per cent acceptance. We might have had 100 per cent with a couple of qualifications, but I think most times we have not had 100 per cent agreement. It is not to say that we would necessarily argue that we are the bible in that respect. We are prepared to agree that sometimes we do get it wrong.

CHAIR—Dr Johnston, do you want to put anything further?

Dr Johnston—No, thank you. I have had a chance to say all we needed to.

CHAIR—Thank you very much.

Committee adjourned at 3.06 p.m.