# JCPAA Review of Accrual Budget Documentation
# Answers to the Committee's follow-up questions
### Department of Finance and Administration
### 26 July 2001

1. **During the round table discussions held on the 22 June, Mr Tony Harris raised the issue of whether the budget outcome should be audited. Mr Ian McPhee, deputy Auditor-General responded that 'it would be within the capability of the ANAO to review the budget outcome.' (Transcript p. 31)**

   - **Would you discuss the merits and feasibility of auditing the budget outcome?**

Response:

As part of the Commonwealth's move to an accrual budgeting and reporting framework in 1999-2000, the Final Budget Outcome (FBO) reports now incorporate audit cleared accrual-based revenue and expenses, balance sheet and cash flow information. Such information is obtained from the annual process of compliation of the Consolidated Financial Statements (CFS).

The CFS and the underlying individual financial statements published by Government entities are already subject to audit by the Auditor-General prior to their publication in September/October each year. The FBO performs a different function – the emphasis is on timely, indeed speedy, issue of this information, to an acceptable degree of accuracy. The main question, discussed below, is whether audit of the FBO would compromise its timeliness and end-year utility, pending release of the CFS.

At a practical level, there are several issues that require consideration. Firstly, like other budget documentation, the FBO includes two sets of financial reports, one prepared in accordance with Australian Accounting Standards (AAS), the second prepared in accordance with Government Financial Statistics (GFS) standards. The FBO document also includes other financial and statistical data.

Secondly, the introduction of full audit sign-off of the FBO would introduce very tight time pressures on the audit and publication process in order for the 30 September deadline for publication of the FBO under the Charter of Budget Honesty to be met.

Lastly, if the auditor were to audit the full FBO, the level of audit assurance needs to be considered. The auditor could provide the traditional positive assurance audit report, which requires a full scope audit approach. This is the approach adopted for the audit of the Consolidated Financial Statements. Alternatively, the Auditing Standards provide for the provision of a negative assurance report, based on a review only, not a full scope audit.

Finance is concerned that audit of the FBO would compromise its timeliness and regards an audit as being unnecessary given the present approach. In the event that audit of the FBO were to be recommended, and accepted by the Government, the audit approach to be followed would need careful consideration by the Committee, the Auditor-General and Finance.

2. **Report of the Senate Finance and Public Administration Legislation Committee (SFPALC), *The Format of the Portfolio Budget Statements, Third Report.***

   **The SFPALC concluded that Senators were 'exhibiting varying levels of patience with the current levels of instability in the reporting frameworks in some portfolios; there is a clear expectation that the frameworks should stabilise sooner rather than later.' (Report, p. 39)**

   - **Do you feel that year-on-year stability in the outputs/outcomes structure and performance measures contained within Budget documents and annual reports is being achieved?**

Response:

Finance's first submission to the current inquiry noted that in the initial years of a new system there can be significant variations in the numbers of outcomes and outputs as portfolio structures settle down. However, it is desirable that we enter a period of greater stability in this area.

The Performance Management Principles, which were attached to our initial submission, note that performance reporting is most effective where trends can be compared over time. They also note that reporting can be expected to evolve with experience, changing needs, and the availability of more relevant or more reliable information.

3. **Appropriation Act No.1 2001–2002 authorises the Minister for Finance to issue out of the Consolidated Revenue Fund the sum of $41 425 224 000 in accordance with the Schedule which forms part of the Act.**

   **It has been suggested that the Appropriation Act No.1 could alternatively authorise each Portfolio Minister to issue out of the Consolidated Revenue Fund the amount for each entity in the Minister's Portfolio.**

   - **Would you care to comment?**

Response:

Finance would not support the above proposal for a number of reasons.

Under the devolved banking arrangements which were put in place on 1 July 1999, agencies are responsible for managing the funds that they receive from the Budget and other sources. This responsibility includes:

- ensuring the cost-effectiveness of agency cash management and banking practices;

- ensuring the adequacy of working capital;
- ensuring that receipts are collected by due dates and banked promptly;
- ensuring that payments are made only when due except where earlier payment would create a net advantage to the Commonwealth;
- optimising return on assets employed; and
- minimising the cost of capital.

While agency chief executives are responsible for managing the cash resources coming within agency control, the Finance Minister, in collaboration with the Treasurer, has responsibility for managing the Commonwealth's overall cash position. One of the key objectives of Commonwealth central cash management policy is to minimise the overall cost of Commonwealth borrowings, that is, public debt interest costs.

In recognition of the time value of money, an important element of the Commonwealth's central cash management framework is the Finance Minister's capacity to manage the timing of funding to Commonwealth agencies. Under the arrangements in place since 1 July 1999, the Finance Minister's delegate negotiates and agrees the timing of the cash to be transferred to agencies in respect of, inter alia: outputs; departmental equity injections; departmental loan drawdowns; departmental special appropriations, administered capital injections; administered grants, benefits and subsidies; specific purpose payments to the States and Territories; payments to be made from special accounts; GST funding; and refunds of taxes, excise, fees and charges. The agreed timing of the funding flows to agencies is based upon agencies' business needs. By carefully managing the timing of funding to agencies, the central pool of cash available to fund the emergent needs of all Government programs is optimised, with minimal borrowing costs. Less than optimal cash management in this area could significantly impact on public debt interest cost.

In addition, central management of the agency funding function affords the Government an important degree of flexibility in the reprioritisation of Government programs throughout the year, within clear accounting and budgeting rules.

Against the background of consideration of the Commonwealth's broader cash management responsibilities, Finance would not support the suggestion that the Appropriation Act No.1 could be changed to authorise each Portfolio Minister to issue out of the Consolidated Revenue Fund the amount for each entity in the Minister's Portfolio. In our view, such a change would present considerable risk to Government's capacity to centrally manage the timing of the provision of funding to agencies, with consequential risk to optimal cash management and public debt interest. It would potentially diminish Government's flexibility to adjust Government programs throughout the year within accounting and budgeting rules.

**4. Budget Paper No. 4 provides that basic appropriations are made as either Departmental or Administered items.[1] In relation to Departmental items, Budget Paper No. 4 provides that:**

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[1] Agency Resourcing 2001-02, Budget Paper No.4, Appropriation Bill (No.1) 2001-02, Part 2-Basic Appropriations, p. 34-35.

***S7(1) For a departmental item for an entity the Finance Minister may issue out of the Consolidated Revenue Fund amounts that do not exceed, in total, the amount specified in the item.***

**The wording of S7 does not explicitly state that appropriations are linked to outcomes.**

**Conversely, for Administered items, Budget Paper No. 4 provides that:**

***8 (1) For an administered item for an outcome of an entity, the Finance Minister may issue out of the Consolidated Revenue Fund amounts that do not exceed……….***

**In this case there is a clear link between an appropriation and an outcome.**

**Further, Budget Paper no. 4 defines a Departmental item as:**

***the total amount set out in the Schedule in relation to an entity under the heading "Department outputs".***

**Once again there is no linkage of appropriation to outcomes. This suggests that for legal purposes, the relevant parts of the schedule in relation to appropriations are the *entity* and the *total amount* only.**

**It may therefore be construed that from a legal viewpoint, Departments/Agencies are not bound to expend appropriations on the outcomes they have nominated in the Schedule. Instead, an *entity* has a *total amount* that in theory could legally be expended for any purpose.**

- **If the interpretation is correct, what are the implications as regards accountability and transparency of Government expenditure?**

Response:

At least since the introduction of the running costs system in the late 1980's the definition of appropriations for what are now departmental outputs has been very broad. Under the running costs arrangements, agencies were appropriated a single line item labelled "running costs" with this term being undefined in the legislation. There appeared to be no Appropriation Act limitation per se to the purpose to which these running costs appropriations could be devoted.

The new accrual appropriation framework, operating from the 1999-2000 Budget, includes an explicit interpretive linkage between the appropriation bills and the Portfolio Budget Statements which are declared to be "relevant documents for the purposes of section 15AB of the *Acts Interpretation Act 1901*". The PBS's then provide detailed splits by output group of the amounts shown against "departmental outputs" for each outcome in the bills.

The difference in treatment of administered and departmental items under the accruals appropriation framework reflected a desire to maintain the flexibilities of the original running costs system. In particular the intent was to maintain the ability of agencies to redirect their departmental resourcing as required between their various activities so as to meet changing circumstances or priorities and achieve identified outcomes within legislative constraints. This is why the definition of a departmental item in section 3 refers to “the total amount in relation to the entity” and departmental output allocations are defined as “notional” and why section 7 (1) also refers to the item as a whole rather than the individual outcome splits.[2]

As to transparency and accountability, Finance considers that the accruals appropriation and performance management framework is clearer than the old cash budgeting system because:

(i) Departmental expenditure is notionally split by outcome in the bills:
- The running costs line had no supporting explanation in the old cash appropriation structure;

(ii) There is a clear and unambiguous link between the appropriation items in the bills and detailed breakdowns by output group in the agency PBS:
- The mapping between appropriation structures and the old programme structures (in PBS’s) of the cash regime was not always clear.

(iii) The structure of annual reports reflects that of the PBS, allowing a “clear read” between estimated resourcing and final performance.

**5. Anecdotal evidence suggests that DoFA's main role in relation to the PBSs has been to advise entities about the wording of outcome and output statements and that this advice has been restricted to the form of the wording, not the content.**

**- Would you discuss your role in ensuring the various agency outcome and output statements and performance measures are consistent with each other?**

Response:

The move to the new accrual-based outcomes and outputs framework was accompanied by a substantial training and workshop program for agencies, designed and executed by Finance. There is also an ongoing dialogue with agencies through the Chief Finance Officers’ Forum, convened and chaired by Finance, which meets monthly.

There were significant legislative changes accompanying the move to an outcome/output framework. These reflect increased devolution of authority and accountability. While responsibility continues to rest with relevant portfolio ministers for the specification of outcomes, chief executive officers (CEOs) are now explicitly

[2] For example see sections 3 and 7 of Appropriation Bill (No 1) 2001-02 (pages 32 and 34 of 2001-02 Budget Paper No 4).

responsible for the products and services delivered (outputs). Guidance on outcome and output specification, and on changes to these, is available on the Finance website.

For outcomes, agencies are expected to obtain legal advice to confirm that the new outcomes form "valid appropriations" under Sections 81 and 83 of the Constitution, obtain approval from their Minister; and obtain endorsement from the Minister for Finance and Administration. Any changes require endorsement in a similar manner.

For outputs and performance information, agencies are responsible and accountable for the delivery of outputs and monitoring of performance against both outcomes and outputs. They are expected to seek agreement to proposed changes to outputs through the clearance procedures agreed by the relevant portfolio minister. Although agencies do not need to seek endorsement from the Minister for Finance and Administration, it is suggested that they consult with relevant stakeholders, including Finance.

Finance's website guidance advises that changes to outputs should only be undertaken if there will be a material improvement in the specification and such improvements are not outweighed by the need for year-on-year consistency.

Consultation between agencies and Finance on outputs often occurs as part of the outcomes process.

**6. In its submission the CPA commented that variations to the information presented in the PBS from period-to-period can be confusing and can partly be addressed if 'maps or notes are provided to highlight the changes in outputs, outcomes and performance measures.'**

- **Would it be valuable to include flow charts and diagrams to highlight variations to the information presented from period-to-period?**

- **Would you discuss the advantages and disadvantages of an entity's output structure reflecting its program structure?**

- **Would it be valuable to indicate diagrammatic and quantitative measures to demonstrate the link between programs and outputs?**

Response:

On the first matter, Finance agrees that there is value in agencies providing information in their PBS of changes in outcomes, outputs and performance measures.

In 1999-2000 agencies identified the necessary changes from objectives and programmes to outcomes and outputs as part of the introduction of the new framework, often using diagrams. They have continued to identify in PBSs subsequent changes to outcomes and outputs. The question is whether they should also identify changes in performance information. Finance's view is that this should be encouraged for the more significant changes but this is more properly a matter for each agency CEO, given their responsibilities under the Financial Management and Accountability Act.

Finance's first submission indicated our firm view that an alignment of agency organisational structure with their outcomes/outputs is best practice because this best defines management accountabilities and responsibilities, and enables agencies to directly translate internal activity reporting to external outcome reporting.

The term "programme" is in many ways a remnant from the previous Programme Management and Budgeting framework. It can be ambiguous. In the current context, it may relate to an outcome or a wide-ranging activity encompassing several items or outputs. It can also sometimes refer to or all or a small component of an administered item or departmental output. While the "programme" terminology may be useful in some circumstances, it can create confusion unless some clear relationship is defined between it and the related outcomes, outputs, and administered items.

**7. On pages 15-16 of its report, the SFPALC provided a model table for inclusion in the PBS which gave information for the reasons for change at the output level between the estimated actual and the Budget estimate for the following year.**

- **Would you comment on this suggestion?**

Response:

The Government did not favour the SFPALC's suggestion, as its view was that the PBSs provide sufficient information, explanation and justification as to the purpose of each item in the Appropriation Bills. It noted that modifying the existing format to explain variations at an output level would add complexity without enhancing clarity.

**8. On page 40 the SFPALC recommended that forward estimates at the output level be required to be provided in the PBS for administrated items (it would consider the case for extending this to departmental items in the future). On pages 16–17 it is reported that forward estimates information is available and that some agencies are in fact prepared to publish them. (DETYA has published forward estimates in their last two PBSs).**

- **In light of the SFPALC's recommendation and the information in its report, would you expand on DoFA's reason (given in the report at page 17) for not requiring agencies to provide forward estimates in the PBSs?**

Response:

Finance's first submission noted (page 8) that the Government had considered the appropriate level of detail in the recording of forward estimates, and determined that there is already extensive reporting of forward estimates provided in the budget documentation. Forward estimates information is already provided at an aggregate level (cash and accrual) as well as for agency expenses, measures and on a functional basis. This information is published at the time of both the Budget and the Mid Year Economic and Fiscal Outlook.

The Government also noted that the purpose of the PBSs is to explain the annual Appropriation Bills before the Parliament. As such, forward estimates information by output and for each administered item (or by programme prior to the introduction of outcome-output budgeting) has never previously been included in the PBS, nor in the Explanatory Notes.

The PBS Guidelines represent minimum requirements for the document, across all portfolios. The guidelines do not prevent agencies responding to the particular information needs of individual committees in estimates or other contexts.

9. **The PBS does not currently provide forward performance information in addition to forward financial information. This does not assist members and senators to understand how agencies are performing today and how they expect to perform in the longer term.**

   - **Would you discuss the merits and feasibility of providing forward performance information in addition to forward financial information in the PBS?**

Response:

As mentioned in the answer to question 8 above, the Government's position is that the function of the PBSs is to explain the annual Appropriation Bills before the Parliament. Quantified performance information for the Budget year would indeed be useful where appropriate, and the Performance Management Principles encourage portfolios to identify, where appropriate, specific benchmarks, targets or activity levels, rather than unquantified performance information. However, in line with the Government' position on forward financial information, the publication of quantified performance information for the forward years would not be appropriate in the PBSs.

10. **On page 41, the SFPALC raised the difficulty of using the PBS or estimates process to examine whole of government issues. Examples given were:**

    - **the difficulty in linking ministerial cross-portfolio budget statements to the PBS;**
    - **regarding GST information expenditure senators had to approach individual agencies; and**
    - **consolidated information such as savings from IT outsourcing is not released by the consolidators because it 'belongs' to individual agencies.**

    **Apart from a Parliamentary committee or ANAO inquiry into whole of government activities, the SFPALC saw no immediate solution to the problem and invited comment.**

    - **Do you see any solution to the problem identified by the SFPALC?**

Response:

The Government commissions reports on a cross-portfolio basis as it considers necessary – a recent example is the report from the Reference Group on Welfare Reform, titled: Participation Support for a More Equitable Society. The Government also requests the Productivity Commission to report on matters which are often of a cross-portfolio nature.

There are also a number of Budget-related papers released each year, most of which deal with issues on a cross-portfolio basis. The 2001-02 Budget was accompanied by the release of papers dealing with matters affecting, for example, women, indigenous Australians, people in regional Australia, and our natural and cultural heritage.

Fundamentally, the PBSs are portfolio-specific documents, issued under the authority of the relevant portfolio minister and intended to meet the needs of the particular estimates committee covering the portfolio. The SFPALC's report acknowledged (p41) that neither the PBS nor the estimates process lend themselves well to an examination of whole-of-government issues.

It remains open to the Parliament to commission a Committee or ANAO inquiry into a specific whole-of-government matter of sufficient concern.

**11. Do any agencies have a MOU with another agency to deliver a shared outcome?**

- **If so, what arrangements are in place for performance measuring and external reporting in the PBS and Annual Report?**

Response:

Under the outcome-output framework, there are no outcomes shared between portfolios. There are, however, arrangements in place between agencies who enlist the assistance of others to achieve the portfolio outcomes required by government.

For example, several agencies have Business Partnership Agreements with Centrelink which contribute to the delivery of client agency outputs. This in turn contributes to the achievement of the relevant government outcome. The 1999-2000 Centrelink Annual Report identifies these various agreements and reports results against performance targets at pp 25-35. The purchasing agencies also report the results in their own annual reports (eg Department of Employment, Workplace Relations and Small Business 1999-2000 Annual Report, pp54-55).

**12. In its submission ACOSS drew attention to delays in being able to obtain copies of the PBSs.**

- **How practical would it be for PBSs to be readily available at the Government Bookshop and on the internet on Budget night as well as the lockups?**

Response:

Portfolio Budget Statements are available online following the conclusion of the Treasurer's Budget night speech.  They can be accessed via the Commonwealth Government Entry Point, Treasury's Budget web site, or through the individual websites of portfolio agencies.

The Government Info shops are open on each Budget night from 7.30pm to 9.00pm to retail the Budget papers.  They no longer carry PBSs as there has been a low demand for copies in recent years.

Portfolios are encouraged to make free copies of their PBS available to major client organisations and to the libraries of tertiary institutions.

**13. It has been suggested that the following could assist departments/agencies to accurately measure their outputs:**

- **develop a data dictionary of the terminology used in their outcomes and outputs framework;**
- **promulgate agency wide measurement methodologies and counting rules to ensure consistent measurement of performance measures particularly, where more than one functional area is involved in reporting agency performance; and**
- **set up appropriate audit trails to monitor progress against delivery of their outputs.**

– **Have you provided guidance to agencies concerning the above mentioned points relating to output measurement? If yes, could you provide a copy of the guidance provided?**

– **Do you already use some or all of the above methods? If yes, which ones?**

Response:

Outcomes and outputs guidance to agencies is primarily presented on the Finance website at http://www.finance.gov.au under the Government Finances banner.  The areas identified above are matters best addressed by CEOs in a manner appropriate to the operations of their agencies.  There is a range of private sector advisers offering performance management and audit services, and these issues are aired at conferences.

The PBS Guidelines include a dictionary of terms which is reproduced in all PBSs. Finance updates in an ongoing way its website guidance on specifying and reporting against outcomes, outputs and administered items.  This, together with ANAO guidance available and foreshadowed in the area of performance information, is considered an appropriate level of central guidance in the Commonwealth's devolved environment.

**14. The main aim of the CUC was to encourage agencies to recognise their assets and promote good asset management.**

- **Would you discuss whether in practice the CUC has been beneficial?**

Response:

The Capital Use Charge (CUC) is a first step in enabling agencies to understand the concept of there being a cost related to the use of capital resources. The net assets (equity) charging basis has been adopted as a process to include a cost of capital in the price of agency outputs and consequently lead to improved agency asset management.

The CUC was introduced as part of the Government's intention that agencies be put on a more businesslike footing. Improved financial management information incorporating accruals, and more active balance sheet management are both fundamental ingredients of the Commonwealth's approach.

While experience in other jurisdictions may have revealed that improvements in asset management practices as a result of capital charges have been limited, the CUC is one of a range of tools used by the Government to ensure improved financial practices within agencies. It remains important to ensure that the cost of capital used within each agency is included in the price of their outputs to facilitate comparison with other providers in the public and private sectors.

Together with other reforms, such as the publication of capital budget statements, early signs are that Commonwealth agencies are placing greater emphasis on balance sheet management.

**15. The ANAO stated in their submission that they raised with DoFA 'whether the capital use charge more accurately reflects a financing cost or charge imposed on agencies and is thus more appropriately disclosed as an expense.'**

- **Would you comment?**

Response:

There are two approaches to the treatment of the Capital Use Charge (CUC), firstly as an expense, above the operating result line or secondly, below the operating result line in the form of a dividend.

Finance has reviewed the merits of each of these alternative treatments. That review indicated that the current approach of treating the CUC as a dividend, instead of an expense, was conceptually correct. The rationale for this approach is that the CUC is a return on the Commonwealth's investment in an agency.

Treatment as an expense, on the other hand, would not be in line with this objective. Finance will liaise with the ANAO as part of the continuing refinement of policy in this area.

**16. From time to time agencies can achieve a significant operating surplus separate from the Capital User Charge. There appears merit in requiring agencies to specifically identify the details of any surplus to output level with explanations in the agency Annual Report which can be matched to the audited financial statements.**

- **Would you discuss the merits and feasibility of this proposal?**

Response:

Finance supports the reporting of financial performance and to that end, it supports the separate disclosure of the “true” operating position, net of any surpluses achieved in order to pay the CUC dividend. It remains open for the Government to require the payment of a dividend over and above that relating to the CUC.

The Finance Minister’s Orders 2001-02 relating to financial reporting will require the major revenue and expense items at the output (output group) level to be disclosed in the notes of agencies’ financial reports.

In addition, Finance is examining ways of achieving summary or concise financial reporting in Annual Reports. Separate disclosure of “true” operating results and surpluses achieved to pay the CUC will be considered as part of this review.

**JCPAA Review of Accrual Budget Documentation**
**Answers to Questions from Mr D. Cox, MP**
**at hearing on 22 June 2001**
**Department of Finance and Administration**
**26 July 2001**

**1. I was asking [Mr Bartos] in the last session about the breakdown of non-tax revenue which, in summary tables, is just a one-line item of $12 billion. For the purposes of the committee preparing a report, it would be helpful if Finance could send us a much more detailed breakdown of the $12 billion so that we could hazard our hand at suggesting some categories that they might subsequently report on.**

**Answer**: In referring to a one-line item in summary tables, Mr Cox may be citing Tables A1 and A2 at pages 5-24 and 5-25 in Budget Paper 1, 2001-02.

A more detailed breakdown of the $12 billion into seven categories of non-taxation revenue appears at Table 9 on page 5-21 of the same Budget Paper.

**2. [Could you advise] the number of line items then [under the previous budget framework] and the number of line items now.**

**Answer**: There were 633 line items in Appropriation Bills 1 and 2 for 1998-99 and 225 for 2001-02. In both cases items with nil values have been excluded.

**3. Can we get a list of all the non-financial asset sales for the last five years and all the sales of financial assets for policy purposes?**

**Answer**: Non-financial asset sales (for example, sales of excess plant and equipment, furniture etc) are matters for which individual portfolios are responsible. This dates back to the previous running costs system, under which from 1989-90 agencies had access to a negotiated portion of net proceeds from such sales. Finance understands that the Australian Bureau of Statistics has provided Mr Cox with information on the more significant sales of non-financial assets. If he requires further information, Mr Cox would need to approach individual agencies.

In respect of sales of financial assets, it is understood that the Australian Bureau of Statistics has already provided information to Mr Cox.