

Chapter 5

Improving transparency and specificity of budget documents

5.1 In this chapter the Committee discusses how the nature of the system of Commonwealth funding and expenditure is revealed in the presentation of the Budget and the Budget documents.

Previous parliamentary reports

5.2 Parliamentary committees in the past have reported on the adequacy of the explanatory material provided with the Budget.

Reports on the Portfolio Budget Statements

5.3 One of the Committee's predecessor committees, the Finance and Public Administration Legislation Committee, published three reports on *The Format of the Portfolio Budget Statements* in 1997, 1999 and 2000. In its third report, tabled in November 2000, that committee concluded, *inter alia*, that:

... the PBS are ... well-crafted documents which contain a wealth of useful information, once the reader has grasped the underlying concepts of accrual budgeting, budgeting processes, the reporting framework and reporting requirements. The PBS are not for the uninitiated.

They are evolving, however, and may eventually reach a point where they can more closely merge the government's aspirations for them as budgeting statements and senators' hopes for a simple, straightforward, user-friendly, yet detailed guide to the estimates.¹

5.4 The question regarding the adequacy of budget reporting was raised with the Auditor-General in this inquiry. He responded as follows:

I think the short answer is that this whole area is a journey rather than a destination. The system continues to evolve. We need to learn from the experience as we go. I think there are some areas that are worthy of attention. Our submission points out some of those areas, including, for instance, the description of the outcomes and the consistency of the use of outcomes across agencies and whether greater use of program information would assist senators in their work. There is the perennial issue of performance information. There is also the issue of the understanding of the financial management framework itself. I came into the room as Ms Campbell was speaking about Finance's plans, where appropriate, to try to

1 Senate Finance and Public Administration Legislation Committee, *The Format of the Portfolio Budget Statements: Third Report*, November 2000, p. 39.

simplify the financial framework, because in some areas it is complex and does require a level of detailed knowledge.²

Report on the accrual budget documents

5.5 In June 2002 the Joint Committee of Public Accounts and Audit (JCPAA) reported on a review of the accrual budget documents. Among its several other recommendations the JCPAA recommended that:

Agency outcome statements should:

Completely and clearly define their key objectives to reflect the impacts Government expects from their work;

Completely and clearly define the impacts Government expects from agency administered items; and

Accurately articulate the purpose of the relevant appropriations under the Appropriation Acts of the Commonwealth Budget.³

5.6 The Government agreed in principle with these recommendations and in its response to the committee's report on 13 May 2003 stated that Finance was developing Outcomes Principles that would require the development of more specific, less aspirational outcomes statements where appropriate.⁴

Reporting on forward estimates in the PBS

5.7 In the second report on the format of the PBS, the Senate Finance and Public Administration Legislation Committee recommended that forward estimates for outcomes and outputs should be included in the PBS.⁵ In its third report the committee again recommended that forward estimates be provided in the PBS, but only for administered items.⁶

5.8 The Government did not accept those recommendations because:

... there is already extensive reporting of forward estimates provided in the budget documentation. Forward estimates information is provided at an aggregate level (cash and actual) as well as for agency expenses, measures and on a functional basis. This information is published at both Budget and Mid Year Economic and Fiscal Outlook update.

2 Mr Ian McPhee, *Committee Hansard*, 8 September 2006, p. 36.

3 Joint Committee of Public Accounts and Audit, *Report 388 Review of the Accrual Budget Documentation*, June 2002, p. xxi.

4 JCPAA Report 388: Review of the Accrual Budget Documentation – Government response to recommendations of a policy nature, *Senate Hansard*, 13 May 2003, p. 10580.

5 Senate Finance and Public Administration Legislation Committee, *The Format of the Portfolio Budget Statements: Second Report*, October 1999, p. 28.

6 Senate Finance and Public Administration Legislation Committee, *The Format of the Portfolio Budget Statements: Third Report*, November 2000, p. 40.

The purpose of the Portfolio Budget Statements (PBS) is to explain the annual Appropriation Bills before the Parliament. As such, forward estimates information by output and for each administered item (or by program prior to the introduction of outcome-output budgeting) have never previously been included in the PBS, nor in the Explanatory Notes.⁷

5.9 The Committee agrees that one important purpose of the PBS is to explain the annual appropriations. This is manifested by the inclusion of specific reference to the documents in the Appropriation Acts, and particularly to the provision that declares that the PBS are relevant documents for the purposes of section 15AB of the *Acts Interpretation Act 1901*.⁸ However, the PBS also have other purposes, which should include informing the Parliament of the expected future levels of expenditure on particular budget measures. The Committee's predecessor committee stated:

Mr Murphy [a Finance official] responded that the focus of the PBS was the budget year. From a strictly budgeting viewpoint, this is correct. But as the committee has repeatedly pointed out, in approving the Appropriation Bills, senators have to satisfy themselves that previous expenditure has been wise. Were detailed forward estimates available in the PBS, they might disclose that, in two years' time, a given output required a huge injection of money, one explanation for which might be wastage or inefficiency in the past. At the very least, the proposed changing expenditure pattern would be worthy of examination.⁹

Committee's conclusions

5.10 The Committee is aware that much detailed information is provided in connection with the Budget, including some financial information for forward years, and it appreciates that much effort and many resources are needed to produce that information. The Committee also accepts that government provides that information in good faith in part to assist the Senate to perform its role in scrutinising government funding and expenditure. Nevertheless, this Committee, like the Senate Finance and Public Administration Legislation Committee, also considers that the provision of program level forward estimates for outcomes, outputs and administered items in the PBS would enhance the transparency and accountability of government for its funding

7 Senator the Hon. Christopher Ellison, Minister for Justice and Customs, *Senate Hansard*, 8 February 2001, p. 21745.

8 *Appropriation Act (No. 1)2006*, ss. 4(1).

9 Senate Finance and Public Administration Legislation Committee, *The Format of the Portfolio Budget Statements: Third Report*, November 2000, pp 16-17.

and expenditure,¹⁰ especially in view of the carry over of funds and programs to future years. (See Chapter 3, paragraphs 3.63 to 3.74.)

5.11 The Committee also notes that there is insufficient mapping of spending by agencies on particular programs between the Budget Papers and the PBS. Expenses are classified on two different bases. The PBS classify expenses by outcome. Budget Paper No. 1 classifies by function or purpose. The two are not reconciled. Transparency is further reduced where responsibilities sit across portfolios. For example, spending on the Housing and Community Amenities function and the three sub-functions¹¹ traverses programs in the portfolios of Defence, Transport and Regional Services and Family and Community Services. There are no program descriptions. Instead, users have to try their luck hunting programs through at least three different sets of PBS.

Recommendation 11

5.12 The Committee recommends that a common approach be taken for the Portfolio Budget Statements and that estimates for three forward years be included for departmental and administered items at the program level. This should be able to be referenced back to functional and sub-functional splits in the other Budget papers.

Formulation of statement of outcomes

5.13 It seems to have been widely accepted by most observers, including by Parliamentarians, ever since the Government decided to adopt the accrual-based outcomes/outputs framework from the 1999-2000 Budget that appropriating moneys according to outcomes, with departmental outputs and administered items contributing to the achievement of those outcomes, would emphasise *performance* rather than *process* in the public sector and would increase accountability.¹²

5.14 Professor Bartos submitted that:

The transition to outcomes/outputs accrual budgeting in 1999-2000 was accompanied by further significant changes in budget reporting. Some of these added to transparency and accountability: in particular, information is now available on assets and liabilities, changes in the net worth of government can be monitored, and there is now consistency between the

10 In its recent report on the application of the outcomes and outputs framework ANAO also has suggested that the provision of forward estimates on the basis on which Parliament appropriates funds should be further considered in any future review of the framework. Australian National Audit Office (ANAO), *Application of the Outcomes and Outputs Framework*, Audit Report No. 23 2006-2007 p. 93.

11 See *Budget Paper No. 1 2005-2006*, pp 6-13.

12 See, for example, Australian National Audit Office, *Submission 4*, p. 9.

reporting structure in the budget papers and departments'/agencies' Annual Reports.¹³

5.15 But as pointed out in a Research Paper published by the Commonwealth Parliamentary Library in 2002:

... there is an apparent paradox. The adoption of an accruals-based system of accounting makes the Executive's financial activities more transparent to the Parliament in its role of holding the Executive more accountable for those activities *after the event*. Yet the supposedly necessary complementary changes to the appropriation structures, wherein the Parliament's authority is given *before the event* for the Executive's financial activities, may actually have diminished Parliament's capacity to control the Executive in the way the Constitution envisaged.¹⁴

5.16 The current situation contrasts with that in earlier times:

Although Parliament was presented with a detailed list of intended budgetary spending, in practice there was little or no management information on what or how resources were expended. The system was strong on *ex ante* controls but weak on expenditure management...¹⁵

5.17 To the extent that Parliament's capacity to control the spending of the executive has been diminished, this appears to have resulted from the current structure of the annual Appropriation Acts and in particular the outcomes/outputs presentation of proposed expenditure.

5.18 The JCPAA has registered concern about the broad formulation of outcomes. In its 2002 report the committee stated that:

The Committee highlighted several examples of poor output and outcome definitions during the public hearing. There was concern that the outcome statements were too broad and far reaching, whilst some output statements were difficult to comprehend.¹⁶

5.19 Professor Geoff Lindell submitted that '... the statement of outcomes can frequently be so open ended as to cease to be a meaningful description of the purpose of any expenditure'.¹⁷

13 Professor Stephen Bartos, *Submission 5*, p.2.

14 Maurice Kennedy, *Cheques and Balances: Research Paper No. 16 2001-2002*, Department of the Parliamentary Library, p. 34.

15 John Wanna, Joanne Kelly & John Forster, *Managing Public expenditure in Australia*, Allen & Unwin, St Leonards, NSW, p. 301.

16 Joint Parliamentary Committee of Public Accounts and Audit, *Report 388 Review of the Accrual Budget Documentation*, June 2002, p. 11.

17 Professor Lindell, *Submission 10*, p. 9.

5.20 Professor Lindell observed that a need for greater specificity of purposes is not inconsistent with the need for flexibility. He suggested that a category of departmental expenditure could be drafted that would describe running and regular expenditure for items of expenditure that are not thought to require detailed itemization. These items could include the acquisition of office furniture and stationery and the payment of salaries. Professor Lindell submitted that this category of expenditure should not include departmental expenditure which is capable of being identified by reference to the nature of the policies promoted and implemented by an agency.¹⁸

5.21 ANAO pointed out that broad statements of outcomes allow budget-funded agencies to attribute particular activities or programs to more than one outcome and that this reduces the information value of nominated outcomes to Parliament. This was highlighted in ANAO's recent audit of the Roads to Recovery Programme administered by the Department of Transport and Regional Services.¹⁹ In that case, payments that related to the transport outcome were subsequently reported against the regional services outcome so as to prevent the department being reported for breaching Section 83 of the Constitution.

5.22 In its supplementary submission, ANAO suggested that if there were greater specification of the purposes of appropriations in Appropriation Acts (for example through greater specification and/or the number of outcomes) the potential for this type of cross-outcome program attribution might be reduced.²⁰

5.23 Broad formulation of outcomes may lead to further obfuscation of the government's accountability to the Parliament even with regard to administered expenses. In this context, Maurice Kennedy wrote:

Under the terms of an annual appropriation, an entity is allowed to switch its operating capacity resources (Departmental Outputs) between Outcomes, but not its 'deliveries' (Administered Expenses): those appropriated amounts can only go to the recipients covered by that particular Outcome. However ... the Outcomes for Administered Expenses are often expressed so broadly that they do not impose particularly strict legal limits on the purposes for which the appropriated amounts may be applied.²¹

5.24 ANAO submitted that:

The experience to date suggests that there would be merit in further reviewing the breadth and presentation of outcome descriptions; and

18 Professor Lindell, *Submission 10*, p. 9.

19 Audit Report No. 31 of 2005-2006, *Roads to Recovery*, Australian National Audit Office, 1 March 2006.

20 ANAO, *Supplementary Submission 4b*, [p. 12.]

21 Maurice Kennedy, *Cheques and Balances*, Research Paper No. 17 2001-02, Department of the Parliamentary Library, 28 May 2002, p. 40.

examining whether the greater use of programme-level information would assist Parliament in its work, and improve the transparency and accountability of Commonwealth public funding and expenditure'.²²

5.25 In its recent report on the application of the outcomes and outputs framework ANAO recommended that agencies incorporate periodic reviews of outcomes into their business or budget planning processes with the aim of ensuring that outcome statements are sufficiently specific and enable the identification and measurement of an agency's contribution to the achievement of outcomes.²³

5.26 Professor Bartos submitted that the Committee should:

Recommend to the executive that the Minister for Finance and Administration be delegated a power to require outcomes descriptions to be expressed in clear, simple and measurable terms. In practice, this power would be exercised by his department in negotiations with other departments, and could be expected to result in considerable improvement in budget transparency...²⁴

5.27 With regard to the specificity of outcomes Finance informed the Committee that it was:

In a process of continuing improvement in assessing outcomes to determine whether or not they provide the parliament and the people with an appropriate level of detail and [was] working with agencies to refine their outcome descriptions as well as performance indicators that go with those outcomes.²⁵

Committee's conclusions

5.28 The Committee has concluded that the broad formulation of outcomes has accompanied a loss of program detail and specificity in the appropriations processes of the Parliament. This poses challenges for parliamentary scrutiny. Outcomes must be more precisely and meaningfully specified in the appropriations bills and in all other budget documentation. There is also a need for cross-agency consistency of performance with measures of cost, quality and timeliness. Systematic evaluation of results against targets also needs to be built into budgeting processes, including through active involvement of Finance.

22 Australian National Audit Office, *Submission 4*, p. 23.

23 Australian National Audit Office (ANAO), *Application of the Outcomes and Outputs Framework*, Audit Report No. 23 2006-2007, p. 31.

24 Professor Stephen Bartos, *Submission 5*, p. 11.

25 Ms K Campbell, *Committee Hansard*, 8 September 2006, p. 21.

Recommendation 12

5.29 The Committee recommends that outcomes be expressed in clear, simple and measurable terms and that the Department of Finance and Administration play an active role in improving and evaluating the quality of outcomes.

Program-level expenditure information

5.30 Witnesses suggested that one way of ensuring that the Parliament is presented with a greater level of detail in the Appropriation bills and the supporting documentation is by the use of program-level information.

5.31 ANAO, for example, suggested that the greater use of program-level expenditure information might assist parliament in its work. Reference has also been made earlier in this report to suggestions that financial reporting in the budget documents should be according to programs, and that the current outcomes/outputs reporting should be at a level that the public and ministers commonly understand as programs.²⁶

5.32 The Committee was informed that the government already collects expenditure information at this level for its own internal purposes. ANAO informed the Committee that:

There have been recent moves to increase the use within government of programme-level information and controls. For example, additional internal reporting requirements, particularly in relation to programme information, have been established to provide better information for decision-making. Similarly, programme level controls also exist for funding of long-term commitments by some Departments (in accordance with Regulation 10 of the Financial Management and Accountability Regulations 1997).²⁷

5.33 Also in relation to programs, Finance informed the Committee that:

The need for a greater range of information below outcome level was recognised in the Budget Estimates and Framework Review (BEFR) in 2002, with the decision being made by Government at that time that agencies would be required to develop and submit programme information.

The introduction of the Central Budget Management System (CBMS) has assisted agencies to submit this information in a more comprehensive form, and Finance is still evaluating the quality of the data. The decision to publish programme information is one for the Government to make. However, once quality issues are addressed Finance will be in a position to advise the Government on options for greater use, including publication, of programme information.²⁸

26 See Professor Bartos, *Submission 5*, p. 11.

27 Australian National Audit Office, *Submission 4*, p. 23.

28 Department of Finance and Administration, *Submission 4b*, [p. 5.]

5.34 Professor Bartos made the following suggestions for change:

Either a) seek reporting on the program information currently used for budget decision making or b) a preferable option, break the current outcomes/ outputs structure down to a level that corresponds to what the public and ministers commonly understand as programs.²⁹

5.35 As the Committee has reported earlier, in Chapter 2, ANAO recommended in its recent report on the application of the outcomes and outputs framework that Finance consider opportunities for improvement that relate to better integration of programs into the outcomes and outputs framework, including developing criteria to guide agencies' decision-making on the inclusion of program information.³⁰

5.36 Bearing in mind that program level information is capable of being reported from the CBMS³¹ the Committee suggests that the budget documents might be presented as shown in Appendix 3 at outcomes, outputs and program levels. Presentation of the government's finances in this or a similar form would assist senators and others in their scrutiny of the annual budget and would thus enhance transparency.

5.37 ANAO submitted that a key issue in any move to greater use of program-level information and controls would be a sound approach to identifying individual programs:

A reasonable principle to adopt would be to identify distinguishable components (an approach that is advocated by the accounting standard on segment reporting) so as to focus on major and significant programmes. Another useful guide ... would be the breakdown that the agency uses for its own executive decision-making.³²

5.38 The Auditor-General suggested that care should be taken not to require universal presentation of program information:

It needs to be appropriately targeted so that it assists the parliament. You will remember that in the old program budgeting days we used to have programs for corporate services.³³

5.39 Although it might be asserted that program budgeting had been tried and had failed, Wanna et al were of the view that:

During the 1980s the quest to adopt program budgeting took on something of a 'holy grail' with officials treating the term as an incantation – a

29 Professor Bartos, *Submission 5*, p. 11.

30 Australian National Audit Office (ANAO), *Application of the Outcomes and Outputs Framework*, Audit Report No. 23 2006-2007, p. 31.

31 See Ms Campbell, *Committee Hansard*, 8 September 2006, p. 20.

32 ANAO, *Supplementary Submission 4b*, [p. 12.]

33 Mr McPhee, *Committee Hansard*, 27 November 2006, p. 9.

miraculous salvation for the ills of public finance. The 'implementation' of program budgeting remains one of the great myths of the recent era of Australian public sector management. It cannot be said that it was ever discontinued, because despite the rhetoric it was never implemented in the first place.³⁴

Committee's conclusions

5.40 The Committee has concluded that the presentation of program-level information in the Appropriation Acts and in the other budget documentation should lead to greater specification of the objectives of proposed expenditure and hence greater transparency and should be implemented. The evidence and in particular redevelopment of Finance's budgeting systems indicate that presentation of expected and actual expenditure as well as forward estimates on this basis is feasible, and a system of program reporting could be implemented relatively quickly and easily. The Committee considers that presentation of information on this basis should also improve accountability because it should be more focussed and therefore more comprehensible.

Recommendation 13

5.41 The Committee recommends that expenditure should be reported at the levels of programs in the budget documents, including in the schedules to the Appropriation Acts.

Departmental outputs and administered expenses

5.42 The terms 'departmental' and 'administered' are not defined in the Appropriation Acts.³⁵

5.43 The Committee was informed that 'departmental' and 'administered' are defined in Finance Minister's Orders and those definitions have been refined over time, but ANAO indicated that it might be beneficial if the expenditure that is 'departmental' and expenditure that is 'administered' were explicitly addressed in the Appropriation Acts.³⁶ ANAO also informed the Committee that the Australian Accounting Standards Board (AASB) is undertaking work that relates to the distinction between 'administered' and 'controlled' items and how they should be accounted for.³⁷

34 John Wanna, Joanne Kelly & John Forster, *Managing Public Expenditure in Australia*, Allen & Unwin, St Leonards, NSW, p. 304.

35 'Administered item' and 'departmental item' are defined respectively in the Acts by reference to an amount set out in the Schedule under 'Administered Expenses' and as the total amount set out under 'Departmental Outputs'.

36 ANAO, *Submission 4*, pp 14-15.

37 ANAO, *Supplementary Submission 4b*, [p. 9.]

5.44 ANAO submitted examples of difficulties that agencies have encountered as a result of the apparent confusion surrounding the interpretation of these items. One department in 2002-2003 had reclassified expenditure appropriated as a departmental output as an administered expense; others had drawn (erroneously) on administered items to meet the departmental costs of administering those same items; and appropriations for similar activities undertaken by different agencies have been allocated differently, either as departmental outputs or administered expenses.³⁸

Committee's conclusions

5.45 Obviously there is an element of confusion surrounding the allocation of expenses as departmental or administered, and that confusion must necessarily be reflected in the documentation provided to the Parliament. This in turn will adversely affect the transparency of government funding and expenditure. The Committee considers therefore that this issue should be resolved swiftly and trusts that the work of the AASB will assist in this regard. However, given the progress made by that body on the harmonisation of accounting standards, the Committee questions whether the government should necessarily await the AASB findings before moving to alleviate the confusion that apparently exists.

5.46 The Committee considers that when a reasonable consensus is reached on the definitions of 'administered' and 'departmental' that those definitions should be explicitly addressed in the Appropriation Acts.

Recommendation 14

5.47 The Committee recommends that the terms 'administered' and 'departmental' be defined in the appropriation bills or other appropriate documents.

Accounting standards

5.48 The Committee was informed that the use of two different accounting standards and inadequate cash reporting lead to confusion and a waste of resources.

5.49 Professor Bartos submitted that the adoption of accruals led to the unnecessary duplication of reporting in the budget papers against two accounting standards: Government Financial Statistics (GFS) and Australian Accounting Standards (AAS). In his submission Professor Bartos touched on the strengths and weaknesses of both standards but concluded that:

There can be unproductive debates over the details contained within reporting standards that make not the slightest differences to decision making, accountability or transparency.³⁹

38 ANAO, *Supplementary Submission 4b*, [pp 9-10.]

39 Professor Bartos, *Submission 5*, pp. 7-8.

5.50 Professor Bartos concluded that the standard itself is not important; what is important is that one standard be adopted and applied consistently so that reliable estimates of trends can be reported. He submitted that there is currently an attempt being made to harmonise the AAS and GFS standards and that harmonisation would be a highly desirable outcome. In the meantime in his view the best approach would be to adopt just one of the two.⁴⁰

5.51 Mr Harris submitted that having two accounting standards leads to confusion. He asserted that the Parliament is entitled to impose its own choice on what standard the executive should use to report to Parliament:

If Parliament insisted, as it can, that GFS be used by Commonwealth departments and other government reporting entities, the cost of duplicated reporting would be eliminated and the clarity of government reporting would be enhanced.⁴¹

5.52 Professor Barton has written that:

The present system of accounting in the Australian Government is untenable with the presentation of two sets of accrual budget statements and outcome financial statements which show very different results for all components; and secondly, the absence of CABS [Cash Accounting and Budgeting System] which is needed for fiscal policy purposes, appropriation bills and good cash management. In principle, the solutions are obvious ones, i.e. –

a) the reintroduction of CABS as a subset of AABS [Accrual Accounting and Budgeting Systems] for the direct recording and timely reporting of cash transactions as occurred prior to 1999; and

b) harmonisation of the sound features of AAS [Australian Accounting Standards System] and GFS [Government Finance Statistics System] into one combined, robust accrual accounting FMIRS [Financial Measurement Information and Reporting System] system which is based on the GFS model and is relevant for the public sector.⁴²

5.53 Professor Barton submitted that if agreement is not reached shortly by the AASB the GFS system, as modified according to the recommendations of the HoTARAC [Hheads of Treasury Accounting and Reporting Advisory Committee] Committee, be adopted. He noted that the implementation of that system would require an amendment to the Charter of Budget Honesty Act 1998.⁴³

40 Professor Bartos, *Submission 5*, p. 8.

41 Mr Harris, *Submission 7*, p. 4.

42 Professor Barton, *Accrual Accounting and Budgeting Systems Issues in Australian Government, Submission 8a*, p. 22.

43 Professor Barton, *Submission 8*, p. 1,

5.54 Professor Barton also submitted that budgeting and financial reporting of administered items would be simplified if they were reported on a cash basis, and commented that, 'They are normally cash transfers and they would be more easily understood as such'.⁴⁴

5.55 Professor Barton informed the Committee that it 'would be easy for Parliament to follow each set of budget statements if the full cash budget statements are presented, and are then adjusted for below-the-line non-cash accrual items'.⁴⁵

Committee's conclusions

5.56 Witnesses acknowledged that the current use of two different accounting standards for the budget documents is at least potentially confusing and supported the harmonisation exercise that is underway. They also acknowledged that the harmonisation exercise has taken some time. The Committee considers that the sooner this matter is finalised the better because any confusion must inevitably lead to less transparency than would otherwise be the case. There were suggestions that if a standard were not agreed upon within twelve months, that the Parliament should unilaterally declare that the budget documents brought before must conform to one standard, and that this standard should be based on the GFS system.

5.57 The Committee shares the frustration of those who have advocated this course and will revisit the issue if significant progress towards a single agreed standard has not been reported within twelve months from the time of the tabling of this report.

Recommendation 15

5.58 The Committee recommends that the ongoing process being undertaken to harmonise the accounting standards should continue and should be expedited by the Government setting a deadline for its completion.

Other suggestions for improved transparency

5.59 Professor Bartos made a number of other suggestions for changes to the Budget documentation that he considered would result in greater transparency. These included the provision of better functional information in Budget Paper No. 1; the provision of more functional information in the estimates reconciliation table in Budget Paper No. 1; and publication of time series and graphs on trends in net worth, together with an explanation for those trends.⁴⁶

5.60 ANAO commented on the above suggestions as follows:

Some of the other additional information being advocated ... may provide additional information for some users but may not be of information value

44 Professor Barton, *Submission 8*, p. 3.

45 Professor Barton, *Correspondence*, 28 August 2006.

46 Professor Bartos, *Submission 5*, pp 11-12.

to many Parliamentarians. The Budget Papers are already voluminous, and ANAO is unaware of the extent to which Parliamentarians require the additional information suggested.⁴⁷

Committee's conclusions

5.61 The Committee considers that these matters of detail are probably best left for the consideration of the different Legislative and General Purpose Committees when they are examining the estimates. The committees may wish to note the suggestions and determine in the light of their experience whether their adoption would assist them in their work.

Reporting on budget, financial and public sector reform

5.62 Professor Bartos submitted that there is virtually no information in the public domain on what (if any) financial management improvement projects are underway within government.⁴⁸

5.63 ANAO agreed that there is value in the early signalling of proposed changes to the financial framework but suggested that the amount and rate of change has reduced in recent years as the framework has stabilised and that there is no need for such disclosure.⁴⁹

Committee's conclusions

5.64 The Committee accepts that it is possible that as the accruals based outcomes/outputs framework has matured that there has been a perception within government that there is little need for review and reform. If senators were concerned that insufficient work has been undertaken (or published) they could raise the issue in the context of the estimates processes.

5.65 There is an ongoing need to ensure that accountability deficits do not arise from the implementation of the current framework.

Treatment of depreciation

5.66 Professors Barton and Bartos and Mr Harris commented adversely on the current treatment of depreciation expenses in the Commonwealth Budget.

5.67 Mr Harris submitted that the Parliament's loss of control over the appropriations can be seen in many areas, including in the provision of appropriations for depreciation. He noted that the appropriations made for depreciation seem to have neglected that at the outset of the new financial arrangements, the Parliament had

47 ANAO, *Supplementary Submission 4b*, [p. 13.]

48 Professor Bartos, *Submission 5*, p. 13.

49 ANAO, *Supplementary Submission 4b*, [p. 16.]

already provided the funds to acquire the assets being depreciated. Appropriating for depreciation reimburses the government for appropriations it has already received.⁵⁰

5.68 Professor Bartos suggested that there has been double dipping – agencies may be being funded for depreciation while still receiving additional funds for new assets. He submitted that it now appears that many agencies are not making provision for replacement of assets, and are still seeking supplementation when they need to replace assets or make system replacements or upgrades. He cited the Customs replacement IT system as an example.⁵¹

5.69 Professor Bartos concluded as follows:

It would be desirable for the Auditor-General to be asked to report on whether agencies have misused depreciation funding, and if there is supporting evidence that they have, for this component of departmental funding to be withdrawn.⁵²

5.70 Professor Barton submitted that depreciation charges should not be directly funded in the budget because:

While they are necessary accounting charges for the use of physical assets in the outcome statements, funding them directly creates confusion and complications with respect to the accountability for the expenditure of budget appropriations. Rather, gross capital expenditure should be separately reported and budgeted for as required, with a subdivision of expenditures between asset replacement (i.e., the depreciation component), and asset expansion. This methodology has the effect of funding depreciation charges each year only as required for replacement purposes in that year. This is useful information for Parliament and management. *As well, it would avoid the questionable practice of departments building up internal cash balances for future asset replacement or whatever other purpose they may use to spend the funds on.* Also in practice, the lifespans over which costs are allocated for long life assets may bear little relationship to reality, and the annual depreciation charges can be, ‘soft’ figures. Lifespans are greatly affected by obsolescence, repair and maintenance, and general management of the asset. These matters are not given much consideration in determining asset lifespans for depreciation purposes.⁵³ (Committee's emphasis)

5.71 Professor Barton informed the Committee that:

I make a point in my paper with respect to some of the allocations to departments for depreciation purposes. I can give you probably two very good examples. The National Museum of Australia depreciates some of its

50 Mr Harris, *Submission 7*, pp. 1-2.

51 Professor Bartos, *Submission 5*, p.13.

52 Professor Bartos, *Submission 5*, p.13.

53 Professor Barton, *Submission 8*, p. 3.

collection items over 5,000 years. They happen to be rocks. I assume Geoscience Australia does the same—Geoscience has a very large collection of rocks. Is it appropriate to fund those depreciation charges? I would say not.⁵⁴

5.72 ANAO commented on the evidence given by other witnesses as follows:

Budget Paper 4 2006-2007 states (page 4) that expenses typically included in Departmental Outputs appropriations include operational expenses including depreciation. Accordingly, as depreciation funding is not separately identified, or funded, the use of such amounts is not restricted to asset replacement. Because depreciation funding for asset depreciation can be significant and asset replacement expenditure often occurs in large amounts at irregular intervals, it would be open to Finance and the Government to consider approaches such as that outlined by Professor Barton.⁵⁵

5.73 Finance submitted that it continues to review the framework and its different aspects and will examine the issues raised by Professor Barton.⁵⁶

5.74 ANAO has also noted that the funding of depreciation is an issue in any consideration of the Compact of 1965, especially in relation to the matters that should be included in appropriations bill No. 2.⁵⁷ The Compact of 1965 has been discussed elsewhere in this report.

Committee's conclusions

5.75 The evidence suggests that there are problems with funding for depreciation in the current framework. Funding for depreciation, particularly for replacement purposes, is opaque. The Committee has recommended earlier in this report that the Government should consider whether funds should continue to be appropriated for depreciation. In that context, the Government should also consider new approaches that would result in greater transparency and, in particular, should consider the approach suggested by Professor Barton.

Recommendation 16

5.76 The Committee recommends that the Government should give consideration to a system for funding depreciation whereby gross capital expenditure would be separately reported and budgeted for as required, with a subdivision of expenditures between asset replacement (i.e. the depreciation component) and asset expansion.

54 Professor Barton, *Committee Hansard*, 12 October 2006, p. 23.

55 ANAO, *Supplementary Submission 4b*, [p. 20.]

56 Department of Finance and Administration, *Supplementary Submission 4b*, [p. 7.]

57 ANAO, *Supplementary Submission 4b*, [p. 20.]

Portfolio Budget Statements

5.77 The extensive and detailed explanatory documents that are tabled with the Budget documents and are now known as Portfolio Budget Statements (PBS) have evolved from the explanatory material first provided by some ministers to the early estimates committees. The PBS in their various guises, eg Explanatory Notes, Program Performance Statements or Portfolio Budget Measures Statements, have often been commented upon not only by committees considering the estimates but also by other committees, including one of this Committee's predecessor committees.

5.78 Those committees generally have been interested in the format of the PBS or in their adequacy as explanatory documents.

5.79 The legal status of the documents is significant. In 2002, when he was considering the legal implications of the sections in the Appropriation Acts that declare that the PBS are relevant documents for the purposes of section 15AB of the *Acts Interpretation Act 1901*, Maurice Kennedy made the following observations:

The important point is that the PBSs, when read with the relevant provisions of the Appropriation Act, do not impose any additional legal restriction on the purposes to which an entity may apply amounts appropriated to it under an annual Appropriation Act so long as such a purpose is not inconsistent with the terms that describe the entity's outcome(s). Consequently, there seems to be no legal impediment to the Executive's undertaking, during the course of a financial year, *totally new or expanded activities* which had not been foreshadowed to Parliament in the PBSs. Provided that the new or expanded activities were, in some way, related to the achievement of a described outcome, and their costs could be accommodated within the total appropriation provision for that outcome, Parliament may not be formally aware of the matter until details were later revealed in the entity's annual report and financial statements.⁵⁸

5.80 The PBS provide a wealth of information but their value as documents for informing the Parliament as to how funds will be spent is problematic. ANAO informed the Committee that:

- Whilst the PBS provide considerable additional material in respect of departmental outputs, the amounts are not required to be spent in the manner identified in the PBS (as outlined in *Combet v Commonwealth of Australia*);
- For administered expenses, generally less detail is provided in the PBS than for departmental items. Further, whilst an administered appropriation may be used for any or all of the activities mentioned for that item in the PBS, its use is not restricted to those activities mentioned in the PBS; and

58 Maurice Kennedy, *Cheques and Balances*, Research Paper No. 17 2001-02, Department of the Parliamentary Library, 28 May 2002, pp 40-41.

- Notwithstanding the additional detail provided, the final appropriation sources may not be certain, especially where outcomes are specified so as to overlap with the purposes of other funding sources, such as special appropriations.⁵⁹

5.81 ANAO accepts that the PBS have value as accountability documents, in that they set out performance measures and statements of expected performance, with the results of that performance being reported later in annual reports. However, ANAO has found through its audit activities that in certain cases the PBS have not provided a good indication of how some appropriated funds will actually be used by entities. ANAO referred in particular to its audits of the Management of Net Appropriation Agreements and the Financial Management of Special Appropriations, which have been discussed earlier in this report.⁶⁰ ANAO also referred to a finding in its report on the Post Sale Management of Privatised Rail Business Contractual Rights and Obligations that:

... the PBS reporting of FACS [Department of Family and Community Services] had consistently over-estimated the amount of funding required to pay the purchaser of the passenger rail business for concessional rail travel.⁶¹

Committee's conclusions

5.82 As mentioned earlier, one of the Committee's predecessor committees considered in depth the content and format of the PBS. Apart from making the above observations the Committee does not propose to comment further in this inquiry, but suggests that the Senate Legislative and General Purpose Committees in their consideration of the estimates should report on the format and content of the PBS of the portfolios that are referred to them. The committees might, for example, comment on the specificity of the definition of outcomes. They might also attempt to determine expenditure on outcomes (or programs) and compare that expenditure with the estimates set out in the PBSs. While this would be accounting for expenditure after the event, such an exercise would enable committees to gauge the accuracy of previous PBS estimates and provide a measure by which new PBS estimates could be tested and assessed.

Contingency reserve

The contingency reserve is a global reserve which is supposed to allow for: amounts not yet allocated to individual programs; the tendency to underestimate costs of

59 ANAO, *Submission 4*, pp 24-25.

60 ANAO made recommendations with regard to PBS performance indicators in its report on the outcomes/outputs framework which has also been discussed earlier in this report. (See Australian National Audit Office (ANAO), *Application of the Outcomes and Outputs Framework*, Audit Report No. 23 2006-2007, p. 31.

61 ANAO, *Submission 4*, p. 25

existing programs in future years; and the tendency to overestimate administered item expenses in the early years as the programs get up to speed. The Committee considers that the transparency of the contingency fund could be improved by production of a reconciliation table by sub-function for changes across the forward estimates. This would be produced in the Budget and in the Mid Year Economic and Fiscal Outlook.

