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Efficiency Through Contestability Programme

No.41 2017–18

Cross Entity:

Department of Finance, Department of Jobs and Small Business, Department of Health, Department of Foreign Affairs and Trade, Department of Social Services, Comcare, Department of Veterans' Affairs, Department of Agriculture and Water Resources, Australian Public Service Commission, Attorney-General's Department, Australian Bureau of Statistics, Australian Federal Police, Australia Sports Anti-Doping Authority, Australian Taxation Office, Australian War Memorial, Bureau of Meteorology, Department of Education and Training, Department of Environment and Energy, Department of Home Affairs, Department of Human Services, Department of Industry, Innovation and Science, Department of Infrastructure, Regional Development and Cities, Murray Darling Basin Authority, Department of Prime Minister and Cabinet, and Department of the Treasury.

Background

1. In 2014–15, the Government introduced the Efficiency through Contestability Programme (the Programme) led by the Department of Finance (Finance). The Programme aimed to apply the most efficient way of designing and delivering government policies, programmes and services. The Programme was part of a Contestability Framework, which first considered whether government should deliver a function, and then assessed whether a function should be open to competition and the appropriate means for this to occur.

2. Under the Framework, a Contestability Programme Steering Committee developed and recommended a programme of work for Contestability Reviews, Functional and Efficiency Reviews, and Portfolio Stocktakes. Also under the framework:

- the Minister for Finance was to approve the programme of work, which was intended to progressively cover all areas of government;
- responsible Ministers, with the support of their entities, were to ensure the completion of planned reviews and make recommendations to Government on review outcomes, implementation arrangements and cessation of functions; and
- reviews were to provide the public sector and government with a robust evidence base to inform and guide its decision making.

3. After commencing a pilot in 2014, Finance implemented the Programme in 2015 and published supporting *Contestability Programme Guidelines*. The Programme ceased on 30 June 2017, although as envisaged at the outset of the Programme, implementation of many review recommendations by responsible entities was ongoing. In May 2017, the Minister for Finance observed that most portfolios had been reviewed through the Programme and that 'Functional and Efficiency Review outcomes have achieved savings of around \$5 billion from 2014–15 to 2020–21'.

Audit objective and criteria

4. The objective of the audit was to assess the effectiveness of the Efficiency through Contestability Programme in supporting entities to improve the efficient delivery of government functions. The criteria were:

- the Department of Finance effectively designed, administered and supported the oversight of the Programme;
- all reviews supported entities to design initiatives to improve the efficient delivery of government functions and make recommendations to Government (through the responsible Minister) on implementation arrangements; and
- selected entities have implemented agreed initiatives as planned and have monitored and reported on achieving planned financial and non-financial efficiency gains to Finance and the responsible Minister.

Conclusion

5. The Efficiency through Contestability Programme was effective in supporting entities to review the efficient and effective delivery of government functions. The Programme has produced many recommendations to improve the efficiency of administrative systems and, to a lesser extent, the contestability and means of delivering government functions. Substantial Budget savings have arisen from the Programme, although entities have not yet demonstrated the extent of efficiency and performance improvements supporting those Budget savings. Entities would benefit from developing performance measures that capture improvements in efficiency over time—such as through the use of baselines or benchmarks.

6. Finance effectively designed, administered and supported the implementation of many elements of the Programme. The department's planning was sound and it provided adequate support and guidance to entities conducting reviews. Finance undertook planned evaluation, and in December 2017 concluded that the Programme supported Budget repair in excess of \$5 billion over the forward estimates. Finance could have provided the Contestability Programme Steering Committee with more support to determine whether Functional and Efficiency Reviews met their terms of reference.

7. While often not following Programme guidelines, the reviews made a large number of recommendations to improve delivery of government functions and/or increase operational and administrative efficiencies, but did not often propose market based improvements. Many recommendations have been accepted or are being considered by Government, and the projected total net savings to Budget greatly exceed the cost of conducting the reviews.

8. Virtually all projected Budget savings from the Programme are from the four reviews whose implementation of recommendations was examined in detail in this audit.¹ There has been divergence between entities in implementing recommendations against plans. Monitoring has focused on implementation progress, with little evaluation of whether savings from implementing recommendations are based on efficiency improvements rather than reductions in services or other outputs. Entity reporting to Finance has been mainly through the Budget process that focuses on net changes to appropriations.

¹ The ANAO examined four reviews to determine whether agreed recommendations had been implemented as planned. These were Functional and Efficiency Reviews of the Department of Foreign Affairs and Trade, Department of Health, Department of Social Services, and Management of the Commonwealth's Insurable Risk Contestability Review that involved Comcare and the Department of Employment.

Supporting findings

Administration of the Programme by Finance

9. To support the implementation of the Programme, Finance developed a programme implementation plan and programme guidelines, established governance arrangements including clear roles and responsibilities, conducted risk analyses and provided support and guidance to entities undertaking reviews on the limited occasions this was requested. In line with initial planning, support and guidance arrangements were focused on the conduct of reviews, with lesser coverage of the implementation of recommendations.

10. Finance supported the Contestability Programme Steering Committee to effectively carry out some but not all of its roles for the Programme. The department supported the Committee to provide strategic guidance and direction, consider the forward work programme and report on the progress of individual reviews and the Programme, but not to clearly determine whether Functional and Efficiency Reviews met their terms of reference. Finance provided administrative support for Committee meetings, including by preparing briefing papers, although it did not maintain records of decisions and action items for many meetings.

11. Finance undertook the majority of the monitoring and evaluation required under the Programme Implementation Plan. In particular, it regularly monitored individual reviews, monitored savings and analysed themes in recommendations across Functional and Efficiency Reviews, identified lessons learned and prepared a Programme Evaluation Report in December 2017. Finance has not evaluated Contestability Reviews completed after the pilot phase or undertaken a structured evaluation of Functional and Efficiency Reviews. Finance considers that the Programme has positively contributed to Budget repair, efficiencies, effectiveness and supporting Government decision making. However, the department has had limited visibility of the implementation of recommendations from reviews, which has diminished the extent to which conclusions can be drawn about improvements in efficiency and effectiveness. In early 2018, Finance was undertaking a stocktake of the implementation of review recommendations, to inform the Minister for Finance about the outcomes of the Programme and support the Secretaries APS Reform Committee.

Review recommendations, savings and costs

12. The conduct of reviews was compliant with many, but not all, expectations established in the *Contestability Programme Guidelines* and the review terms of reference. Less than half of the 22 Functional and Efficiency Reviews met planned timeframes for consideration by the responsible Minister and/or Government, and few reviews were assessed as meeting the terms of reference. Review reports generally did not include benchmarks to demonstrate efficiencies or assessments to evaluate the benefits of implementation. Transition arrangements to implement recommendations, where included in review reports, were not specific or detailed.

13. The Programme proposed many recommendations to improve the efficient delivery of government functions. A total of 960 and 74 recommendations were made across 22 Functional and Efficiency Reviews and 11 Contestability Reviews respectively. Recommendations often focused on internal system improvements such as structural change, streamlining processes, and adopting improved products and services. Relatively few recommendations were made to cease functions or identify opportunities for alternative providers of the function, and market based improvements almost exclusively focused on outsourcing.

14. Responsible Accountable Authorities generally considered all Functional and Efficiency Review recommendations, and supported or agreed, agreed in part, or in principle, a substantial majority (73 per cent) of those recommendations, and the relevant Minister considered and largely endorsed entities' positions. Approximately one quarter of all recommendations were considered by Government, and generally focused on reducing expenditure or generating income. Few recommendations from these

reviews were rejected by Accountable Authorities (68 recommendations, seven per cent), Ministers (79 recommendations, eight per cent) or the Government (35 recommendations, four per cent). Similarly, very few recommendations (three recommendations, four per cent) from Contestability Reviews were rejected, and the Government either accepted or is considering over half of all recommendations from these reviews. However, for three of the 11 Contestability Reviews, the responsible Minister had not considered recommendations, and recommendations from four Contestability Reviews were not considered by Government.

15. Estimated net savings to Budget of more than \$5 billion over the forward estimates exceed the total reported cost (\$18.7 million) of undertaking Functional and Efficiency Reviews and Contestability Reviews—although few entities were able to provide the full cost of the reviews. Savings to Budget were derived exclusively from Functional and Efficiency Reviews, and mainly from reductions in programme outlays (\$5.0 billion) rather than departmental outlays (\$122.3 million). Most reviews have not led to a net saving to Budget, with savings being reported for only eight of 25 participating entities.

Implementation of review recommendations

16. For the four reviews examined in detail, the Department of Employment, Comcare, the Department of Health and the Department of Social Services developed implementation plans for all or most of their accepted recommendations, while the Department of Foreign Affairs and Trade developed implementation plans for only ten per cent of its accepted recommendations. Where implementation plans were developed, they regularly included implementation milestones and lines of accountability. Eight plans (five per cent) established performance measures, and only one plan established benchmarks for performance measures.

17. While all entities have implemented or commenced implementing between 65 and 90 per cent of accepted recommendations from the four reviews, the Department of Employment, Comcare and the Department of Health demonstrated that implementation was in accordance with plans. The Department of Social Services provided plans for implementing eight of its 12 accepted recommendations, and demonstrated that it had implemented six recommendations and was implementing another six recommendations. The Department of Health had a number of accepted recommendations where implementation had not commenced or would not be progressed (35 per cent), and the Department of Foreign Affairs and Trade had not established completion dates for a number of recommendations where implementation had commenced.

18. Entities monitored and reported on the implementation of recommendations from the four reviews, but focused on milestones and deliverables and rarely on achieving outcomes. Only Comcare and the Department of Employment established and reported on measures of efficiency or effectiveness. One of the entities established baselines to support an assessment of efficiency or performance improvements. The Department of Health regularly monitored and reported to senior governance committees on the implementation of recommendations from its Functional and Efficiency Review. The Department of Social Services undertook some reporting on the implementation of individual recommendations to governance committees. The Department of Foreign Affairs and Trade undertook ad hoc monitoring and reporting arrangements to report on the progress of implementation. For some recommendations, departmental appropriations were reduced on the premise that operating efficiencies would be achieved. In the absence of a baseline, performance measures and trend analysis for efficiency, service level and quality it is difficult for entities to demonstrate that these initiatives have led to efficiencies and performance improvements.

19. Reductions over the forward estimates to the Budget arising from the Functional and Efficiency Reviews of the Department of Health, Department of Social Services and the Department of Foreign Affairs and Trade totalled \$4.9 billion, which represented 95 per cent of total net savings for the Programme reported by Finance. Of the four reviews examined, only the Department of

Employment has evaluated and reported the outcomes of the implementation of recommendations—from the Insurable Risk Contestability Review, although any savings arising from this review have not been returned to the Budget. The Department of Social Services has evaluated the implementation of one recommendation but could not demonstrate that all planned savings and efficiencies were achieved. The responsible Ministers for Health, Social Services and Foreign Affairs were involved in proposing savings through submissions to Government and the Budget process for individual or groups of recommendations arising from these reviews. Beyond these pre-established arrangements, processes were largely not in place to evaluate and report to these Ministers on the outcome of the implementation of recommendations.

Summary of entity responses

20. The proposed audit report, or an extract, was provided to the 25 entities. Eleven entities formally responded, and 14 entities confirmed that they would not be providing a formal response to the audit. Summary responses from the primary audited entities are provided below.

Department of Finance

Finance notes the findings and key learnings in the Report.

Department of Education and Training

The Department of Education and Training acknowledges the Australian National Audit Office's (ANAO) report and the associated work undertaken on the Efficiency through Contestability Programme. The department also acknowledges that there are no recommendations or findings to which it needs to respond.

Department of Jobs and Small Business

The Department of Jobs and Small Business agrees with the key learnings from the audit and was pleased the Australian National Audit Office found the Department had, in the context of the Commonwealth's Insurable Risk Contestability Review:

- developed implementation plans for the accepted recommendations including milestones, performance measures and lines of accountability;
- demonstrated implementation was in accordance with these plans and had a structured approach to monitoring and reporting on implementation; and
- had evaluated and reported the outcomes of implementation.

Department of Health

The Department of Health was one of the key departments reviewed by the ANAO in assessing the effectiveness of the Efficiency through Contestability Programme. The Department notes that nearly all projected Budget savings for the Programme came from the four reviews contained in the ANAO report, [with a substantial proportion from the Department of Health].

The Programme, along with other reviews being undertaken in the Department at that time, assisted in identifying opportunities for efficiencies and improvements to be made in organisational capability. The ANAO acknowledged the large number of recommendations to be implemented by the Department and the well-developed implementation plans. The Report also highlighted that the recommendations of the Programme were integrated into the Health Capability Program Action Plan which had been developed to respond to the Health Functional and Efficiency Review.

The Department agrees with the ANAO's key learnings for agencies identified in the Report focussing on programme design, governance and risk management, and performance and impact measurement outlined on [page 7] of the Report.

Since the reviews, the Department has undergone a number of structural changes and Machinery of Government changes. The outcomes of the reviews and learnings identified in the ANAO report will contribute to the ongoing need to improve organisational performance to support implementation of the Government priorities and ensure the Department is seen as a high performing agency.

Department of Human Services

The Department of Human Services (the department) notes the report's findings. The department also notes that the report does not identify any issues or make any recommendations that are specific to the department.

Department of Social Services

The Department of Social Services (the department) welcomes the conclusion and key learnings for Australian Government entities identified in the audit report on the Efficiency through Contestability Programme. The audit report notes that 12 recommendations were accepted by the Government and/or the department during the department's Functional and Efficiency Review in 2015. Since the ANAO concluded its fieldwork for this audit an additional three recommendations from the department's 2015 Functional and Efficiency Review have been accepted, or partially accepted, and are being implemented. These include the cessation of Sickness Allowance and Utilities Allowance, which formed part of the *Social Services Legislation Amendment (Welfare Reform) Act 2018* and the introduction of a family income test for Carer Allowance, subject to the passage of the Social Services Legislation Amendment (Payment for Carers) Bill 2018.

The department notes that of the total \$5 billion in savings across the Forward Estimates achieved by all agencies, the department contributed \$3.21 billion of these savings.

Department of Foreign Affairs and Trade

DFAT thanks the ANAO for this audit and observations on DFAT's implementation of the Functional and Efficiency Review (FER) recommendations. DFAT's FER delivered \$50.5 million of savings and generated \$221.5 million in additional revenue.

Of the 75 recommendations identified in the FER, 33 have been implemented. Implementation plans were in place for 23 recommendations, 12 of which have been fully implemented. Implementation plans were used where the recommendation was assessed by DFAT as having a level of complexity and risk that required additional oversight and governance.

Key learnings for all Australian Government entities

21. Below is a summary of key learnings identified in this audit that may be considered by other Australian Government entities.

Programme design

- In the programme design phase, entities should provide advice on implementation risks, and prepare an implementation plan—or if that is not feasible, early in the post-announcement period, prior to implementation.
- Policy design, advice to Government, and programme implementation should all be informed by sound analysis and a strong evidence base.

Governance and risk management

- Risk management plans and strategies should be supported by institutional frameworks that ensure continuity in risk management and mitigation for the duration of the project.
- Key actions that need to be undertaken to meet responsibilities under a programme should be documented, assigned and monitored.
- Sufficient records should be created and retained to demonstrate key actions and decisions taken and support easy identification and retrieval. This would include records of:
 - meeting programme requirements and expectations established in frameworks, guidelines and terms of reference;
 - fulfilling responsibilities;
 - key decisions and actions of the Accountable Authority; and
 - providing advice to Ministers and Government and the relevant decisions made.

Performance and impact measurement

- Review and evaluation arrangements should be identified in the design phase, including baseline data and access to reliable sources of data, to help measure or evaluate the intended impact of programmes.
- Costs, savings and benefits (where relevant) associated with projects should be outlined during the project planning phase to enable informed value assessments and enhance accountability.
- During and following implementation of an activity to improve performance (including service levels and/or efficiency), trends in performance measures against the baseline should be monitored and reported to demonstrate whether implementation objectives have been achieved.
- Following completion of the implementation of significant change programs and recommendations, an evaluation of the outcomes against objectives should be made to determine the success of the actions taken, and whether further or different actions are required.

Effectiveness of Monitoring and Payment Arrangements under National Partnership Agreements No.42 2017–18

Department of the Prime Minister and Cabinet; Department of the Treasury; Department of Agriculture and Water Resources; Department of Health; Department of Infrastructure, Regional Development and Cities

Background

1. The 2009 *Intergovernmental Agreement on Federal Financial Relations* (Intergovernmental Agreement) established the overarching framework for Australia's federal financial relations. It recognised that while state and territory governments (States) have constitutional responsibility for many areas of service delivery, coordinated action may be desirable to address Australia's economic and social challenges. The framework was intended to provide the States with flexibility to deliver services, while increasing governments' accountability to the public through a combined focus on the achievement of outcomes, clearer specification of roles and responsibilities, and enhanced performance reporting.
2. A key to achieving the aims of the Intergovernmental Agreement is in the design of National Partnership Agreements, which outline agreed policy objectives in areas of nationally significant reform or for service delivery improvements. Commonwealth payment is tied to achieving outcomes and outputs, which requires well-defined performance measures and deliverables that are clearly linked to the outcomes and outputs of the National Partnership Agreements.
3. National Partnership Agreements are administered by Commonwealth portfolio departments that approve payments on assessment that States have met the performance measures and milestones outlined in agreements, while the Commonwealth Department of the Treasury is responsible for making payments.

Audit approach

4. The ANAO selected National Partnership Agreements for audit because of the risk associated with the transfer of significant Commonwealth funding to the States (on average \$16 billion per year) through these agreements under the Intergovernmental Agreement. The Intergovernmental Agreement established a new framework designed to improve the transparency and accountability of National Partnership Agreements with a clearer focus on the delivery of specified outcomes. The audit aims to provide assurance that National Partnership Agreements have been developed and implemented in line with the transparency, funding and performance requirements of the Intergovernmental Agreement.
5. The objective of the audit was to examine the effectiveness of monitoring and payment arrangements under National Partnership Agreements. The audit criteria were to assess the extent to which:
 - monitoring and payment arrangements for National Partnership Agreements have been developed in line with the principles and design requirements of the *Intergovernmental Agreement on Federal Financial Relations*;
 - monitoring of the performance of the states and territories by portfolio departments has been conducted in line with National Partnership Agreements; and
 - the Department of the Treasury has made payments in line with the financial requirements of National Partnership Agreements and the advice of the administering portfolio departments.

6. The audit assessed 17 of 71 National Partnership Agreements funded as at 1 July 2016. These 17 agreements involved the transfer of 55 per cent of funding under National Partnership Agreements to the States. The ANAO targeted high risk, high value agreements in the selection process, with a quarter of the sampled agreements randomly selected. The selected National Partnership Agreements were administered by five Commonwealth Departments—Prime Minister and Cabinet; Treasury; Agriculture and Water Resources; Health; and Infrastructure, Regional Development and Cities.

Conclusion

7. Strong frameworks have been established for designing the monitoring and payment arrangements under National Partnership Agreements, but implementation has been mixed. For 30 per cent of agreements examined, implementation has been effective, with suitable performance measures that track progress towards well specified outputs and outcomes, portfolio departments' conducting sound assessments to verify that milestones have been met, and the Department of the Treasury making payments accordingly. More commonly, there have been weaknesses in some aspects of the monitoring and payment arrangements of National Partnership Agreements, particularly specifying outcome measures, obtaining sufficient evidence to verify all milestones have been met and publicly reporting the results achieved.

8. The National Partnership Agreements examined are largely consistent with the principles and design requirements of the Intergovernmental Agreement, but there was mixed adherence to the performance and funding requirements of the Intergovernmental Agreement. While listing National Partnership Agreements on the Council on Federal Financial Relations' website provides transparency of the intent of the agreements, there is no public reporting of performance on that website and there is disparate reporting elsewhere, which weakens transparency and accountability about the value of the agreements.

9. There was mixed performance by the five portfolio departments examined in assessing performance against prescribed performance measures/milestones of National Partnership Agreements, with milestones being assessed as met without sufficient supporting evidence in 31 per cent of projects examined. Once assessments are made, the departments have sufficient controls to ensure accurate payment information is provided (with the required approval) to the Department of the Treasury via the Federal Payments Management System, and the Department of the Treasury has implemented sufficient controls to gain assurance over the accuracy and timeliness of payments.

Supporting findings

Developing National Partnership Agreements

10. The National Partnership Agreements examined are consistent with the principles of the Intergovernmental Agreement, relating to clarifying responsibilities, providing flexibility in service delivery and enhancing accountability to the public. The 17 agreements examined are also consistent with the design requirements of the Intergovernmental Agreement. Where there was some inconsistency, this was virtually always because the design requirement did not apply at the time of signing or to the type of agreement. The high level of consistency across National Partnership Agreements reflects central oversight and common processes introduced by the Department of the Prime Minister and Cabinet and the Department of the Treasury following the introduction of the Intergovernmental Agreement.

11. Although the last existing agreement with reward payments recently ceased, these agreements remain a feature of National Partnership Agreements. While not urgent, the Intergovernmental Agreement should be updated to reflect the current role of the Productivity Commission in assessing performance benchmarks for reward payments, rather than reflecting the previous arrangements involving the abolished COAG Reform Council.

12. The National Partnership Agreements examined have mixed adherence to the performance and funding requirements of the Intergovernmental Agreement—a performance framework with payments linked to progress against outcomes or outputs, based on clear and precise measures of performance. Eight of the 17 agreements examined (47 per cent) did not have both an outcome-focused performance framework and sound payment design:

- five agreements (29 per cent) did not have an outcome-focused performance framework with payments linked to progress against outcomes, and outputs based on clear and precise measures of performance such as performance benchmarks or milestones;
- two agreements (12 per cent) did not have sound payment design, where payments were linked to the achievement of performance milestones; and
- one agreement did not have either an outcome-focused performance framework or a sound payment design.

13. Public reporting under National Partnership Agreements does not provide adequate accountability and transparency. While expected outcomes and outputs for all National Partnership Agreements are listed on the Council on Federal Financial Relations website, the extent to which outcomes and outputs have been successfully achieved is not reported on the website. There is some reporting on performance achieved through agreements on portfolio departments' websites and annual reports, which has typically focused on the major agreements. More consistent, centralised public reporting of achievement of outcomes and outputs under all National Partnership Agreements is required to meet the transparency and accountability objectives of the Intergovernmental Agreement.

Assessing performance and authorising payment

14. All five portfolio departments examined by the ANAO had assessed State performance against prescribed performance measures/milestones of National Partnership Agreements, although the adequacy of evidence used to assess performance varied across agreements. In five of 16 projects examined for 2015–16 and 2016–17, the departments had not assessed sufficient evidence to fully verify if milestone requirements of the agreements had been met. Two of these were for National Partnership Agreements that facilitate reform. Portfolio departments usually had a stronger evidence base for assessing achievement against performance milestones for those projects examined that had been assigned a high risk rating by the Department of the Treasury than those with a medium or low risk rating, which is appropriate.

15. The five portfolio departments examined have adequate controls over the payment approval process. The departments have adopted a range of payment approval processes, although a number of standard controls are also in place. As part of auditing 2016–17 financial statements, the ANAO confirmed that in all five departments National Partnership Agreement payments had been correctly approved by authorised delegates. Also, the information submitted by these departments to the Department of the Treasury via the Federal Payments Management System had been in accordance with the certified payments and the requirements of National Partnership Agreements.

16. The Department of the Treasury has implemented sufficient controls to gain assurance over the accuracy and timeliness of National Partnership Agreement payments. While the Department of the Treasury places some reliance on assessments undertaken by portfolio departments in certifying payments, it performs standard quality assurance checks before authorising final payment. Moreover, the Department of the Treasury performs additional checks for payments for National Partnership Agreements that have been rated as high risk.

Recommendations

Recommendation no.1
Paragraph 2.12 The Department of the Prime Minister and Cabinet and the Department of the Treasury recommend to the Council of Australian Governments, through the Council on Federal Financial Relations, that the 2009 *Intergovernmental Agreement on Federal Financial Relations* and associated documents be amended to remove reference to the abolished COAG Reform Council and refer to the Productivity Commission as appropriate.

Department of the Prime Minister and Cabinet and Department of the Treasury responses: *Agreed.*

Recommendation no.2
Paragraph 2.29 The Department of the Treasury, through the Council on Federal Financial Relations website, facilitates improved public reporting on the outcomes and impact of National Partnership Agreements.

Department of the Treasury response: *Agreed.*

Summary of entity responses

Department of the Prime Minister and Cabinet

The Department agrees with the recommendations of the report.

The management of funding agreements with the States and Territories is important for the Department and the broader Commonwealth due to the amount of expenditure they cover and the important outcomes they are trying to achieve. This report provides useful insights into how we can continue to improve the operation of these agreements.

The Department works with the Treasury and relevant portfolio departments during the development of National Partnership Agreements to ensure they are consistent with the Intergovernmental Agreement on Federal Financial Relations. The Department and the Treasury will continue to ensure National Partnership Agreements have robust accountability and transparency mechanisms.

Department of the Treasury

Treasury welcomes the report, which recognises that the *Intergovernmental Agreement on Federal Financial Relations* provides a robust framework for the development and implementation of Commonwealth payments to the states and territories. The report also identifies opportunities to strengthen and enhance existing processes, especially with regard to reporting and transparency. Treasury will continue to work with the Department of the Prime Minister and Cabinet, portfolio agencies and the states and territories to deliver on these objectives. Treasury agrees with both recommendations in the report.

Department of Agriculture and Water Resources

The department agrees with the performance review report's two Recommendations aimed at improving the transparency and accountability of National Partnership Agreements through consistent, public reporting on outcomes achieved, and amending the 2009 *Intergovernmental Agreement on Federal Financial Relations* to reflect current practice.

The department notes the report's findings regarding agreements it administers. The ANAO found that two of these agreements are weakened in that they do not contain outcome-focused performance frameworks in accordance with the Conceptual Framework for Performance Reporting endorsed by COAG in February 2011.

The department notes that one of these agreements, on *Water for the Future - Sustainable Rural Water Use and Infrastructure*, predates the COAG-endorsed framework for performance reporting and all the projects under it have been completed. The second agreement, on *Implementing Water Reform in the Murray-Darling Basin*, was negotiated in 2013–14, concludes in 2019–20, and would require the agreement of five other jurisdictions to change. However, the department is re-considering the criteria it

uses to assess progress against the agreement milestones based on the ANAO findings and recommendations from the department's mid-term review of the agreement, completed in August 2017.

The department notes this performance audit draws in part on the ANAO's Assurance Review report on *New South Wales' protection and use of environmental water under the National Partnership Agreement on Implementing Water Reform in the Murray-Darling Basin*. The department has published its response to this Assurance Review at www.agriculture.gov.au/about/media-centre/on-the-record/response-anao-assessmentmurraydarling.

Department of Health

The Department of Health was one of five portfolio departments with management responsibility for a number of the 17 National Partnership Agreements assessed by the ANAO. As the manager of a large number of National Partnership Agreements (14 Agreements), the Department of Health notes the ANAO conclusion that Agreements were generally sound in design and demonstrated sufficient controls around payment approval processes.

The Department agrees with the key learnings identified in the Report, focussing on a need for increased discipline in policy and program design, implementation and performance measurement. The Department continues to look at how it can improve the frameworks it uses to support better performance measurement and reporting, and enhance the organisational emphasis on program assurance and successful program delivery. The learnings identified in the ANAO Report will support this work.

Department of Infrastructure, Regional Development and Cities

The Department of Infrastructure, Regional Development and Cities (the Department) welcomes the audit's overall conclusions and findings. The Department acknowledges that there is merit in strengthening the performance framework of the National Partnership Agreement on Land Transport Infrastructure Projects (the Agreement). The Agreement expires on 30 June 2019 and the Department will take into consideration the ANAO's comments in this report in negotiating a new agreement.

Key learnings for improvement for all Australian Government entities

17. Below is a summary of key learnings and areas of good practice identified in this audit report that may be considered by other Commonwealth entities when managing partnership agreements.

Policy/program design

- In refining or redesigning partnership agreements, coordinating entities should review the effectiveness of existing agreements to establish areas for improvement, including any significant non-adherence to key terms by participating entities.

Policy/program implementation

- To support compliance with key terms of partnership agreements, entities should develop risk-based arrangements to obtain assurance about the ongoing level and nature of non-adherence to key terms.
- On completion of projects subject to partnership agreements, final payment should not be made until evidence is provided of successful completion.

Performance and impact measurement

- Where agreements have outcome measures, entities should ensure that these measures are clearly aligned to well-specified output measures and to suitable performance milestones that are based on valid and reliable data.

- Where there is consolidated reporting of the objectives and success measures for sets of agreements, such as on a particular website, there should also be consolidated reporting of performance achieved against those objectives and measures.

Domestic Passenger Screening – Follow Up
Audit Report No.43 2017–18
Department of Home Affairs

Summary and recommendations

Background

1. The aim of domestic passenger screening is to prevent prohibited items such as weapons and explosives from being carried onto aircraft. Specialised equipment and screening personnel are used to detect and control prohibited items at 62 security controlled airports across Australia.¹ Since October 2012, the number of domestic aircraft passengers has trended upwards with 62.13 million domestic passengers carried on 639 400 regular public transport and charter aircraft trips during the year ending October 2017.²

2. On 31 August 2016, the Australian National Audit Office (ANAO) tabled Audit Report No.5 2016–17, *Passenger Security Screening at Domestic Airports* in the Parliament. In that report, the ANAO found that the Department (then, the Department of Infrastructure and Regional Development) was unable to provide assurance that passenger screening was effective, or to what extent screening authorities had complied with the Regulations, due to poor data and inadequate records.³ The ANAO also found that the Department did not have meaningful passenger screening performance targets or enforcement strategies and did not direct resources to areas with a higher risk of non-compliance.⁴ The ANAO made five recommendations aimed at improving the Department's regulatory performance.⁵ The Department accepted all five recommendations and advised the ANAO that:

The Department notes that following significant review work in 2015 it is investing in the broad reform of its transport security regulatory operations. This is to ensure that the Office of Transport Security's regulatory activities are well positioned to respond to changing threats and risks, future industry growth and diversification, and that its approvals and compliance operations are efficient. This reform program comprises three elements: redesign of the transport security operating model, the establishment of competency based learning and development framework and improvements to the regulatory management system (RMS).⁶

Audit objective and criteria

3. The objective of this audit was to examine the extent to which the Department of Infrastructure and Regional Development, now the Department of Home Affairs (the Department) has implemented the recommendations from ANAO Report No.5 2016–17, *Passenger Security Screening at Domestic Airports*.

¹ Regulation 4.17 of the *Aviation Transport Security Regulations 2005* establishes the methods, techniques and equipment to be used for screening.

² Department of Infrastructure and Regional Development, *Statistical Report: Aviation: Domestic aviation activity*, October 2017, p. 9.

³ ANAO Report No.5, 2016–17, *Passenger Security Screening at Domestic Airports*, p. 7.

⁴ *ibid.*

⁵ *ibid.*, pp. 9–10.

⁶ *ibid.*, p. 10.

4. To form a conclusion against the audit objective, the ANAO adopted the following high level criteria:

- To what extent has the Department implemented an effective compliance monitoring program?
- To what extent has the Department implemented an appropriate learning and development framework?
- To what extent has the Department implemented effective performance monitoring and reporting arrangements?

Rationale

5. Due to the significance of the findings from the previous audit, the associated recommendations, and the response from the Department advising that a number of initiatives to address the shortcomings identified were already underway, it was expected that the Department would act quickly to address and remediate the issues identified. Timely implementation is necessary if the audited entity is to achieve full value from the agreed recommendations. On this basis, the ANAO decided to commence a follow-up audit in the 2017–18 financial year to determine if the Department is implementing the recommendations from the previous audit in a timely manner, and if the Department is now in a better position to provide assurance of the effectiveness of passenger screening.

Conclusion

6. As at March 2018, the Department has implemented one and partially implemented four of the five recommendations made in ANAO Audit Report No.5 2016–17, *Passenger Security Screening at Domestic Airports* (see Table S.1 below). Consequently, while the Department has made progress, it is not yet well placed to provide assurance that passenger screening is effective and that screening authorities comply with the Regulations.

Table S.1: Assessment of the extent to which the recommendations made in ANAO Audit Report No.5 2016–17 have been implemented

Recommendation	Status
<p>ANAO Recommendation No.1 Set a date at which the grandfathering provisions for passenger screening equipment requirements will cease, and amend the Aviation Screening Notices accordingly.</p>	Implemented
<p>ANAO Recommendation No.2 a) establish an analysis function to identify non-compliance trends based on accurate, reliable compliance activity data; and b) incorporate the results of the analysis into the compliance program, focusing on areas at risk of non-compliance.</p>	Partially implemented ^a
<p>ANAO Recommendation No.3 Develop performance measures for passenger screening that are practical, achievable and measurable.</p>	Partially implemented ^b

Recommendation	Status
<p>ANAO Recommendation No.4</p> <p>Conduct a training needs analysis for users of the regulatory management system, deliver appropriate training, and monitor its effectiveness.</p>	Partially implemented ^c
<p>ANAO Recommendation No.5</p> <p>Provide targeted reporting to its stakeholders, based on accurate data, which enables an assessment of the effectiveness of passenger screening, and promotes improved passenger screening effectiveness.</p>	Partially implemented

Note a: Recommendation No.2 will be implemented through a broader *OTS data strategy*.

Note b: Recommendation No.3 will be implemented as part of a broader *Enhanced Mandatory Reporting Project*.

Note c: The Department decided to broaden the application of the training needs analysis and associated learning and development framework to all staff within the Transport Security Operations branch.

Source: ANAO analysis of Departmental documentation.

7. The extent to which the Department has implemented an effective compliance monitoring program has been constrained by the quality of data captured in the Regulatory Management System. Consequently, the ability of the Department to conduct meaningful analysis of compliance activity data and identify non-compliance trends in passenger screening is limited. While the Department has developed a data analysis function to work around the limitations of the Regulatory Management System, its initial analysis was not used to inform planning. The Department has further work to do to be able to identify non-compliance trends and incorporate the results of the analysis into the annual compliance program as recommended in the previous audit.

8. The Department has developed and approved a learning and development framework. However, the plan to implement the framework has not yet been approved, and a key element yet to be finalised is the approach to monitoring and evaluating the framework. Delivery of appropriate training was delayed by the Department's decision to broaden the application of the training needs analysis beyond the initial Regulatory Management System focused training recommended by the ANAO (Recommendation No.4) in the previous audit. While steps were taken to address short-term training needs, the first training courses outlined in the learning and development framework commenced in February 2018.

9. The Department has developed, but not yet implemented performance monitoring arrangements despite numerous reports⁷ including ANAO Audit Report No.26, 2002–03, *Aviation Security in Australia* recommending that performance measures be implemented. Most recently, the timely implementation of these performance measures has been impacted by the Department's decision to implement the measures in July 2018 as part of the broader *Enhanced Mandatory Reporting Project*. While the Department has made progress to improve the reporting provided to its stakeholders, the ability of the Department to accurately assess the effectiveness of passenger screening is limited due to the quality of the data captured in the Regulatory Management System, the lack of an associated reporting function and because performance measures have not yet been implemented.

⁷ Since 2002, 10 reviews into Aviation Security have been conducted. A full list of these reviews was included at Appendix 2 of the previous audit. Of the 10 reviews, four have specifically noted the need for the Department to develop and implement performance measures.

Supporting findings

Compliance monitoring

10. The Department has established a data analysis function, as recommended by the ANAO (Recommendation No.2a) in the previous report and delivered its initial (and only) analysis in July 2017. The analysis provided a breakdown of compliance activities conducted for each category of airport and aircraft operator, the number of findings by type for each state, and the number of findings per security mitigation category. However, the analysis could not be used to identify trends in non-compliance and issues in relation to the quality of compliance activity data remain.

11. The results of the July 2017 analysis were not incorporated into the 2017–18 National Compliance Plan as intended by the ANAO (Recommendation No. 2b). Instead, the plan was informed by separate compliance activity data extracted from the Regulatory Management System and the Microsoft Excel regional office work plans. The analysis used to inform the plan did not include a comprehensive analysis of compliance outcomes or identify areas at risk of non-compliance.

12. The Department directs compliance resources to categories of airports and airline operators that present a higher security risk. The Department has not yet established an effective approach to direct compliance resources within categories. As a result, compliance resources are not targeted towards individual airports and airline operators where the risk of non-compliance is higher or additional support is needed to comply with regulatory requirements.

13. The Department has developed a compliance and enforcement framework, which identifies the need to develop clear guidance outlining the various enforcement options, and the escalation process to assist in the management of non-compliance. However, the framework has not yet been implemented.

Learning and Development

14. An analysis of training needs was completed in February 2017. It took longer to complete than expected because the Department decided to conduct a broader analysis than had been recommended by the ANAO (Recommendation No.4) in the previous audit report.

15. The Department has developed a learning and development framework based on the training needs analysis. However, one element of the framework remains incomplete—the framework does not include a monitoring and evaluation component.

16. Delivery of the training identified in the learning and development framework commenced in late February 2018. Prior to the formal commencement of the training modules identified in the learning and development framework, short-term training needs were met through the development of quick reference guides and the provision of procedural fairness and administrative decision making training.

Performance Monitoring and Reporting

17. The Department has developed performance measures in consultation with stakeholders informed by the performance measures outlined in the 2009 *Aviation Security Screening Review*. However, implementation has been delayed due to the Department's decision to incorporate implementation into the *Enhanced Mandatory Reporting Project*. As a result, the extent to which the measures are practical, achievable and measurable cannot be currently assessed.

18. The Department provides a range of activity and information reports to its various stakeholders. While this information is useful, and supports some stakeholders assess specific elements of their screening operations, it does not enable the Department to assess the

effectiveness of passenger screening or the extent to which the compliance monitoring program promotes improved passenger screening effectiveness.

Recommendations

Recommendation no.1
Paragraph 2.12 In implementing Recommendation No.2 from the previous audit, the Department should ensure that its approach delivers a meaningful analysis of passenger screening compliance activities and outcomes. The analysis should: be capable of accurately identifying non-compliance trends; generate results that are used to inform the development of the risk and compliance prioritisation ratings; and be incorporated into subsequent compliance monitoring programs.

Department of Home Affairs response: Agreed

Recommendation no.2
Paragraph 3.9 In implementing Recommendation No.4 from the previous audit, the Department should develop and implement a monitoring and evaluation strategy, so it can assess to what extent the objectives of the learning and development framework are being met.

Department of Home Affairs response: Agreed

Recommendation no.3
Paragraph 4.12 In implementing Recommendation No.3 from the previous audit, the Department should ensure that performance measures are established in a timely manner alongside an effective monitoring and review mechanism to provide assurance that the performance measures developed for passenger screening are practical, achievable and measurable.

Department of Home Affairs response: Agreed

Summary of entity response

19. The Department of Home Affairs was provided with a copy of the proposed audit report for comment. A summary of the response received from the Department is provided below.

Department of Home Affairs

The Department agrees with all recommendations in the audit.

The Department is continuing to work on the implementation of the recommendations from the original audit of passenger security screening at domestic airports and has made significant progress. The Department is strengthening ICT systems and staff skills; improving compliance planning, data quality and analytical capabilities and working with industry to share key data.

Key learnings for all Australian Government entities

Below is a summary of key learnings and areas for improvement identified in this audit report that may be considered by other Commonwealth entities when administering regulatory programs and implementing recommendations.

Governance and risk management

- To provide assurance that risks are being effectively managed, entities should not depend upon qualitative assessments alone. To assess the effectiveness of critical risk controls, qualitative assessments should be supported by quantitative data and incorporated into a feedback mechanism capable of identifying if the approach to delivering government policy is appropriate and supports achievement of the stated policy objective.

Implementation of recommendations

- Entities should ensure that agreed timeframes to implement recommendations are determined in accordance with the assessed risk. Clearly defining roles and responsibilities, priority, resourcing, desired outcomes, and including appropriate monitoring and reporting arrangements will lead to better results.

Performance and Impact measurement

- Entities should ensure that performance measures are included when designing an approach to deliver government policy. Performance measures should be implemented in a timely manner, and support the ability of the entity to provide assurance to stakeholders that the outcomes of the program established support the entity to deliver the objectives of the policy.

Defence's management of sustainment products—health materiel and combat rations

[No.44 2017–18]

Department of Defence

Summary and recommendations

Background

1. Non-platform products are items and supplies that do not represent weapons platforms, but are required to maintain the capability and operation of the Australian Defence Force. These can include clothing items, small firearms, health and dental equipment, and other consumables. The procurement, management and supply of these capabilities is conducted by Systems Program Offices within the Department of Defence (Defence).
2. The Health Systems Program Office (Health SPO) is responsible for the procurement and sustainment of pharmaceuticals, medical and dental equipment and consumables, and combat rations. The Health SPO's budget for sustainment in 2017–18 was \$78 million.
3. In 2017, Health SPO undertook procurements for health materiel and combat rations with the resultant contracts having an estimated annual expenditure of \$24 million and \$26 million respectively. The approved estimated expenditure of the pharmaceuticals and combat rations contracts over a five year period is \$120 million and \$133 million respectively.
4. Defence's effectiveness in delivering health materiel and combat rations was selected for audit to provide assurance over significant Commonwealth expenditure not previously subject to audit coverage as well as to provide transparency and assurance to the Parliament with regards to: the operation of sustainment Systems Program Offices; value for money in Defence's sustainment of non-platform products; and compliance with the Commonwealth procurement framework for the areas under audit. This audit is part of the ANAO's program of audits relating to Defence sustainment, which has included the recent ANAO Audit Report No.2 2017–18 *Defence's Management of Materiel Sustainment*¹—which focused on Defence wide governance arrangements for sustainment, including the strategic review of the Systems Program Offices.

Audit objective and criteria

5. The objective of the audit was to assess the effectiveness of Defence's arrangements for delivering selected non-platform sustainment. To form a conclusion against the objective, the ANAO adopted the following high level audit criteria:
 - Defence has implemented effective governance arrangements for the selected Systems Program Office; and
 - Defence has appropriate procurement and contract management arrangements for the selected non-platform sustainment products.

¹ The audit report is available from:
<https://www.anao.gov.au/sites/g/files/net3721/f/ANAO_Report_2017-18_02.pdf>.

Conclusion

6. Defence's arrangements for delivering health materiel and combat rations through the Health Systems Program Office are effective other than in the areas outlined below.

7. Defence has put in place appropriate governance, reporting and accountability arrangements for the Health Systems Program Office. Effectiveness could be improved through increased IT systems integration and revising the use of internal key performance indicators.

8. Defence's 2017 procurement and contract management arrangements for the supply and delivery of health systems products were appropriate except Defence did not:

- meet the risk policy of the Department, comply with the Commonwealth Procurement Rules in relation to records management, or implement arrangements for risk and probity management consistent with the intent of the Commonwealth Procurement Rules;
- seek to negotiate a reduction in tendered prices during contract negotiations; or
- plan effectively for the transition to the new contractual arrangements.

9. Defence's 2017 procurement arrangements for the supply and delivery of combat rations were appropriate except Defence did not:

- meet the risk policy of the Department, comply with the Commonwealth Procurement Rules in relation to records management, or implement arrangements for risk and probity management consistent with the intent of the Commonwealth Procurement Rules; or
- implement a performance-based contract.

10. Defence's decision to supply freeze-dried meal components as Government Furnished Material rather than through the combat rations contract may have limited the market and impacted the achievement of value for money for the Commonwealth.

Supporting findings

Governance Arrangements and Performance Reporting

11. Defence has established appropriate reporting and accountability mechanisms for the sustainment of health materiel and combat rations. However the reporting under these arrangements is not fully effective as not all data requirements are being met.

12. Defence has in place appropriate policies to manage the sustainment of the selected products, including a specific Health Materiel Manual. Effective implementation of these policies is hindered by Defence's monitoring of multiple IT systems that are not linked, leading to complex workarounds and instances of duplication, redundancies or out of date data.

13. Defence has a fit for purpose framework for performance reporting and monitoring within the Health SPO but its implementation is not fully effective. Key performance indicators in the Sustainment Performance Management System are: relevant and reliable, but not complete; linkages between Defence's internal key performance indicators and those included in the audited prime vendor contracts are limited for the new pharmaceutical contract and there are no linkages with the new combat rations contract; and the Sustainment Performance Management System does not include all indicators used to monitor health materiel. The Sustainment Performance Management Systems allows for performance monitoring, trend analysis and cross-product comparison, however Land Systems Division only uses the System to report on key performance indicators. Two of the five key performance indicators for health materiel reported in the Sustainment Performance Management System are consistently not met, indicating Defence should take action to remedy performance shortfalls or reconsider the indicators.

14. Risks pertaining to the sustainment of health materiel and combat rations are reported on at key committees and meetings by Health SPO. Defence has not provided evidence that key operational and change management risks faced by Health SPO have been documented in risk management or business plans or that they are being managed.

Health Systems Fleet

15. In Defence's procurement for pharmaceuticals, medical and dental equipment and medical and dental consumables, Defence largely complied with the Commonwealth Procurement Framework and most of its internal policies; however, it did not meet the risk policy of the Department, records management was not compliant with the Commonwealth Procurement Rules, and Defence's arrangements for risk and probity management were not consistent with the intent of the Commonwealth Procurement Rules.

16. Defence records indicate that tender information was removed from Defence's secure system during the procurement evaluation.

17. The 2017 tender and evaluation process for pharmaceuticals, medical and dental consumables and medical and dental equipment was designed to produce a value for money outcome, including the use of an open tender process as a basis for introducing competition. Defence negotiated with the preferred tenderer on a number of issues which improved the value for money outcome for the Commonwealth but did not seek to negotiate a reduction in tendered prices.

18. Defence implemented a performance based contract, which is supported by appropriate reporting procedures and management plans. The contract provides for scheduled reviews of the prime vendor's performance, with the first review due in early 2018. Defence did not plan effectively for the transition to the new contractual arrangements.

Combat Rations

19. In Defence's procurement for combat rations, Defence largely complied with the Commonwealth Procurement Framework and most of its internal policies; however, it did not meet the risk policy of the Department, records management were not compliant with the Commonwealth Procurement Rules, and Defence's arrangements for risk and probity management were not consistent with the intent of the Commonwealth Procurement Rules.

20. Defence records indicate that tender information was removed from Defence's secure system during the procurement evaluation.

21. The 2017 tender and evaluation process for combat rations was designed to produce a value for money outcome. Defence undertook a two stage, open tender process and conducted detailed evaluation of tenders. Defence negotiated with the preferred tenderer on a number of issues, including actively negotiating a reduction in distribution costs. Defence decided to supply freeze-dried meal components itself as Government Furnished Material rather than having those components supplied under the contract as initially indicated in tender documentation. This may have limited the market and, as Defence did not negotiate a reduction in tendered prices for the relevant ration pack, impacted on the achievement of value for money for the Commonwealth.

22. Whilst the contract for the supply of combat rations sets out the requirements and standards of the products to be delivered and contains some individual delivery payment controls, Defence has not implemented a performance-based contract. The contract does not specify how performance issues will be managed, or link key performance indicators to payments.

Recommendations

Recommendation no.1 That Defence refines its performance reporting and management arrangements for health materiel and combat rations by:

Paragraph 2.27

- (b) aligning key performance indicators reported on in the Sustainment Performance Management System to the prime vendor contracts; and
- (c) making use of the full reporting functionality of the Sustainment Performance Management System.

Department of Defence response: *Defence accepts the recommendation.*

Recommendation no.2 That for future procurements which involve a new service provider, Defence develops adequate phase-in plans.

Paragraph 3.63

Department of Defence response: *Defence accepts the recommendation.*

Summary of entity response

Defence acknowledges the observations contained in the audit report on *Defence's Management of Sustainment Products – Health Materiel and Combat Rations*; and agrees to the two recommendations made by the ANAO.

Key learnings for all Australian Government entities

23. Below is a summary of key learnings and areas for improvement identified in this audit report that may be considered by entities when managing procurements.

Governance and risk management

- Implementing risk management arrangements—risks should be identified and mechanisms put in place to manage business and operational risks and monitor the effectiveness of risk treatments.

Procurement

- Procurement processes—procurement is a standard business operation in the Australian Public Service and procurement processes should be compliant with the Commonwealth Procurement Rules.
- Implementing probity arrangements—implementation of probity arrangements helps ensure the ethical administration of procurements, including the management of potential conflicts of interest.
- Retaining documentation—entities should institute processes to ensure officials formally file all relevant procurement documentation to ensure the process and decisions are transparent and have an accessible audit trail.

Transition to new contracting arrangements

- Transitioning to new contracting arrangements—planning should reflect adequate consideration of key risks throughout the transition process, particularly where revised arrangements involve new delivery models, new technology and the phase out of extant contractors.

Performance monitoring and reporting

- Performance-based contracts—performance-based contracting helps ensure that ongoing value for money is achieved in a procurement over the life of the contract.
- Effective performance monitoring—clear linkages between the key performance indicators monitored internally and the performance requirements in contracts support entities in driving contracts to achieve value for money.

The integration of the Department of Immigration and Border Protection and the Australian Customs and Border Protection Service

No.45 2017–18

Department of Home Affairs

Background

1. In February 2014, the National Commission of Audit (NCOA) recommended:

... that a single, integrated border agency, to be known as Border Control Australia, be established through the merger of the border control functions of the Department of Immigration and Border Protection and the Australian Customs and Border Protection Service.
2. On 9 May 2014, the Minister for Immigration and Border Protection announced that the government would carry out this recommendation and integrate Australia's immigration and customs functions into a single entity - the Department of Immigration and Border Protection (DIBP - the department). The Australian Border Force (ABF), headed by a Commissioner, would be established within the department as the 'frontline operational border agency'. The new department and the ABF came into existence on 1 July 2015, and operated under this nomenclature through to 2017.
3. On 18 July 2017, while this audit was in progress, the Prime Minister announced that the government had decided to establish a Home Affairs portfolio. From 20 December 2017, the Department of Home Affairs has assumed all of the department's functions (including the ABF) in addition to functions from each of the Departments of Prime Minister and Cabinet; Social Services; Infrastructure and Regional Development and the Attorney-General's department.
4. In addition to the ABF, the Home Affairs portfolio also includes the following entities:
 - the Australian Federal Police;
 - the Australian Criminal Intelligence Commission;
 - the Australian Transaction Reports and Analysis Centre; and
 - the Australian Security Intelligence Organisation.
5. This audit principally focusses on the period May 2014 to December 2017, while the department was known as DIBP. However, some of the department's responses to ANAO inquiries occurred after it became the Department of Home Affairs. For simplicity, this report refers to 'the department' to signify both the Department of Immigration and Border Protection and the Department of Home Affairs (except where the context requires a distinct reference).

Rationale for undertaking the audit

6. Effective immigration and border control are essential to Australia's national security. The possibility of combining both functions within one entity have been considered on a number of occasions historically. The emergence of threats such as people smuggling and transnational crime led the government to decide in 2014 that integration of the Department of Immigration and Border Protection (DIBP) and the Australian Customs and Border Protection Service (ACBPS) would more effectively address the emerging threats and deliver efficiencies.

7. Both DIBP and ACBPS are sizeable entities from a geographical and functional perspective, and have a history of publicised administrative issues. The ANAO has previously audited both entities on numerous occasions, and this audit presented an opportunity to provide assurance that risks associated with the integration process were being properly managed.

Audit objective and criteria

8. The objective of this audit was to examine the effectiveness of the integration of the Department of Immigration and Border Protection (the department) and the Australian Customs and Border Protection Service (ACBPS).

9. To form a conclusion against the audit objective, the ANAO adopted the following high-level criteria:

- Did the department establish sound governance arrangements for implementation of the integration and capability reform process?
- Did the department manage the integration and capability reform process in accordance with government decisions and relevant plans?
- Can the department demonstrate that the intended outcomes of integration and the capability reform process are being achieved, including financial outcomes?

Conclusion

10. The Department of Immigration and Border Protection achieved the integration of DIBP and ACBPS and the creation of the Australian Border Force in a structural sense and is also progressing with the implementation of a suite of reform projects. However, it is not achieving commitments made to government in relation to additional revenue, and is not in a position to provide the government with assurance that the claimed benefits of integration have been achieved.

11. The department established largely effective governance arrangements which were revised over time in response to emerging issues.

12. The department's record keeping continues to be poor.

13. The department is effectively managing a suite of 38 capability reform projects and has developed sound monitoring arrangements, although the Executive Committee does not have visibility of the overall status of individual projects.

14. The efficiency savings committed to by the department were removed from its forward estimates and have thus been incorporated in the budget. However, the department has not verified whether efficiencies have been delivered in the specific areas which were nominated in the Integration Business Case.

15. Based on progress to the end of December 2017, if collections continue at the current rate the department will only collect 31.6 per cent of the additional customs duty revenue to which it committed in the Integration Business Case.

16. In the Integration Business Case, the department committed to a detailed Benefits Realisation Plan. The plan was not implemented despite several reviews identifying this omission. As a result, the department cannot demonstrate to the government that the claimed benefits of integration have been achieved.

Supporting findings

17. The department moved quickly to establish a sound governance framework for the integration. The framework was revised on a number of occasions in response to emerging issues, particularly with respect to the capability reform projects. The abolition of the Reform and

Integration Task Force resulted in a loss of momentum in the reform process and a drop-off in internal communication with staff. The department recognised this and re-established a similar coordination mechanism. More recently, the department has engaged a consultant to review the framework.

18. Reporting to the Executive focused primarily on integration and organisational reform, with minimal coverage of progress in delivery of the suite of 38 capability reform projects. Following the identification of this as a gap in the 2017 Gateway Review, an Enterprise Transformation Blueprint was established to provide the Executive Committee with greater visibility over the progress of activity across the department.

19. There was no evidence identified to indicate that written briefings were provided to the Minister on progress throughout the implementation process.

20. Detailed communication plans were established and implemented to support the integration process. 'Pulse Check' surveys were regularly taken to evaluate staff satisfaction and engagement with the process.

21. The audit found that the department did not maintain adequate records of the integration process. This finding repeats the outcomes of a substantial number of audits and reviews going back to 2005. The department's own assessment is that its records and information management is in a critically poor state. The problems and their solutions are known to the department, and it has an action plan to address them, although numerous previous attempts to do so have not been successful.

22. The department also experienced a loss of corporate memory due to the level of turn-over of SES staff, with almost half of SES officers present in July 2015 no longer in the department at July 2017.

23. The department initially identified possible risks to effective integration. However, regular reporting against those risks ceased when the Reform and Integration Task Force was disbanded.

24. The department made extensive use of consultants to assist it with the integration process. Despite a requirement to evaluate contracts upon completion, this did not occur in 31 out of 33 (94 per cent) of contracts with a value of more than \$1 million examined by the ANAO, and therefore it is unclear whether these services represented value for money.

25. Following a series of governance changes in October 2015, the department established an effective Project and Program Management Framework which was broadly consistent with the intended future governance state described in the Integration Business Case. While some projects are facing challenges, it is too early to form a view about whether all will be delivered on time and within budget.

26. The department has been subject to budgetary reductions equal to the efficiency savings required by government. It has not verified whether efficiencies were achieved in the specific areas identified in the Integration Business Case.

27. By the end of December 2017, the department had only delivered 42.2 per cent of the additional revenue to which it committed in the Integration Business Case, and if collections continue at the current rate, it will only collect 31.6 per cent of the additional revenue.

28. The department cannot demonstrate that the claimed benefits of integration have been achieved because it did not implement the Benefits Realisation Plan which formed part of the Integration Business Case.

Recommendations

Recommendation no.1
Paragraph 2.46 The Department of Home Affairs give priority to addressing its records and information management deficiencies including by implementing the *Records and Information Management Action Plan 2016–20*.

Department of Home Affairs' response: *Agreed.*

Recommendation no.2
Paragraph 2.64 The Department of Home Affairs develop a business assurance approach to enforce its requirement in the *Contract Management Manual* that contracts be evaluated on completion.

Department of Home Affairs' response: *Agreed.*

Recommendation no.3
Paragraph 4.17 The Department of Home Affairs implement the Benefits Realisation Plan which was included in the Integration Business Case to allow the government to assess whether the claimed benefits of integration have been realised.

Department of Home Affairs' response: *Agreed.*

Summary of entity response

29. The Department of Home Affairs (Home Affairs) recognises and appreciates the efforts of the Australian National Audit Office staff who conducted the audit.

30. Overall the report concludes that the then Department of Immigration and Border Protection (DIBP) successfully achieved integration and continues with the implementation of reform projects. With integration achieved through the establishment of a sound Governance Framework and an effective Project and Program Management Framework, that was supported by detailed communication plans and 'pulse check' surveys. Having in place these frameworks enabled flexible and timely responses to the management of emerging issues.

31. Home Affairs does acknowledge that record-keeping at that time was not in line with best practice and has undertaken significant steps to rectify the situation. Additionally continual improvements are being made in contract management with an automated solution being put in place that will facilitate the assessment of contract performance.

32. Home Affairs disputes in some instances the financial conclusions drawn within the report, and whether or not certain elements were outside the scope of the audit, as well as statements made in regards to project management and the overall visibility of the Executive in relation to the integration project.

33. With the inception of Home Affairs the ongoing development and review of new organisational priorities and strategies, to ensure that governance arrangements are robust, remains a primary focus.

Key learnings for all Australian Government entities

34. Below is a summary of key learnings identified in this audit report that may be considered by other Commonwealth entities when managing large scale organisational change.

Governance and risk management

- When managing large scale organisational change or a complex suite of projects, entities should ensure that there is an appropriate mechanism, under the leadership of an appropriately senior officer, to:
 - manage change and implementation activities across the entire entity;

- identify and manage key interdependencies or resource conflicts as (or ideally, before) they arise;
 - develop and maintain a fit for purpose reporting framework which meets the needs of stakeholders (including Ministers, if appropriate), and effectively escalates issues requiring priority attention; and
 - coordinate internal communications to ensure all staff are engaged with, and feel part of, the process.
- The Reform and Integration Taskforce (RITF) initially established by the Department was an effective example of a body setup with the objective of undertaking these tasks. The RITF's role was to:
 - coordinate and manage the integration and change process for the portfolio;
 - provide a focal point for the preparation of advice to the Government on matters related to portfolio reform; and
 - provide project management oversight, support and reporting of the business led integration and reform activity.
 - An effective governance framework with clearly assigned responsibilities and scopes of authority is essential. Entities should be prepared to revise the framework in response to experience or changing circumstances.

Performance and impact measurement

- Benefits Realisation Plans should clearly identify intended strategic benefits. When drafting such plans, entities should think carefully about whether indicators designed to demonstrate benefits are 'real', measurable and reportable (as opposed to simply aspirational). Implementation work on plans needs to commence from the outset, not left until after the change (or project) is completed.

Record keeping

- In operating an Electronic Data Records Management System, entities should mandate its use and provide relevant training to all staff in order to ensure the full benefits are obtained through the consolidation of fragmented systems and manual records.

Program implementation

- During major organisational change, regular and effective internal communication is critical to fostering staff engagement. Both content and the choice of 'channel' (for example, emails, blogs, FAQs and staff meetings) are important and communication should continue until change has been completed and embedded.

Procurement

- Entities should consider introducing an internal requirement to conduct end-of-contract evaluations of consultancies and other contracts (possibly with a value above a set amount). This would help to ensure that value for money is being achieved from contracts and to identify providers who have not performed satisfactorily.

Management of the National Collections
[No.46 2017–18]
Australian War Memorial
National Gallery of Australia

Background

1. As at 30 June 2017, Australia's major¹ National Collections consisted of heritage and cultural assets estimated to be valued at more than \$10.5 billion.
2. This audit focussed on the collections held by the Australian War Memorial (Memorial), and National Gallery of Australia (NGA). The Memorial and the NGA are corporate Commonwealth entities, subject to the requirements of the *Public Governance, Performance and Accountability Act 2013*, including the Commonwealth Procurement Rules. Both entities have a legislated responsibility to develop, maintain, exhibit and utilise their collections in the national interest.

Rationale for undertaking the audit

3. Of Australia's National Collections, those held by the Memorial and the NGA are arguably the best known. Together, these entities are responsible for safeguarding assets valued at over \$7 billion, or 70 per cent of the total value of Australia's National Collections, holding items of historical, academic, and cultural value to the Australian people.
4. Effective collections management encompasses a range of different activities, including:
 - collections practical management - practices that directly support care for the collection, such as the way items are handled, conserved, stored, secured, displayed and accounted for; and
 - collections governance - effective collection management must also be supported through governance practices, strategic frameworks for the development of the collection, risk management, sound acquisition and disposal processes, and strong financial management controls that enable an entity to develop, maintain and exhibit the National Collection for the Australian people.

This audit has been undertaken to provide transparency into the collections management practices of these institutions from both a practical management and governance perspective.

Audit objective and criteria

5. The objective of this audit was to assess whether the Australian War Memorial and the National Gallery of Australia have implemented effective collection management practices. To form a conclusion against the audit objective, the ANAO adopted the following high-level audit criteria. The Memorial and the NGA have:
 - established effective strategic frameworks to support the management of their collections; and

¹ There are several smaller collections held by the Commonwealth, such as the Bundanon Trust. The Commonwealth also holds significant heritage and cultural assets as part of the Australian Parliament House collections.

- implemented effective systems and processes for managing their collections.

Conclusion

6. The Australian War Memorial has implemented collection management practices which are effective. The National Gallery of Australia's collection management practices are not fully effective due to deficiencies in financial and asset management controls.

7. The Memorial has effective governance and risk management frameworks. The Memorial's framework for collections management requires improvement in relation to the establishment of a central and consistent storage, monitoring and reviewing process for relevant framework documents.

8. The effectiveness of the NGA's governance and financial management controls requires improvement, with the entity in a high risk financial position. At the time of the audit, the NGA was developing a financial sustainability plan to address its financial position. The NGA's collection management documentation framework requires improvement by ensuring that relevant policies, plans and procedures are finalised and in place and that structured review, update and storage arrangements for these documents are established. The NGA's risk management framework is yet to reach a state of maturity.

9. Review of the Memorial's collections management systems and processes found that:

- the Memorial's Collection Development Plan has been out-of-date for five years;
- the Memorial does not have a conservation plan in place to identify and prioritise its conservation activities, and it is difficult to assess whether the Memorial has allocated sufficient resources to conservation;
- storage at the Memorial has been well planned and funded; and
- security at the Memorial is well controlled.

10. Review of the NGA's collections management systems and processes found that:

- the NGA's planned conservation activities exceed the current resources allocated by management;
- the condition of the NGA's storage arrangements and backlog of remedial work present a risk to workplace health and safety and to the optimal maintenance of the collection if not addressed and resourced in a timely manner; and
- NGA's security requires improvement to be compliant with the Commonwealth Protective Security Policy Framework, noting compliance is not mandatory.

11. Both entities utilise a formal collection management system which assists in accounting for the collection, and adopt a risk-based approach to stocktakes.

Supporting findings

Governance and Strategic Frameworks of the National Collections

12. The Memorial was found to have established effective governance structures to oversee its strategic responsibilities for the National Collection. At the NGA, governance requires improvement to ensure the Council fulfils its legislative obligations in relation to financial management.

13. The Memorial was found to be in a sound financial position, with positive liquidity and evidence that it has operated consistently within its fiscal parameters. The NGA is in an 'at risk' financial position, with cash flow problems. In February 2018 solvency was added to the NGA's strategic risk register as a 'major' risk, and needs to be considered in conjunction with such issues as the urgent maintenance works required to the Gallery building.

14. Allied to the issue of financial sustainability is the treatment by each entity of government equity injections in relation to the Collection Development Acquisition Budget (CDAB), described as ‘funding provided to Designated Collection Institutions to allow them to grow and maintain their heritage and cultural asset collections’. The Memorial has appropriate controls around the utilisation of CDAB funding. The NGA has used injections of equity, designed for the purchase and maintenance of the artworks, for operating costs. This does not meet the intent of Parliament in its appropriation of funding under CDAB.

15. Each entity lacks a meaningful performance framework aligned to program objectives. The Memorial does not include any performance indicators or measures in its Portfolio Budget Statements (PBS) or Corporate Plan.

16. The Memorial and the NGA have partially established documentation in relation to their collections management frameworks. There is scope to improve how the entities manage the policies, plans and procedures which make up their collection management frameworks. In particular, both entities should establish arrangements to centrally and consistently store, monitor and review relevant framework documents.

17. The Memorial has well embedded risk management processes, allowing management to monitor and respond to key risks. Improvements to NGA’s risk management framework were observed, however these began in 2017 and hence are yet to reach a state of maturity. Improvements are required in how senior management monitors and responds to risks and how risks are reported.

Management of the National Collections

18. The Memorial’s and the NGA’s planning and monitoring of the development of their collections is partially effective. The Memorial’s Collection Development Plan has been out of date for five years. The development and implementation of a revised Memorial Collection Development Plan has been identified as a key action item since 2014. The NGA operates under an Art Acquisition Statement of Intent², with nine departmental acquisition strategies supporting the Statement of Intent. The final strategies are planned to be completed in August 2018 under the incoming NGA director.

19. The audit identified improvements required to support the effective implementation of collection development policies and procedures. In particular:

- the Memorial needs to continue its efforts to establish and implement its policies and procedures for acquisitions and disposals in order to promote a consistent approach; and
- the NGA needs to better consider the whole-of-life costs of an acquisition by directly involving the storage and conservation teams in the acquisition process and more clearly documenting approvals of acquisitions.

20. The Memorial does not have a conservation plan in place to identify and prioritise its conservation activities. Conservation activities are therefore ad-hoc, and it is also difficult to assess whether the Memorial has allocated sufficient resources to conservation.

21. The NGA’s planned conservation activities exceed the resources currently allocated by management. The NGA needs to align resources and risks with its business priorities in relation to conservation.

² Previously known as the Art Acquisition Strategy.

22. In 2012, the Memorial identified long-term storage needs as an issue, particularly for its large objects collection. As a result, the Memorial, using accumulated funds, redeveloped its Mitchell storage premises, which was to provide an additional 10 years of storage for its large objects.

23. The NGA's National Collection storage onsite at Parkes and offsite at Hume is nearing capacity. This presents risks to workplace health and safety and to the optimal maintenance of the collection if not addressed and resourced in a timely manner.

24. The NGA's financial situation has significantly impacted on building maintenance, and the NGA faces critical infrastructure risks. The storage and display of its collection in less than optimal accommodation is a risk to both the artwork and to the NGA's reputation.³

25. The audit found that security at the Memorial is well controlled. NGA's security requires improvement to be compliant with the Commonwealth Protective Security Policy Framework, noting that compliance is not mandatory.

26. Both entities utilise a formal collection management system (CMS) which assists in accounting for the collection and both entities utilised a risk based approach to stocktaking. At the Memorial stocktakes cover approximately 80 per cent of the financial value of the collection, whilst at the NGA this figure is 71 per cent. The Memorial had 489 items, and the NGA 18 items, which have been recorded as unable to be located during the stocktake process. As at January 2018, the NGA had 809 items that were recorded as 'to be located' in their CMS, which indicates that the NGA has legacy data issues to investigate.

Recommendations

Recommendation no.1 The National Gallery of Australia develop and implement a multi-year financial plan to improve its ratio of expense to revenue.

Paragraph 2.22 **National Gallery of Australia response:** *Agreed.*

Recommendation no.2 The National Gallery of Australia ensure that Collection Development Acquisition Budget funds are utilised for the specific purpose for which they are appropriated.

Paragraph 2.30 **National Gallery of Australia response:** *Agreed.*

³ The NGA received \$16.6 million in the May 2018 Budget and a further \$4.9 million grant from the Department of Communications and the Arts to assist in upgrading NGA's Parkes building.

Recommendation no.3

Paragraph 2.64

The ANAO recommends that the Australian War Memorial and the National Gallery of Australia improve their collection management frameworks by:

- identifying all of the policies, plans and procedures which are relevant to the management of their collections;
- assessing and filling gaps in policies, plans and procedures against applicable standards;
- establishing a structured and regular system of review to ensure that all policies, plans and procedures are up to date; and
- developing arrangements to provide ongoing and consistent storage of and access to collection management policies, plans and procedures.

Australian War Memorial response: *Agreed.*

National Gallery of Australia response: *Agreed.*

Recommendation no.4

Paragraph 3.15

To ensure that entities are effectively developing the National Collections, the ANAO recommends the:

- (a) Australian War Memorial review and update its Collection Development Plan; and
- (b) Australian War Memorial and National Gallery of Australia:
 - establish a structured process to support the development of and monitoring against their respective Collection Development Plan and Art Acquisition Statement of Intent;
 - publish a full or modified version of their Collection Development Plan and Art Acquisition Statement of Intent on their websites; and
 - assess their collections to identify items for disposal/deaccession and establish a plan for removing these items from their collections.

Australian War Memorial response: *Agreed.*

National Gallery of Australia response: *Agreed.*

Recommendation no.5

Paragraph 3.26

The ANAO recommends that the Australian War Memorial continue to improve its acquisition procedures including:

- specifying how the acquisition aligns with the approved Collection Development Plan; and
- assessing the whole-of-life costs of acquisitions in line with the requirements of the Commonwealth Procurement Rules and providing this information to the decision maker.

Australian War Memorial response: *Agreed.*

Recommendation no.6 The National Gallery of Australia improve proposals for acquiring items into its collection by:

Paragraph 3.35

- assessing the whole-of-life costs of acquisitions, in line with the requirements of the Commonwealth Procurement Rules and providing the costs to the delegate;
- investigating the items located in storage areas on the NGA's premises and processing any unaccessioned items as a priority; and
- setting and monitoring standards for the timely processing of proposed acquisitions that have been brought onto the NGA's premises.

National Gallery of Australia response: *Agreed.*

Recommendation no.7 To assist entities in meeting their legislated responsibilities to maintain the National Collections, the ANAO recommends that:

Paragraph 3.60

- (a) the Australian War Memorial review and update its Collection Preservation Plan; and
- (b) the Australian War Memorial and National Gallery of Australia review the resources allocated to conservation activities to ensure that these resources are aligned to conservation risks, meet collection management standards and are appropriate for achieving business priorities.

Australian War Memorial response: *Agreed.*

National Gallery of Australia response: *Agreed.*

Recommendation no.8 The ANAO recommends that the National Gallery of Australia develop and implement a long-term storage solution for the National Collection, ensuring compliance with storage standards for artworks. In the interim, that storage considerations should become a key part of a revised acquisition process.

Paragraph 3.77

National Gallery of Australia response: *Agreed.*

Recommendation no.9 The ANAO recommends that the National Gallery of Australia ensure that it has a fully funded plan in place to provide timely maintenance and replacement of critical infrastructure.

Paragraph 3.87

National Gallery of Australia response: *Agreed.*

Summary of entity responses

27. Summary responses from the entities are provided below.

Australian War Memorial

The Memorial acknowledges the conclusions of the audit and the findings regarding effective governance and risk management frameworks; well planned and funded storage; well controlled security; and sound financial position and use of funding.

The Memorial also acknowledges the ANAO's findings that the collection management framework is effective and will be improved as the recommendations of the audit are implemented.

National Gallery of Australia

The NGA welcomes the ANAO Report on the Management of the National Collections, and accepts all the recommendations it makes. The NGA has been operating for many years in a context of concerning financial pressure and fully understands the ANAO's urging for greater attention to the expense/revenue ratio, and the associated risks. The NGA has recently taken firm measures to balance a decreased budget and sought to make major improvements in its operations including the development of a new Financial Sustainability Plan (approved by Council in 2017).

We are committed to a multi-year financial plan and reducing risk in all areas of our operations.

All of this has strong and relevant implications for collection management. In recent years it has been necessary to spend more than we consider ideal on collection care, given the serious backlog in areas of building maintenance and security. Following two years of careful research and planning, the NGA welcomed an extraordinary capital grant of \$16.6 million through an NPP (announced in the May 2018 Budget) and a further grant of \$4.9 million from the Department of Communications and the Arts, a total of \$21.5 million, to address the many high risk issues directly relevant to the care and safety of the collection. This represents a huge step forward, and is a key part of the NGA's continuing financial recalibration. We remain vigilant in examining the spending of appropriated funds to support the care and growth of the national collection.

The NGA enjoys a national and global reputation for its exemplary collection management processes in all aspects of handling works of art, ranging from preparation for packing and travel, to meticulous conservation approaches to works designated for exhibition, either on-site, or part of our ambitious external loans program. We accept the ANAO's recommendations on a range of collection issues, from deaccessioning, to calculating at the time of acquisition "whole of life" storage and conservation costs, and we value its commentary on the management of supporting policies, plans and procedures, including acquisition processes, and planning for future storage. NGA Management is committed to delivering appropriate actions on all the ANAO recommendations.

Key learnings for all Australian Government entities

28. Below is a summary of key learnings, which have been identified in this audit, that may be relevant for the operations of other Commonwealth entities particularly those with responsibility for managing National Collections and/or other cultural and heritage assets.

Governance and risk management

- The significance of the National Collections means that the financial and non-financial value of the assets within a collecting entity's display and storage facilities will often exceed the financial value of the facilities themselves. A shortfall in facility performance with respect to temperature, humidity or security can substantially compromise the collections they hold. Entities should ensure that budget allocations for ongoing maintenance, storage and security are appropriate according to risk.
- All entities should have systems in place to provide the Accountable Authority with assurance that budgets are being managed appropriately and within the intent of appropriations. This is particularly relevant for entities created by statute, where the relevant Act limits the conditions to which an appropriation may be allocated (for example - *developing, maintaining and exhibiting the collections in the national interest*).

Procurement

- Entities using limited tender procurements (such as when procuring works of art) must ensure they comply with the mandatory requirements of the Commonwealth Procurement Rules, including providing an assessment of whole-of-life costs.

Records Management

- To ensure that collection and other asset management frameworks are complete, up-to-date and accessible to all appropriate staff, entities should: identify all relevant policies, plans and procedures; assess and fill in any gaps in these framework documents, ensuring that they meet applicable standards; and maintain them using appropriate version control and approval. Regular review is necessary to ensure that they are current and relevant; as is maintaining them in a central and accessible location.

**Interim Report on Key Financial Controls of Major Entities
47 of 2017-2018
Financial Statement Audit**

Executive summary

1. The primary purpose of financial statements is to provide relevant, reliable information to users about a reporting entity's financial position. In the public sector, the users of financial statements include Parliament, Ministers and the community. The preparation of timely and accurate audited financial statements is also an important indicator of the effectiveness of an entity's financial management and fosters confidence in an entity on the part of users.
2. The Australian National Audit Office (ANAO) prepares annually two publications that report the outcomes of the financial statements audits of Australian government entities¹ and the Consolidated Financial Statements (CFS) of the Australian Government. These reports provide Parliament with an independent examination of the financial accounting and reporting of public sector entities.
3. This report focuses on the results of the interim audits, including an assessment of entities' key internal controls, supporting the 2017–18 financial statements audits. This report examines 26 entities, including all departments of state and a number of major Australian government entities. The entities included in the report are selected on the basis of their contribution to the income, expenses, assets and liabilities of the 2016–17 CFS. Significant and moderate findings arising from the interim audits are reported to the responsible Minister(s), and all findings are reported to those charged with governance of each entity.
4. The second report provides the results of the 2017–18 final audits of the financial statements of all Australian Government controlled entities and the CFS.

Summary of audit findings and related issues

Entity internal controls

5. A central element of the ANAO's financial statements audit methodology and the focus of the planning phase of ANAO audits is a sound understanding of an entity's environment and internal controls. This understanding informs our audit approach, including the reliance placed on entity systems to produce financial statements that are free from material misstatement. To do this, the ANAO uses the framework contained in the Australian Auditing Standard 315 *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment* (ASA 315).

¹ The term 'entity' applies to all organisations subject to the *Public Governance, Performance and Accountability Act 2013* (PGPA Act).

6. The interim audit phase includes an assessment of the effectiveness of each entity's internal controls as they relate to the risk of misstatement in the financial statements. At the completion of our interim audits for the 26 entities included in this report we noted that key elements of internal control were operating effectively for 20 entities. For five entities², except for particular finding/s outlined in chapter 3, the key elements of internal control were operating effectively to support the preparation of financial statements that are free from material misstatement. For the National Disability Insurance Agency, the ANAO identified a number of findings which reduced the level of confidence that could be placed on key elements of internal control and limited the assurance that could be obtained from that entity's control framework.

Summary of audit findings

7. A total of 99 findings were reported to the entities included in this report as a result of interim audits, comprising of nil significant, 12 moderate and 87 minor findings. This is a decrease from the interim results of 2016–17 with a total of 114 findings reported comprising two significant, 22 moderate and 90 minor findings.

8. Eighty-three per cent of moderate findings continue to be in the areas of: compliance and quality assurance frameworks supporting program payments, revenue collection and financial reporting; and management of IT controls. These areas warrant further attention by entity management.

Reporting of gifts and benefits

9. The ANAO has reviewed the gifts and benefits policies of the entities in this report. The ANAO sees merit in the development of a whole of government gifts and benefits policy setting the minimum requirements for entities to include within their policies, to promote good practice across Commonwealth entities. A gifts and benefits policy incorporating regular review and monitoring increases accountability, while transparency would be enhanced through the publication of entity gifts and benefits registers on the internet. The maintenance of a central register may assist entities in meeting accountability and transparency obligations.

Reporting relating to compliance with finance law

10. The ANAO observed that entities had processes in place for monitoring and reporting instances of non-compliance with finance law. Following changes to the mandatory external reporting of non-compliance in 2015–16, there is evidence that some entities are reducing the level of internal reporting of non-compliance captured and reported to audit committees and accountable authorities.

Reporting and auditing frameworks

Summary of developments

11. There are no significant accounting standards changes for the Commonwealth public sector for 2017–18. Major changes in accounting standards will be applicable in 2018–19 and 2019–20 with the implementation of revised standards for financial instruments, revenue and leases. The majority of entities included in this report have indicated that they are still in the planning stage of transition to

² The Departments of: Communications and the Arts; Defence; Home Affairs; the Prime Minister and Cabinet; and the Australian Taxation Office.

the new standards with approximately half of entities having both updated accounting policies and transition plans for standards expected to have a material impact.

Cost of this report

12. The cost to the ANAO of producing this report is approximately \$405,000.

Management of compliance with foreign investment obligations in residential real estate

No.48 2017–18

Australian Taxation Office

Department of the Treasury

Background

1. The Government's policy for foreign investment in residential property is to channel foreign investment into new dwellings to support additional jobs in the construction industry as well as economic growth.¹ Foreign investment applications are considered in light of that policy and the overarching principle that the proposed investment should increase Australia's housing stock.

2. Foreign investors are required to receive approval before acquiring an interest in residential real estate. Taking an interest in residential real estate prior to receiving approval is a breach of the *Foreign Acquisitions and Takeovers Act 1975*. Australia attracts a large volume of foreign investment applications for residential real estate, with 40 149 applications in 2015–16, and approvals that year totalling \$72.4 billion in proposed investments.

3. In the 2015–16 Budget, the Government announced a package of measures aimed at strengthening Australia's foreign investment framework. The package was introduced in response to a:

- Senate committee inquiry report in 2013, *Foreign Investment and the National Interest*, which included 29 recommendations; and
- House of Representatives committee 2014 *Report on Foreign Investment in Residential Real Estate*, which included 12 recommendations.

4. Subsequent to the two reports, responsibility for residential real estate under the foreign investment framework was transferred from the Department of the Treasury (Treasury) to the Australian Taxation Office (ATO), including the collection of fees, upfront screening, compliance and enforcement. Further, the ATO was responsible for establishing a register of foreign investment in agricultural land and residential real estate.

Rationale for undertaking the audit

5. The Australian National Audit Office (ANAO) selected foreign investment in residential real estate for audit because of the extent of parliamentary and public interest in the issue, including concerns that foreign investors were not complying with foreign investment obligations and purchasing properties they were not entitled to own. The audit would also indicate the impact on compliance with foreign investment in residential real estate arising from the change in administrative arrangements.

Audit objective and criteria

6. The audit objective was to assess the effectiveness of the ATO's and Treasury's management of compliance with foreign investment obligations for residential real estate.

¹ Foreign Investment Review Board, *Guidance Note 1*, p. 1, available from <http://firb.gov.au/resources/guidance/gn01/>, [accessed 2 May 2018].

7. To form a conclusion against this objective, the ANAO adopted three high level criteria:
- compliance and enforcement strategies and detection arrangements were in place to support compliance activities;
 - activities were undertaken to promote voluntary compliance and effectively address identified instances of potential non-compliance; and
 - the effectiveness of compliance arrangements was monitored and reported.

Conclusion

8. The ATO's management of compliance with foreign investment obligations for residential real estate is becoming effective as it progressively implements more sophisticated approaches to encourage compliance and detect and address non-compliance.

9. The ATO has developed processes for compiling a land register of residential real estate but faces considerable challenges in populating the register with reliable data in coming years, which it needs to overcome in order to be effective.

10. The ATO has assessed and addressed compliance risks in relation to foreign investment obligations for residential real estate but has not yet compiled and implemented a compliance and enforcement strategy. To promote voluntary compliance with those obligations, the ATO has developed a series of communication strategies. The strategies, which have largely been implemented, incorporate a multi-platform communication approach targeting key audiences with priority messages.

11. The ATO has undertaken a significant amount of work to develop processes and systems to support the detection and investigation of non-compliance with foreign investment obligations for residential real estate. There are a number of minor enhancements the ATO could make to improve its largely effective investigation processes, with more substantial work required in its development of processes to actively detect non-compliance.

12. Monitoring and reporting on compliance activities for foreign investment in residential real estate has been expanded with the transfer of responsibilities from Treasury to the ATO. Many indicators have been developed to measure the success of compliance activities and external reporting established for compliance investigations, outcomes and penalties. The monitoring and reporting arrangements are largely effective, and could be strengthened by more broad coverage of effectiveness—of the ATO in managing the overall compliance risk and Treasury in meeting the policy intent for foreign investment in residential real estate.

Supporting findings

National residential land register

13. The ATO has been compiling a land register of residential real estate by tracking settlements that have occurred since 1 July 2016, and intends to populate the register by December 2018 and report thereafter. The register will use property data from state and territory land titles offices that contains foreign investment identifiers such as foreign investment application number and passport number. In light of the time required for the states and territories to pass legislation to enable the provision of property transaction data with foreign investment identifiers, the ATO has developed interim arrangements to populate the register using data obtained through self-registration processes by foreign investors who have purchased residential real estate.

14. The ANAO's analysis identified serious deficiencies in populating the register with reliable data. There is likely under-reporting of self-registrations², over-reporting of foreign identity information in state property data³ and low levels of matching between datasets for foreign investment applications, self-registrations of foreign investment in residential property and state property data.⁴ Consequently, the ATO will need to undertake extensive manual verification processes in coming years to enable the register to provide accurate information about the nature and extent of foreign investment in residential real estate and produce reliable intelligence for compliance purposes.

Compliance strategies and voluntary compliance

15. The ATO does not have a compliance and enforcement strategy but has a reasonable basis for developing such a strategy, as it has undertaken a risk assessment of foreign investment in residential real estate and identified corresponding risk treatments. In preparing a compliance and enforcement strategy, the ATO should analyse compliance outcomes to inform targeted compliance approaches, address weaknesses in existing controls and incorporate measures of control effectiveness.

16. The ATO's information about foreign investment in residential real estate is comprehensive and readily accessible to foreign investors, stakeholders and the general public through the websites of the ATO and the Foreign Investment Review Board, which include information products in one language other than English (Chinese). There is also a residential foreign investment real estate help line and email inbox, avenues for community and stakeholder engagement, and use of social media. Activities are managed through an up-to-date communication strategy. There would be benefit in the ATO undertaking a broad evaluation of the residential foreign investment communication program to inform future communication strategies.

Detection and investigation

17. The ATO has partially effective processes to detect non-compliance with foreign investment obligations for residential real estate. It detected some 4300 cases of potential non-compliance from mid-2015 when it gained responsibility for compliance through January 2018, mainly from community or self referrals or through approval processes for foreign investors. While the ATO has established a data matching program to actively detect non-compliance, as at April 2018 the program had not addressed all identified key compliance risks and more work was required to mature its processes for actively detecting non-compliance.

18. The ATO has developed and implemented a largely effective program to address identified cases of potential non-compliance with foreign investment obligations for residential real estate in a limited timeframe. Since gaining compliance responsibilities from Treasury in May 2015 through

² While there were a number of self-registrations that could be used to populate the register (2653 to mid-December 2017), there may have been significant levels of non-registration, as the registrations represented only 7.1 per cent of applicants for such foreign investments from 1 July 2015 to mid-December 2017.

³ New South Wales (NSW) was the only jurisdiction that had data available with foreign identifiers. The ANAO's analysis identified 23 431 properties in the NSW data with at least one potential foreign identifier, which was almost twice as high as the number of foreign investors who applied for residential real estate in NSW in 1 July 2015 to 13 December 2017 (12 278). The difference is likely to reflect reporting of information in the foreign identifier fields by non-foreign investors (particularly for the nationality or citizenship and passport number fields).

⁴ Of 504 self-registrations of foreign investment in residential real estate in NSW in 1 July 2016 to 17 December 2017, there were only 56 exact matches with data from application approvals and from NSW property transaction records.

January 2018, the ATO completed 3940 investigations that identified 1158 breaches and resulted in 1067 financial penalties totalling some \$5.5 million, and the disposal of 231 foreign-owned properties valued at \$284.9 million.⁵ The key challenge for the ATO going forward will be addressing the more serious instances of non-compliance with the foreign investment framework; namely, demonstrating wilful non-compliance with obligations and applying criminal and civil penalties. There is also scope for the ATO to improve processes for escalating cases for investigation.

Monitoring and reporting

19. The ATO has over 20 indicators of success for its compliance activities for foreign investment in residential real estate, which it has measured for inclusion in a variety of internal communication and compliance processes. However, the ATO has not yet used the results to broadly assess its effectiveness in managing the overall compliance risk that ‘failure of foreign persons to comply with residential real estate foreign investment rules will undermine the integrity of the foreign investment framework and community confidence’. Similarly, Treasury has not measured effectiveness in achieving the stated policy intent of encouraging foreign investment in new residential dwellings.

20. The ATO and Treasury have largely effective arrangements in place to report on compliance activities for foreign investment in residential real estate, which could be strengthened by more broadly reporting on the effectiveness of those activities. The ATO has extensive internal reporting on compliance activities for foreign investment in residential real estate and shares this information with Treasury. Consequently, the extent of coverage in the Foreign Investment Review Board’s annual reports and Regulator Performance Framework reports has expanded since 2014–15, and includes information on compliance investigations, outcomes and penalties imposed.

Recommendations

Recommendation no. 1
Paragraph 3.13 The Australian Taxation Office compiles and implements a residential foreign investment compliance and enforcement strategy, which draws on existing risk assessment and treatment documentation and information about the results of prior compliance activities.

Australian Taxation Office’s response: *Agreed.*

Recommendation no. 2
Paragraph 4.13 The Australian Taxation Office prioritises developing and finalising data matching rules to address key compliance risks to foreign investment in residential real estate.

Australian Taxation Office’s response: *Agreed.*

Summary of entity responses

21. A summary of entity responses is shown below.

⁵ Treasury had undertaken very little compliance activity prior to the ATO gaining responsibility for managing compliance with foreign investment obligations for residential property. For example, in the *Foreign Investment Review Board Annual Report 2014–15*, Treasury reported one forced disposal and no penalty information.

Australian Taxation Office

The ATO appreciates the ANAO's efforts to undertake this audit and to provide the feedback and suggestions contained within this report. The ATO considers this report to be supportive of our overall approach to managing the administration of the *Foreign Acquisitions and Takeovers Act 1975* and the Government's foreign investment policy for the foreign investor segment. The review recognises the efforts the ATO has made in a relatively short period of time to establish a new program of work for administering foreign investment obligations in respect of residential real estate.

In finding the ATO's program to address identified non-compliance as largely effective, the review has identified a number of areas that the ATO could focus on to further enhance its effectiveness, particularly with regards to detection of non-compliance. The review also acknowledges the processes that the ATO has implemented to overcome some of the challenges that it faces in compiling a land register of residential real estate.

The ATO agrees with the two recommendations contained in the report.

Department of the Treasury

The Treasury welcomes the overall conclusions and findings of the audit.

While the report does not contain any recommendations for the Treasury, we will consider the key learnings within the report in the context of the Treasury's role in relation to administering the foreign investment framework, including our overarching policy responsibilities.

Key learnings for all Australian Government entities

22. Below is a summary of key learnings identified in this audit report that may be considered by other government entities when implementing a compliance function.

Performance and impact measurement

- In monitoring the effectiveness of the implementation of policy (such as foreign investment in residential real estate), entities should monitor the effectiveness of both compliance activities and the achievement of the broader policy intent (in this instance channelling foreign investment into new dwellings).
- If relying on third-party data (such as the ATO relying on state and territory property transaction data to identify foreign investment in residential real estate) be conservative about timelines for implementation and careful about how to ensure the data is accurate.

Governance

- When decisions are being taken about where to place a function, consideration should be given to the expertise and capability of potential delivery entities and which entity has the best fit of skills to administer the function. In the case of managing compliance with foreign investment in residential real estate, the function would have been best placed initially into the ATO rather than Treasury.
- In commencing the administration of a new function, conducting a prospective risk assessment and risk treatment plan (as the ATO did at the outset of its management of compliance with foreign investment in residential real estate) provides a sound basis for establishing a risk-based compliance function and developing an effective compliance strategy.

**Senate Order for Departmental and Entity Contracts (Financial Year 2016–17 compliance)
No.49 2017–18**

Australian Electoral Commission; Great Barrier Reef Marine Park Authority; Department of Home Affairs; Department of Infrastructure; Regional Development and Cities.

Background

1. Inappropriate use of confidentiality provisions in government contracts can impede accountability and transparency in government purchasing. The *Senate Procedural Order of Continuing Effect: Entity Contracts*¹ (the Senate Order/the Order) is based on the principle that parliamentary and public access to government contract information should not be prevented, or restricted, through the use of confidentiality provisions, unless there is sound reason to do so. Successive governments have agreed to comply with the Senate Order and have required entities to put in place suitable procedures to support Ministers to comply with it.

2. The Order requires Ministers to table letters of advice that all entities which they administer have placed on the internet lists of contracts valued at \$100,000 or more, by no later than two calendar months after the end of each financial and calendar year. These lists are to:

- include the details of each contract which has not been fully performed or which has been entered into during the previous 12 months; and
- indicate whether the contracts contain confidentiality provisions or other requirements of confidentiality, and a statement of the reasons for the confidentiality.

3. The Department of Finance (Finance) is responsible for the whole-of-government procurement policy and issues guidance to entities on their obligations, as well as tools to assist their awareness and compliance. Finance's guidance in relation to compliance with the Senate Order includes:

- *Resource Management Guide No. 403—Meeting the Senate Order on Entity Contracts* (RMG 403)²—which provides advice to entities about how to comply with the Senate Order, including how to use confidentiality provisions appropriately;
- *Buying for the Australian Government, Confidentiality Throughout the Procurement Cycle*³ (the Guidance)—which contains the Confidentiality Test, which is designed to assist entities to determine the appropriate inclusion of confidentiality provisions in contracts; and
- a dedicated email, procurementagencyadvice@finance.gov.au, to allow agencies to ask Finance questions and raise concerns regarding procurement.

¹ The *Senate Procedural Order of Continuing Effect 13: Entity Contracts*, 14 May 2015.

² Department of Finance, *Resource Management Guide No. 403—Meeting the Senate Order on Entity Contracts*, February 2017.

³ Department of Finance (Finance), *Buying for the Australian Government, Confidentiality throughout the Procurement Cycle: Practice*, [Internet], available from <<https://www.finance.gov.au/procurement/procurement-policy-and-guidance/buying/contract-issues/confidentiality-procurement-cycle/practice.html>> [accessed May 2018].

Rationale for undertaking the audit

4. The Auditor-General decided to undertake performance audits of entities' use and reporting of confidentiality provisions as requested under the Senate Order. The coverage of this report reflects requests made to the Auditor-General in the:

- initial Senate Order (20 June 2001) which asked the Auditor-General to examine a number of contracts listed on entity websites and indicate whether there had been any inappropriate use of confidentiality provisions; and
- amended Senate Order (27 September 2001) which requested that the Auditor-General include an examination of a number of contracts that have not been included in a list and to indicate whether the contracts should be listed.

5. This is the second of two reports the Auditor-General was requested to provide to the Senate when the Senate Order was amended on 14 May 2015⁴ and is the twentieth audit of the Senate Order undertaken since 2001.

Audit objective and criteria

6. The objective of the audit was to assess the appropriateness of the use and reporting of confidentiality provisions in a sample of Australian government contracts. The ANAO's assessment was based on the following criteria:

- confidentiality provisions have been used appropriately in a sample of Australian Government contracts which were reported by the selected entities to contain confidentiality provisions;
- contract information listed on AusTender was accurate; and
- Ministers' letters have been tabled in accordance with the timing and content requirements of the Senate Order.

7. The entities assessed for criterion one were the: Australian Electoral Commission (AEC); Great Barrier Reef Marine Park Authority (GBRMPA); Department of Home Affairs (Home Affairs)⁵; and Department of Infrastructure, Regional Development and Cities (Infrastructure).

Conclusion

8. Confidentiality provisions continue to be inappropriately used and reported by Australian Government entities. Transparency in government contracting would benefit from entities reviewing how confidentiality is assessed and reported and seeking assistance from Finance to confirm that there is a sound reason to apply confidentiality provisions in contracts.

9. Overall compliance with the Senate Order is still not being achieved. There remains scope for entities to be clearer in their application of the Department of Finance's guidance on assessing and reporting confidentiality and for that guidance to provide further context to assist entities to appropriately assess the supplier claims.

10. Financial year 2016–17 results indicate significant improvement in the accuracy of contract information reported on AusTender.

⁴ *Senate Procedural Order of Continuing Effect 13: Entity Contracts*, 14 May 2015, paragraph five.

⁵ Contracts examined from the Department of Home Affairs included only those entered into by the Department of Immigration and Border Protection. The Audit Work Plan and contract sample was approved before the Department of Home Affairs was formally established on 20 December 2017.

11. For calendar years 2016 and 2017 respectively, 58 per cent and 71 per cent of Ministers' letters were tabled in accordance with the timing and content requirements of the Senate Order. These results are broadly in line with results for calendar year 2015.

Supporting findings

Use of Confidentiality provisions

12. In the sample of contracts, the ANAO found that for 86 per cent of the contracts examined, the use of confidentiality provisions did not comply with Department of Finance guidance (60 per cent) or the contracts did not contain specific confidentiality provisions and were therefore misreported (26 per cent). The audited entities were not able to consistently demonstrate the objective basis for suppliers' claims for confidentiality or their reasons for agreeing for the information to remain confidential.

13. The information contained within 53 of the 62 contracts reviewed (85 per cent) aligned with that reported on AusTender.

14. Of the 62 confidential and non-confidential contracts examined by the ANAO, 59 contracts (95 per cent) included both parliamentary disclosure and ANAO access clauses.

Ministers' letters

15. Ministers provided letters of advice to the Senate for: 50 non-corporate Commonwealth entities (58 per cent) by the due date for the 2016 calendar year reporting period (28 February 2017); and 109 corporate and non-corporate Commonwealth entities (71 per cent) by the due date for the 2017 calendar year reporting period (28 February 2018).

16. The content of the Ministers' letters issued for non-corporate Commonwealth entities largely complied with the content requirements of the Senate Order for excluded contracts. ANAO analysis of Ministers' letters for the 2017 calendar year reporting period suggests that some corporate Commonwealth entities could better understand their obligations under the Senate Order regarding excluded contracts.

17. Entities' listings did not always meet the content requirements of the Senate Order. The most frequent errors in listings were not including the subject matter and not specifying reasons for confidentiality.

18. Sixty per cent of non-corporate Commonwealth entities reported a cost of complying with the Senate Order in the 2016–17 financial year and 53 per cent of corporate Commonwealth entities reported a cost of complying with the Senate Order for the 2017 calendar year. Overall costs ranged from nil to \$49,443.

Recommendations

Recommendation no.1 That all entities meet all mandatory requirements set out in *Senate Order 13: Entity Contracts*, in particular, that contract listings do not contain any inappropriate confidentiality provisions.

Paragraph 2.14

Australian Electoral Commission response: *Agreed*

Great Barrier Reef Marine Park Authority response: *Agreed*

Department of Home Affairs response: *Agreed*

Department of Infrastructure, Regional Development and Cities response: *Agreed*

Recommendation no.2 That all entities document their consideration of supplier confidentiality requests against the Confidentiality Test to provide a record of the reasons for agreeing to any confidentiality provisions and the basis for future decisions.

Paragraph 2.24

Australian Electoral Commission response: *Agreed*

Great Barrier Reef Marine Park Authority response: *Agreed*

Department of Home Affairs response: *Agreed*

Department of Infrastructure, Regional Development and Cities response: *Agreed*

Key learnings for all Australian Government entities

19. Below is a summary of key learnings, including instances of good practice, which have been identified in this and previous audits of the Senate Order that may be relevant for the operations of other Commonwealth entities.

Procurement

- In developing and negotiating contracts, entities should be aware that the Parliament, through the Senate has sought transparency and accountability in procurement arrangements.
- Government contracts should not contain confidentiality provisions unless the supplier can: provide an objective basis for the request; demonstrate that the information is sensitive; and identify a real risk of damage to commercial interests flowing from disclosure.
- The appropriate balance between the interests of accountability and transparency, and appropriate protection of commercial interests should be assessed in each case, throughout the procurement process.
- To further support transparent decision-making, entities should establish processes to support the capture and reporting of information relating to their assessment of claims of confidentiality and decisions.

Primary healthcare grants under the Indigenous Australians' Health Program

No.50 2017–18

Department of Health

Background

1. The Indigenous Australians' Health Program (IAHP) was established in 2014 through the consolidation of four existing Indigenous health funding streams administered by the Department of Health (the department). The IAHP aims to provide Aboriginal and Torres Strait Islander people with access to effective high quality, comprehensive, culturally appropriate, primary healthcare services in urban, regional, rural and remote locations across Australia. Primary healthcare services are usually the 'entry point' for persons into the broader health system and can be contrasted to services provided through hospitals or when people are referred to specialists.
2. The bulk of IAHP expenditure is via grants. Since 2015, IAHP primary healthcare grants totalling approximately \$1.44 billion have been awarded with 85 per cent of this funding going to Aboriginal Community Controlled Health Organisations.
3. As at March 2018, a total of 164 organisations are receiving IAHP primary healthcare grant funding. In 2016–17, IAHP-funded services provided primary healthcare services to an estimated 352,000 Indigenous Australians. This represents 54.2 per cent of the estimated total Indigenous population.

Rationale for undertaking the audit

4. The IAHP was selected for audit because it is intended to contribute towards achieving the Indigenous health-related 'Closing the Gap' targets regarding life expectancy and infant mortality. The program represents the Australian Government's largest direct expenditure on Indigenous primary healthcare.

Audit objective and criteria

5. The audit objective was to assess the effectiveness of the Department of Health's design, implementation and administration of primary healthcare grants under the IAHP.
6. To form a conclusion against this objective, the ANAO adopted the following high-level criteria:
 - Did the department design the IAHP primary healthcare components consistent with the Government's objectives in establishing the IAHP?
 - Has implementation of the IAHP primary healthcare components been supported through effective coordination with key Government and non-Government stakeholders?
 - Has the department's approach to assessing primary healthcare funding applications and negotiating funding agreements been consistent with the Commonwealth Grant Rules and Guidelines?
 - Has the department implemented a performance framework that supports effective management of individual primary healthcare grants and enables ongoing assessment of program performance and progress towards outcomes?

Conclusion

7. The department's design and implementation of the primary healthcare component of the IAHP was partially effective as it has not yet achieved all of the Australian Government's objectives in establishing the program. The department has not implemented the planned funding allocation model and there are shortcomings in performance monitoring and reporting arrangements. However, the department has consolidated the program, supported it through coordination and information-sharing activities and continued grant funding.

8. The Government's original objectives in establishing the IAHP are due to be fully achieved in 2019–20, four years later than originally planned. The majority of IAHP primary healthcare grant funding to date has been allocated in essentially the same manner as previous arrangements rather than the originally intended needs based model. Program implementation has been supported through appropriately aligning funding streams to intended outcomes and coordination and information-sharing with relevant stakeholders.

9. Most aspects of the department's assessment of IAHP primary healthcare funding applications and negotiation of funding agreements were consistent with the Commonwealth Grants Rules and Guidelines (CGRGs). The exception to this was the poor assessment of value for money regarding the majority of grant funds. The grant funding agreements were fit for purpose, but the department has not established service-related performance benchmarks for funded organisations that were provided for in most of the agreements.

10. The department has not developed a performance framework for the Indigenous Australians' Health Program. Extensive public reporting on Indigenous health provides a high level of transparency on the extent to which the Australian Government's objectives in Indigenous health are being achieved. However, this reporting includes organisations not funded under the IAHP and, as such, it is not specific enough to measure the extent to which IAHP funded services are contributing to achieving program outcomes.

11. In managing IAHP primary healthcare grants, the department has not used the available provisions in the funding agreements to set quantitative benchmarks for grant recipients. This limits its ability to effectively use available performance data for monitoring and continuous quality improvement. Systems are in place to collect performance data, but systems for collecting quantitative performance data have not been effective. Issues with performance data collection limit its usefulness for longitudinal analysis.

Supporting findings

Program design and implementation

12. The design of the IAHP was consistent with the Government's objectives of achieving budget savings and reducing administrative complexity through consolidation of existing grant programs. The objective of allocating primary healthcare grant funding on a more transparent needs basis will not be achieved until 2019–20, four years behind the timetable agreed by Government in establishing the IAHP.

13. Three outcomes were established for the program and set out in published IAHP grant guidelines. One of the outcomes does not clearly identify the desired end result. IAHP funding, including the primary healthcare component, are appropriately aligned to the outcomes.

14. The department uses a wide variety of forums and networks to share information and seek feedback about its current and planned Indigenous health activities, including the IAHP. Some coordination and joint planning activities relating to primary healthcare have also been undertaken through the Aboriginal Health Partnership Forums.

Awarding Grants

15. Ninety eight per cent of IAHP primary healthcare grant funding has been provided through non-competitive processes. The department obtained Ministerial agreement for these processes.

16. Most aspects of the assessment of funding proposals were undertaken consistently with the CGRGs and IAHP guidelines. The exception was assessment of value for money. Assessment records for some funding rounds, including the \$1.23 billion 'bulk' round undertaken in 2015, lacked evidence of substantive analysis of value of money considerations. The department was also unable to provide evidence it had undertaken a value for money assessment regarding the \$114 million grant to the Northern Territory Government. In virtually all cases, risk assessments formed part of the assessment process.

17. Departmental delegates were provided with sufficient advice to enable them to discharge their obligations under the *Public Governance, Performance and Accountability Act 2014* in approving IAHP grant proposals. The timeliness of the advice varied, but was provided relatively quickly for the larger 2015 funding rounds.

18. Funding agreements are fit for purpose, using a grant head agreement and an IAHP-specific schedule. The specific services to be provided by each funded organisation are set out in separate Action Plans, which are appropriately referenced in the agreement schedule. The agreements with Aboriginal Community Controlled Health Organisations allow for the setting of individual performance targets, but no targets have been set. All agreements also clearly set out reporting requirements.

Monitoring and Reporting

19. The department has not established a performance framework for the primary healthcare component of the IAHP.

20. Systems are in place to collect performance data, but systems to collect quantitative performance data have not been effective. Several changes to data collection processes have resulted in an increased reporting burden on IAHP grant recipients and two six-monthly data collections being discarded or uncollected. These breaks in the data series limit its usefulness for longitudinal analysis of performance trends. The department has commenced projects to improve the quality of data, but has limited assurance over the quality of data collected before 2017 as it has not been validated.

21. The department relies on public reporting of a range of Indigenous health indicators to monitor achievement of program outcomes. The reporting includes data about services not funded under the IAHP. As such, it is not specific enough to measure the extent to which IAHP funded services are contributing to achieving program outcomes. The department was also unable to demonstrate how it used the data to inform relevant policy advice and program administration.

22. The department is not effectively using available performance data to monitor IAHP grant recipient performance and has not set quantitative national key performance indicator (nKPI) based benchmarks for grant recipients. The department's ability to set performance expectations and assess actual performance is limited by the currency of data and variability in the content of Action Plans.

Recommendations

Recommendation no.1
Paragraph 3.21 The Department of Health improve the quality of IAHP primary healthcare value for money assessments, including ensuring their consistency with the new funding allocation model.

Department of Health response: *Agreed.*

Recommendation no.2
Paragraph 4.10 The Department of Health assess the risks involved in IAHP-funded healthcare services using various clinical information software systems to support the direct online service reporting and national key performance indicator reporting process, and appropriately mitigate any significant identified risks.

Department of Health response: *Agreed.*

Recommendation no.3
Paragraph 4.30 The Department of Health ensure that new IAHP funding agreements for primary healthcare services include measurable performance targets that are aligned with program outcomes and that it monitors grant recipient performance against these targets.

Department of Health response: *Agreed.*

Summary of entity response

23. The Department of Health ('the Department') notes the findings of the report and agrees with the recommendations.

24. It is pleasing that the report finds: the program has been consolidated and supported through coordination and information sharing activities; programme implementation has appropriately aligned funding streams to intended outcomes; and the objective of reducing administrative complexity has been achieved.

25. Work is already underway within the Department which aligns with the report's recommendations, and the report provides a platform to continue these efforts. In particular, the Department has introduced more robust assessment processes for primary health care grants under the Indigenous Australians' Health Programme and has also commenced development of enhanced performance measurements of program outcomes, supported by an outcomes-focussed policy framework. The Department's responses to the individual recommendations provide further detail.

26. The report identifies that the introduction of a new funding allocation model for the distribution of primary health care funding as announced in the 2014–15 Budget is yet to be completed and finds that this deferral has contributed to a partially effective implementation of the Australian Government's objectives in establishing the programme. The Government announced in the 2018–19 Budget that the model will be implemented from 1 July 2019 and the Department will continue to work closely with Aboriginal Community Controlled Health Services to deliver this important initiative. The Department notes that this deferral occurred in the context of extensive stakeholder engagement together with significant data improvement activities designed to support a robust and well-developed funding model.

27. Whilst the Department is committed to continuous improvement of the administration of the Indigenous Australians' Health Programme, the Department wishes to acknowledge and recognise the significant contribution our network of Aboriginal Community Controlled Health Services are making to improve the health of their communities under the Australian Government's Closing the Gap agenda.

Key learnings for all Australian Government entities

28. Below is a summary of key learnings which have been identified in this audit that may be relevant for the operations of other Commonwealth entities.

Performance and impact measurement

- Entities collecting grant performance data should validate the accuracy of data early in the collection cycle or as soon as practical. Validation methodology should take into account the size of the grant program, the key risks to data accuracy, and importance of performance data in influencing future Commonwealth investment in the relevant area.
- Entities should have a clear policy covering the collection, storage, ownership, access and usage of performance data. The policy and associated operational documents should be periodically reviewed and updated to reflect significant changes to processes and systems.

Program design

- Estimated timeframes for program design should be based on an informed assessment of the level of work involved and relevant risks to achieving any key stakeholder support considered essential to the success of the program.

Summary and recommendations

Background

1. In 2017–18 the Australian Government budgeted \$75.3 billion on healthcare representing around 16 per cent of all expenditure. Key drivers of health expenditure are Australia's growing and ageing population, as well as the increasing prevalence of chronic disease and the use of new, but costly technologies in the treatment of illness. In recent years, the Government has pursued a range of strategies to manage the growth in costs of health services and to increase the efficiency of health administration.

2. Following the 2013 election, the Australian Government established processes to examine the appropriate role and scope of government activity as part of its Smaller Government Reform agenda. A series of 'portfolio stocktakes' were undertaken across government under the Efficiency through Contestability Programme instigated by the Minister for Finance. A Functional and Efficiency Review (FER) of the Department of Health (Health or the department), conducted between January and March 2015, made 90 recommendations for clarifying the roles and responsibilities of the department and increasing the efficiency of its operations. The review formed the basis of significant Budget savings.

3. The Department of Health is responsible for implementing the Australian Government's health priorities. The role of the department is to provide high quality advice to the Minister for Health on how the Government's objectives can be met and to action the Government's decisions in line with its overall policy agenda. Within the context of the annual Budget this involves developing policy options for the allocation of funding to give effect to the Government's priorities.

4. In the 2014–15 and 2015–16 Budgets, the health portfolio committed to deliver \$1.2 billion in savings over the forward estimates through a number of measures aimed at achieving the Government's objectives for fiscal constraint. The measures encompassed:

- election commitments to reduce duplication in spending by abolishing two small agencies established under the previous government;
- administered program measures where funds were to be returned to Budget or reallocated to other health policy or program priorities; and
- departmental measures which were to increase the efficiency of the department's activity.

Rationale for undertaking the audit

5. Health's management of savings measures was selected for audit because of the scale of health expenditure and the importance of sound financial management for the Australian Government's overall fiscal position. Sound decision-making and the effective implementation of health savings supports the ability of the Government to maintain service provision into the future. Health has not reported on the impact of the savings measures on its delivery of programs through its annual reports or other means. The audit therefore provides information to Parliament about the status of the Budget measures and has the potential to inform the management and reporting of savings measures by other entities.

Audit objective and criteria

6. The objective of the audit was to assess the Department of Health's design, monitoring and implementation of select 2014–15 and 2015–16 Budget measures aimed at achieving significant savings and other benefits. To form a conclusion against this objective, the ANAO adopted the following high level criteria:

- Were sound processes and practices established to support the design and implementation of specific measures?
- Is the achievement of savings and benefits being appropriately monitored?
- Is implementation of the measures on track?

7. The budget measures are set out below.

Budget 2014–15

- Smaller Government: Australian National Preventive Health Agency (\$6.4 million over five years from 2013–14, departmental)
- Smaller Government: More Efficient Health Workforce Development (\$142 million over five years from 2013–14, departmental).

Budget 2015–16

- Rationalising and Streamlining Health Programs (\$962.8 million over five years from 2014–15, administered)
- Smaller Government: Health Portfolio (\$113.1 million over five years from 2014–15, departmental).

Conclusion

8. The Department of Health was effective in designing the Government's savings commitments. While administered savings were effectively implemented and monitored, the department lacked appropriate arrangements to monitor the implementation and impact of departmental efficiency savings.

9. Health used generally sound processes and practices to support the design and implementation of savings measures. The design of measures was consistent with guidance provided by the Department of Finance and the department's internal budgeting processes. Advice to the Government to inform decision-making on the nature and extent of savings to health spending was relevant and timely.

10. The achievement of savings and benefits has not been sufficiently monitored. The department did not have robust information management systems in place to enable it to produce accurate reports on the status of grants from administered funds. Since the 2015–16 Budget the department has improved its governance arrangements for the management of administered appropriations and strengthened its systems for tracking grant expenditure. Health's monitoring of departmental savings measures focused on high-level information about implementation activities and did not include information about reductions in operating costs or the achievement of specific benefits.

11. The department made appropriate adjustments to internal administered and departmental budget allocations to reflect the Government's decision-making. The department did not establish arrangements to inform itself of the extent to which the intended benefits of efficiency measures had been realised.

Supporting findings

The design of measures

12. Health developed administered savings options in line with guidance provided by Finance. It designed measures, in the first instance, by drawing on uncommitted funding, consistent with its internal budgeting processes. In identifying further opportunities for savings, the department was responsive to the Government's priorities and developed proposals based on policy considerations and program evidence. In designing departmental savings measures Health did not develop costings for all efficiency measures. There is merit in Health strengthening its approach to quantifying potential savings and establishing baselines for measuring their impact on efficiency during implementation.

13. Advice provided to government on administered savings was appropriate, regular, and reflected the Government's policy and fiscal objectives. Health informed the Minister of its response to Functional and Efficiency Review (FER) recommendations and proposed a range of departmental efficiency measures. The department did not provide further briefing to the Minister on matters arising from the FER, including in relation to further work and consultation that it had committed to undertake. Health's advice to the Government to support the abolition of the Australian National Preventive Health Agency (ANPHA) and Health Workforce Australia (HWA) was relevant and timely and included options for managing risks.

14. The department's planning for the implementation of administered savings was generally appropriate, except for the lack of a coordinated strategy for engaging external stakeholders. The department has undertaken work since 2015–16 to improve its Budget stakeholder engagement processes. While departmental measures were incorporated into portfolio-wide plans for organisational change, Health did not undertake sufficient project planning for the measures in relation to implementation risks and mitigation strategies. The department developed timely, fit-for-purpose plans to support the abolition of ANPHA and HWA. Monitoring of savings and benefits

15. Health used appropriate oversight arrangements to monitor the implementation of administered and departmental measures. 16. The oversight arrangements for departmental savings were undermined by a lack of appropriate measures to monitor the progress of implementation and its impact. The integration of efficiency measures into the department's broader change program (Health Capability Program) reduced visibility of the department's progress in achieving the efficiency outcomes.

Implementation and outcomes

17. Health made internal financial adjustments to give effect to the Government's savings decisions. The department did not fully implement all of the efficiency measures included in the Smaller Government: Health Portfolio budget measure. In line with the Government's decision to reduce duplication, ANPHA and HWA were abolished by the end of 2014–15 and functions were transferred to the department. However, the department has generally not retained documentation on performance outcomes.

18. The savings measures contributed to the Government's fiscal agenda by reducing funding for programs, activities and departmental functions. In the absence of reliable information the department is unable to assure itself of whether efficiencies have been achieved. The abolition of ANPHA and HWA reduced duplication in the delivery of health workforce and preventive health functions.

Recommendation

Recommendation no.1 That the Department of Health apply fit-for-purpose performance criteria to assist it to monitor the implementation of savings measures and assess their impact.
Paragraph 3.19

Department of Health response: *Agreed.*

Summary of entity response

19. The Department of Health notes the audit findings and agrees with the recommendation. I am pleased that the ANAO concluded that Health was effective in designing the Government's savings commitments, and that it used generally sound processes and practices to support the design and implementation of savings measures. The audit acknowledges the steps taken by Health since the 2015–16 Budget to improve its governance arrangements for the management and strengthening of systems for tracking administered expenditure, as well as work undertaken to improve the Budget stakeholder engagement process. The Department of Health supports the key learnings identified for consideration by all entities.

Key learnings for all Australian Government entities

20. Below is a summary of key learnings, including instances of good practice, which have been identified in this audit that may be relevant for the operations of other Commonwealth entities.

Policy design

To support implementation and the realisation of intended benefits, savings measures should be costed using information on cost drivers, desired levels of performance and baseline data.

Review and evaluation arrangements for budget savings measures should be identified in the design phase and include access to reliable sources of data to help measure the extent to which the intended impact of departmental efficiency measures has been achieved.

Governance and risk management

To support the effective implementation of significant savings measures, entities should prepare project plans that outline savings and benefits, identify implementation risks and consider the need to engage with stakeholders on the implications of the Government's decision-making.

Performance and impact measurement

When implementing new initiatives and savings measures, trends in performance against baseline data should be monitored to assess whether objectives are being achieved, and to identify and share successful examples of implementation or new approaches.

**Efficiency of Veterans Service Delivery by the Department of Veterans' Affairs
No.52 2017-18
Department of Veterans' Affairs**

Summary and recommendations

Background

1. The Department of Veterans' Affairs (DVA) provides support to current and former Australian Defence Force (ADF) members and their families, ranging from financial support, treatment and services. DVA administers financial and services support under three main pieces of legislation: the *Veterans' Entitlement Act 1986* (VEA); the *Military, Rehabilitation and Compensation Act 2004* (MRCA) and the *Safety, Rehabilitation and Compensation (Defence-related Claims) Act 1988* (DRCA).
2. DVA supported approximately 165,000 veterans and more than 125,000 dependents in 2016-17 at a cost of more than \$12 billion.
3. DVA has approximately 2,000 staff with offices in every State and Territory. Its work is delivered through specialised service delivery programs distributed across its offices.

Rationale for undertaking the audit

4. In August 2017, the Senate Standing Committee on Foreign Affairs, Defence and Trade delivered its report following an inquiry into suicide by veterans and ex-service personnel; *The Constant Battle: Suicide by Veterans*. The report stated that: 'The need to streamline the administrative practices of DVA was the overwhelming concern of the majority of submissions to the inquiry'. Report Recommendation 13 was that the Australian National Audit Office commence the proposed performance audit of the efficiency of veterans' service delivery by DVA as soon as possible.
5. Additional factors supporting the conduct of the audit included:
 - Commencing in 2017–18, the Government provided DVA with \$166.6 million over four years to begin transforming and improving services to more effectively and efficiently meet the current and future needs of veterans and their dependents. The measure is titled 'Veteran Centric Reform'. The audit examined some of the results of DVA's early implementation of the reform.
 - A *Functional and Efficiency Review* (May 2016) of DVA recommended that service delivery functions either be outsourced or transferred to other agencies. The review stated that the reform would lead to 'administrative efficiencies'. This audit included analysis of the efficiency of DVA's Rehabilitation and Compensation (R&C) processes.

Audit objective and criteria

6. The objective of the audit was to assess whether DVA was efficiently delivering services to veterans and their dependents. To form a conclusion against the audit objective, the Australian National Audit Office (ANAO) adopted the following high-level audit criteria:
 - Do business systems and processes in DVA support the efficient delivery of services to veterans and their dependants?
 - Have compensation, support and health services been delivered efficiently by DVA to veterans and their dependants?

Conclusion

7. The majority of DVA Rehabilitation & Compensation (R&C) services are being delivered to veterans and their dependents within DVA's time based performance targets, however a minority of claims take an excessively long period to process due to inefficient handling. These delays can have significant impacts for these veterans.

8. The audit identified weaknesses in DVA's business systems and processes, which do not adequately support the efficient delivery of services. In particular, DVA should improve the structure and consistency of workflow management for R&C claims, and review its highly segmented approach to processing claims under the various elements of applicable legislation. DVA's focus on monitoring the median and the average TTTP across the population of claims does not provide a sufficiently complete picture of performance, and does not address critical reputational and client welfare risks

9. For claims with a high time taken to process (TTTP), the audit identified that this stemmed from excessive time associated with 'inactivity' (delays in the actioning of a claim despite the presence of required information) and medical reviews. DVA should improve its oversight of the progress of individual claims through the processing lifecycle, and its management of medical service provision. The monitoring and reporting of claims is not effective in alerting management to those which are at risk of taking excessive time to process.

Supporting findings

Business systems and processes

10. Whilst a high level workflow methodology has been established for R&C claims, the Rehabilitation and Compensation Integrated Support Hub (ISH) system is not being used to support compliance and management of workflow, but rather as a repository of records associated with a claim at the completion of processes.

11. ISH workflow management has been replaced in practice by individual spreadsheets maintained in various formats.

12. DVA's approach to claims allocation and management means that claims can be 'lost' in the various hand-off points between areas, causing delays and inefficiencies.

13. R&C processes for VEA claims are designed as an end-to-end process. However, R&C processes for DRCA and MRCA claims are not designed to maximise efficiency. The approach to assessment for these claims is resulting in the unnecessary disaggregation and re-aggregation of components within some DRCA claims, information requests to third parties being lodged multiple times for the same claims and multiple areas of DVA being required to review the same voluminous case files.

14. In the ANAO sample, information requests from the Department of Defence and medical specialists took a large proportion of the elapsed TTTP for a claim. DVA's internal targets and external reporting for R&C claims are not well aligned to the current agreement with the Department of Defence.

15. DVA reporting indicates that the average TTTP fell between 3 per cent and 9 per cent across all R&C claim categories in the period 2015 to 2017. Reporting also indicates that the number of cases-on-hand / work-in progress has fallen by 17.9 per cent (2,266) across the same period, and the average age of cases by between 16 per cent and 45 per cent across the relevant claim categories.

16. DVA's focus on the use of the median and the mean TTTP in both operational and external reporting for the performance of the R&C business does not provide a sufficiently complete picture of performance. In addition, it does not necessarily address critical risks given that even a small number of very high TTTP claims can have significant impacts for veterans and DVA's reputation.

17. Testing identified inconsistencies in naming conventions for records in ISH and HP Content Manager, DVA's primary records management system. Locating all relevant documentation associated with a claim during the testing process was inefficient and time consuming.

18. It is apparent that the ISH system does not have controls to ensure integrity over the high volume of manual records placed in the system. This was particularly evident in relation to the dates associated with registration of claims and referral for medical consultations. Instances were also identified where key client documentation was being kept manually by staff for periods prior to lodgement in the ISH system.

Delivery of services

19. Testing indicated that the two main drivers of high TTTP claims were the need to wait for responses from medical specialists, and 'inactivity'.

20. Unlike the Single Access Mechanism (SAM) arrangements with the Department of Defence, there is no formal control or monitoring of requests for information from medical specialists. Time spent waiting for responses from medical specialists in the ANAO's testing was, on average, 10 times greater than for information requests to the Department of Defence.

21. There were two main reasons for 'inactivity': where claims were effectively 'lost' in the system; and where the delegate did not immediately take action after requested information was received and the claim was actionable. Both issues are indicative of a lack of transparency over workflow within the system.

22. DVA has an internal Quality Assurance function which conducts a statistically based review of all DVA activities. The error rate was above tolerable levels for 2016-17 in three of the six primary R&C claim categories.

23. An extensive suite of reports and analysis is prepared at various frequencies containing key metrics and analysis on R&C operations. This reporting has limited analysis about emerging risks or the reasons behind changes in performance. Management reporting does not identify progress on claims or the reasons for any delays, and is largely unutilised by team leaders.

24. The significant reorganisation of R&C operations following the creation of a national R&C business in 2015 has meant that internal benchmarking by location does not currently provide reliable comparisons. Comparisons between processing locations will become more reliable, as measures relative efficiency, when more comparable data becomes available.

25. Comparisons between DVA and Comcare show significant differences in approach to claims processing. However, there may be value to DVA in implementing comparisons based on trends or detailed processes.

Recommendations

Recommendation no.1
Paragraph 2.20 The ANAO recommends that DVA establish appropriate workflow management over R&C processes that will allow for identification of potentially problematic claims and delays in processing earlier in the claims investigation process.

Department of Veterans' Affairs response: *Agreed.*

Recommendation no.2
Paragraph 2.42 The ANAO recommends that DVA review the current approach to processing R&C claims to address efficiency issues including aggregation and disaggregation of DRCA claims, multiple instances of information requests to third parties and the number of staff involved in the processing of individual claims.

Department of Veterans' Affairs response: *Agreed.*

Recommendation no.3
Paragraph 2.65 The ANAO recommends that DVA implement claims processing targets that include consideration of the distribution of the TTTP as well as the average/median.

Department of Veterans' Affairs response: *Agreed.*

Recommendation no.4
Paragraph 2.76 The ANAO recommends that DVA addresses weaknesses in information and records management, in particular: retention of records outside of primary systems, inconsistent use of naming conventions, and ensuring the completeness and accuracy of client records.

Department of Veterans' Affairs response: *Agreed.*

Recommendation no.5
Paragraph 3.21 The ANAO recommends that DVA implement greater control and monitoring over its requirement for information from medical specialists. This should include contractual arrangements that prescribe timeliness and quality for independent medical specialists engaged directly by the DVA and prompt and frequent follow up where the client has elected to use their own treating medical specialist.

Department of Veterans' Affairs response: *Agreed.*

Recommendation no.6
Paragraph 3.39 The ANAO recommends that DVA develop and implement R&C reporting into its RACER system that:

- will allow the identification of claims that are potentially problematic at an individual claim level for operational management and at an aggregated level for oversight and governance; and
- provides transparent flow of consistent information at levels suitable for governance, module management and team and individual performance management.

Department of Veterans' Affairs response: *Agreed.*

Summary of entity response

26. The Department of Veterans' Affairs notes the results of the audit and thanks the Australian National Audit Office for the opportunity to respond to the issues raised. The Department notes and agrees with the six recommendations outlined in the audit report.

Key learnings for all Australian Government entities

27. Below is a summary of key learnings, including instances of good practice, which have been identified in this audit that may be relevant for the operations of other Commonwealth entities.

Governance and risk management

Entities should ensure that oversight and management reporting is focused on potential / emerging risks in addition to the monitoring of existing activities.

Entities should ensure that there is a clear line of sight from business operations to strategic management through the use of transparent and consistent management and performance information.

Contract management

Effective control of third parties is dependent on the existence of formal agreements. Entities should ensure that such agreements are established in instances where there is a reliance on

third party deliverables as an input to a decision making process. The agreements should be sufficiently specific to allow the identification and resolution of any issues associated with quality and timeliness.

The Single Access Mechanism (SAM) agreement established between DVA and the Department of Defence to channel and manage requests and responses for information is a useful example of such an agreement.

Records management

Entities should ensure that basic controls over the completeness and accuracy of client records are consistently implemented and that critical client records can be reliably located.

Cyber Resilience

No.53 2017-18

Department of the Treasury; National Archives of Australia; Geoscience Australia

Summary and recommendations

Background

1. Cyber security is a strategic priority for the Australian government.¹ A secure cyberspace provides trust and confidence for individuals, business and the public sector to share ideas, collaborate and innovate.² To strengthen trust online, effective implementation of a comprehensive cyber security strategy across government systems is critical to protect Australians' privacy and Australia's social, economic and national security interests from targeted cyber intrusions and emerging cyber threats. The Attorney-General's Department Protective Security Policy Framework outlines the core requirements for the effective use of protective information and communications technology (ICT) security.
2. In February 2017, the Australian Signals Directorate issued the updated Strategies to Mitigate Cyber Security Incidents as a priority list of practical actions entities can take to make their ICT environment more secure. It referred to these cyber security strategies as the Essential Eight and recommended that entities implement the strategies as a security baseline. In June 2017, the Australian Signals Directorate also released the Essential Eight Maturity Model, to assist entities to assess the level of implementation of the Essential Eight mitigation strategies. A revised Model was issued in October 2017.
3. Of the eight mitigation strategies, four are mandatory (the Top Four).³ Since 2013, entities have been required to undertake an annual self-assessment against the mandatory requirements of the Protective Security Policy Framework. Key elements to achieving compliance with the mandatory mitigation strategies are: sufficient investment; appropriate processes; and a culture that recognises the importance of and requirements for cyber resilience.
4. Three entities were included in the audit: Department of the Treasury (Treasury), National Archives of Australia (National Archives), and Geoscience Australia. These entities were selected based on the character and sensitivity of the information collected, stored and reported.

¹ Joint Committee of Public Accounts and Audit, Report 467: Cybersecurity Compliance, 2017, p. 13, available from http://parlinfo.aph.gov.au/parlInfo/download/committees/reportjnt/024076/toc_pdf/Report467CybersecurityCompliance.pdf;fileType=application%2Fpdf, [accessed 9 January 2018].

² Prime Minister and Cabinet, Australia's Cyber Security Strategy [Internet], 2016. Available at <https://cybersecuritystrategy.pmc.gov.au/>, [accessed 9 January 2018].

³ The Top Four strategies are application whitelisting, patching applications, patching operating systems, and minimising privileged user access. The non-mandatory strategies are disabling untrusted Microsoft Office macros, user application hardening, multi-factor authentication, and daily backup of systems and data.

5. Since 2013–14, the Australian National Audit Office (ANAO) has conducted three performance audits to assess the cyber resilience of 11 different government entities.⁴ These audits have identified high rates of non-compliance with the requirements of the Protective Security Policy Framework.

Audit rationale

6. The ANAO decided to conduct this fourth audit of entities' management of cyber risks recognising ongoing parliamentary interest (including enquiries by the Joint Committee of Public Accounts and Audit) and the level of non-compliance with mandatory requirements identified in previous audits. In Report 467: Cybersecurity Compliance, the Joint Committee of Public Accounts and Audit recommended that the ANAO outlines the behaviours and practices it would expect in a cyber resilient entity and assess against these.

Audit objective and criteria

7. The objective of the audit was to assess the effectiveness of the management of cyber risks by the Department of the Treasury, National Archives of Australia and Geoscience Australia.

8. The audit criteria were:

- do entities have effective arrangements in place for managing cyber risks;
- do entities monitor and report against cyber security deliverables; and
- were entities cyber resilient, with a culture of cyber resilience?

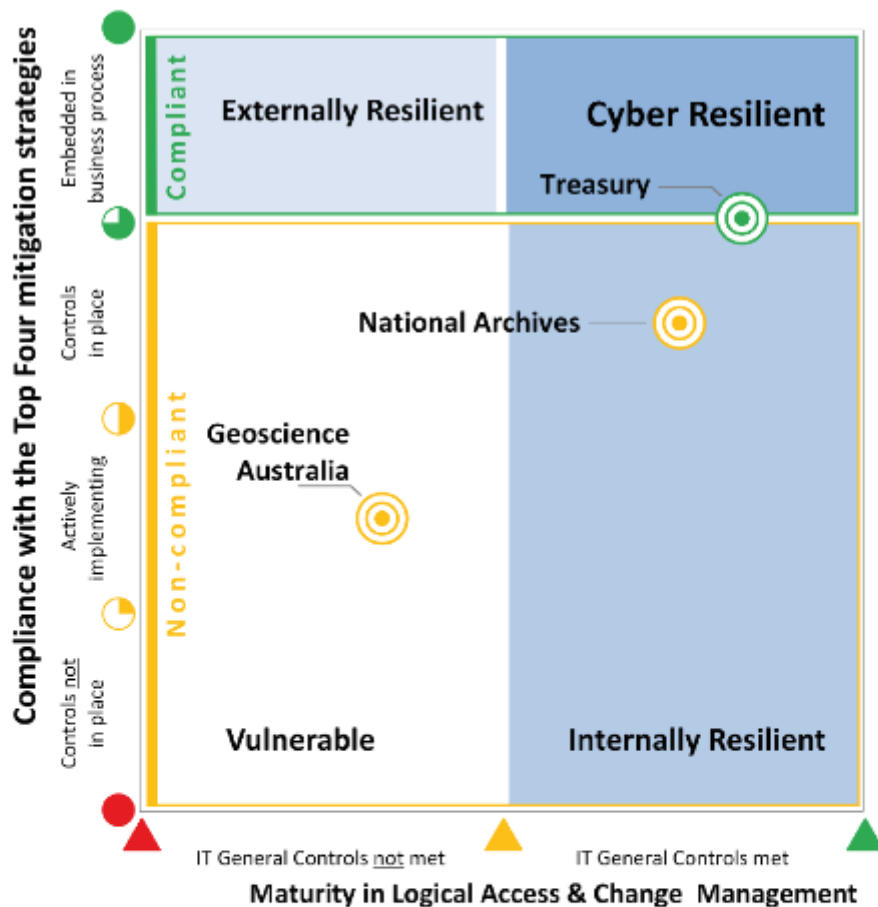
Conclusion

9. As with the ANAO's previous audits of cyber security, this audit identified relatively low levels of effectiveness of Commonwealth entities in managing cyber risks, with only one of the three audited entities compliant with the Top Four mitigation strategies. None of the three entities had implemented the four non-mandatory strategies in the Essential Eight and were largely at early stages of consideration and implementation. These findings provide further evidence that the implementation of the current framework is not achieving compliance with cyber security requirements, and needs to be strengthened.

10. Of the three entities, only Treasury was compliant with the Top Four mitigation strategies and cyber resilient. National Archives was not compliant with the Top Four mitigation strategies but had sound ICT general controls and so was assessed as not cyber resilient but internally resilient. Geoscience Australia was not compliant with the Top Four mitigation strategies and did not have sound ICT general controls so was assessed as vulnerable to cyber attacks. All three entities had implemented only one of the four non-mandatory mitigation strategies in the Essential Eight, and were not well progressed in considering an implementation position for the other three strategies. Figure S.1 shows each entity's cyber resilience.

⁴ ANAO Report No.50 2013–14, Cyber Attacks: Securing Agencies' ICT System; ANAO Report No.37 2015–16 Cyber Resilience; and ANAO Report No.42 2016–17 Cybersecurity Follow-up Audit.

Figure S.1. Entities' cyber resilience^a



KEY:

- Control *not* in place and *no* dispensation authorised by the Accountable Authority.
- Control *not* in place but a dispensation is authorised by the Accountable Authority.
- Control *not* in place but entity is actively implementing, with a minimum of design deliverables in evidence.
- Control in place and meeting control objectives.
- Control in place and maintenance is part of business processes, including monitoring and taking corrective action as required.
- ▲ Control objective *not* met.
- ▲ Identified control *not* in place but compensating controls in place and observed.
- ▲ Control objective is met.

Note a: An entity's position on the matrix indicates its overall cyber resilience—in essence how well the entity is protected from external intrusions, internal breaches and unauthorised disclosures of information, and how well it is positioned to address threats.

Source: ANAO analysis.

11. Two entities had accurately self-assessed and reported their level of compliance with the Top Four mitigation strategies, and the other entity had not. There are shortcomings in the Essential Eight Maturity Model that limits its usefulness in its current form, and could lead to entities inadvertently overstating their cyber security compliance if it is used in performing the self-assessment. With activities underway to revise security reporting under the Protective Security

Policy Framework, it is timely to also strengthen guidance supporting entities to self-assess compliance with the mandatory mitigation strategies and processes to verify the correctness of those assessments.

12. The three entities had partly effective arrangements for managing cyber security risks, with specialist staff in dedicated security positions contributing to existing ICT processes and broader business models. However, the entities did not adopt a risk-based approach to prioritise improvements to cyber security, with cyber security investments focused on short-term operational needs rather than long-term strategic objectives. Until the National Archives and Geoscience Australia achieve compliance with the mandatory strategies, it is inappropriate to consider that a positive cyber resilience culture is in place.

Supporting findings

Implementation of cyber risk mitigation strategies

13. Treasury complied with the requirements of the Top Four mitigation strategies, while National Archives and Geoscience Australia did not comply. National Archives met the requirements for two of the strategies, patching ICT applications and minimising privileged user access, but not for application whitelisting or patching operating systems. Geoscience Australia was not compliant with any of the four strategies.⁵

14. Of the three entities, only Treasury was cyber resilient, with a high level of protection from external intrusions and internal breaches. The department complied with the Top Four mitigation strategies and had sound ICT general controls in place for logical access and change management. The ANAO assessed National Archives as internally resilient but vulnerable to attacks from external sources. Geoscience Australia was assessed as vulnerable, with a high level of exposure and opportunity for external attacks and internal breaches and unauthorised disclosures of information.

15. The three entities had each implemented one of the four non-mandatory strategies in the Essential Eight—daily backup of important data. Treasury, National Archives and Geoscience Australia had made limited progress in implementing the other three non-mandatory strategies—disabling untrusted Microsoft Office macros, user application hardening and multi-factor authentication. In a few instances, the entities had considered risks and commenced developing plans to implement controls as part of the non-mandatory strategies, but were generally not well progressed in determining an implementation position for the strategies.

Self-assessment and maturity model

16. All three entities conducted self-assessments against the Top Four mitigation strategies and reported their compliance in accordance with government requirements. Treasury and Geoscience Australia accurately assessed their level of compliance. National Archives incorrectly reported compliance against two strategies. In conducting the self-assessments, the entities did not have access to comprehensive guidance or supporting tools, such as control assessment test plans or grading schemes, which would have assisted accurate self-assessments according to the requirements of the Protective Security Policy Framework.

⁵ Geoscience Australia had recently reassessed its cyber security arrangements and commenced an IT program of work to achieve compliance with the Top Four mitigation strategies, including deploying application whitelisting for critical ICT infrastructure, by late 2018.

17. In its current form, the Essential Eight Maturity Model is unlikely to achieve its objective of assisting entities to determine their maturity in implementing the Essential Eight mitigation strategies. This is primarily because there is inconsistent and incomplete alignment between the definitions of the mitigation strategies in the Australian Government Information Security Manual and the criteria for attaining a particular maturity level in the Essential Eight Maturity Model document.

18. A revised Protective Security Policy Framework and updated reporting requirements is scheduled for 2018–19. In light of the continued low level of compliance with the Top Four mitigation strategies, the revised framework should incorporate adequate technical guidance to support entities to accurately self-assess against those strategies, additional verification of compliance with those requirements and enhanced transparency about entities' compliance.

Management arrangements and cyber resilience culture

19. The three entities had partly effective arrangements for managing cyber security risks, with scope for improvement in important elements of risk management and governance. Two of the three entities had established a business model and ICT governance that incorporated ICT security into strategy, planning and delivery of services, and all entities had key ICT operational staff with a sound understanding of the vulnerabilities and cyber threats that may affect their ICT systems. The three entities had not adopted a systematic risk-based approach to prioritise improvements to cyber security across their ICT systems, or identified and documented cyber initiatives beyond 2017–18, and key ICT security management roles had not been consistently filled.

20. The three entities were at different stages in embedding a cyber resilience culture. Treasury was aware of the importance of its sensitive data holdings and had ongoing activities to strengthen its cyber security approaches. National Archives had a number of longstanding practices and could have learnt more from looking outwardly to the cyber resilience practices of other entities. Geoscience Australia has traditionally had a culture of scientific independence that it had allowed to override cyber resilience considerations. All entities are aiming to better understand the shared attitudes, values and behaviours to make the most of ICT opportunities while effectively managing cyber risks.

Recommendations

Recommendation no.1

Paragraph 2.15

Geoscience Australia and National Archives of Australia each establish a plan and timeframe to achieve compliance with the Top Four mitigation strategies, and monitor delivery against that plan.

Geoscience Australia response: Agreed.

National Archives of Australia response: Agreed.

Recommendation no.2

Paragraph 3.39

In revising security reporting and cyber-related requirements under the Protective Security Policy Framework, the Attorney-General's Department, Department of Home Affairs and Australian Signals Directorate work together to improve compliance with the framework by:

- providing adequate technical guidance to support entities to accurately self-assess compliance with the Top Four mitigation strategies and their underlying controls contained in the Information Security Manual;
- developing a program for verifying entities' reported compliance with the mandatory cyber security requirements; and
- increasing transparency and accountability about entities' compliance with those requirements.

Attorney-General's Department response: Agreed to part (a) and part (c); Agreed in principle to part (b).

Department of Home Affairs response: Agreed.

Australian Signals Directorate response: Agreed.

Summary of entity responses

21. Entities' responses to the proposed report are provided at Appendix 1 and entities that provided summaries of their responses have been included below.

Department of the Treasury

The Treasury agrees with the findings and the recommendation within the performance audit of Cyber Resilience, dated 16th May 2018. The Information Security Manual will continue to be used to inform future cyber security strategies and policies for the department.

The Treasury acknowledges the importance of diligence and attentiveness to cyber security for all Treasury staff. The Treasury will continue to develop and implement robust cyber security strategies and policies to strengthen the security of ICT systems to mitigate the risk of cyber intrusion.

National Archives of Australia

The National Archives will develop a cyber resilience framework and a supporting plan to effectively implement the Essential Eight. It is intended the framework will underpin a secure, stable and contemporary ICT environment that supports the business of the National Archives. The activities to achieve the cyber maturity model for the National Archives will be prioritised by the National Archives Enterprise Board taking into consideration resourcing and whole-of-government posture for cyber resilience.

Geoscience Australia

Geoscience Australia welcomes this report and agrees with the two recommendations. We agree that the report is an accurate assessment of our compliance at the time of the audit.

Geoscience Australia is committed to improving its security compliance and cyber resilience to a level appropriate for a government organisation that plays a role in providing scientific information and services to industry and the broader community.

We have already commenced actions to improve compliance to address the security issues identified including: the engagement of a senior consultant to advise on an overarching security framework; the establishment of a Security Working Group; and an action plan to address compliance with the Australian Signals Directorate's Strategies to mitigate cyber security incidents.

Key learnings for improvement for all Australian Government entities

Below is a summary of behaviours and practices identified in this and previous audit reports that, if implemented, may improve the level of cyber resilience of Commonwealth entities. A more comprehensive list is at Table 4.3 of this report. These learnings include expected, appropriate behaviours and practices of a cyber-resilient entity that the ANAO has observed from audits of cyber security that entities can apply to embed a culture of cyber resilience.⁶

Governance and risk management

- Self-assess the Top Four cyber security risk mitigation strategies of the Protective Security Policy Framework using a controls-based approach. If the self-assessment is non-compliance, make the necessary investments and changes to become compliant.
- Make decisions about how and when to implement the four non-mandatory strategies in the Essential Eight mitigation strategies promulgated by the Australian Signals Directorate.
- Establish a business model and ICT governance that incorporates ICT security into strategy, planning and delivery of services.
- Ensure management understand their roles and responsibilities to enhance security initiatives for the services for which they are accountable. This includes senior management understanding the need to oversight and challenge strategies and activities aimed at ensuring the entity complies with mandatory security requirements.
- Manage cyber risks systematically, including through assessments of the effectiveness of controls, security awareness training, and adopting a risk-based approach to prioritise improvements to cyber security.
- Assign information security roles to relevant staff and communicate the responsibilities.

⁶ The ANAO will continue to refine this list of behaviours and practices in response to Recommendation 6 in the Joint Committee of Public Accounts and Audit's *Report 467: Cybersecurity Compliance*.

**The Implementation and Performance of the Cashless Debit Card Trial
No.1 2018–19
Department of Social Services**

Summary and recommendations

Background

1. Welfare quarantining, in the form of income management, was first introduced in 2007 as part of the Commonwealth Government's National Northern Territory Emergency Response.¹ The aim of income management is to assist income support recipients to manage their fortnightly payments — such as Newstart/Youth allowance, parenting or carer payments, and the Disability Support Pension — for essentials like food, rent and bills.²
2. On 1 December 2014, the Government agreed to trial a new approach to income management — the Cashless Debit Card (CDC), in Ceduna and the East Kimberley. The Cashless Debit Card Trial (CDCT or the trial) aimed to: test whether social harm caused by alcohol, gambling and drug misuse can be reduced by placing a portion (up to 80 per cent) of a participant's income support payment onto a card that cannot be used to buy alcohol or gambling products or to withdraw cash; and inform the development of a lower cost welfare quarantining solution to replace current income management arrangements.
3. On 14 March 2017, the Minister for Human Services and the Minister for Social Services announced the extension of the trial in Ceduna and the East Kimberley for a further 12 months. In addition, funding was allocated as part of the 2017–18 Budget to trial the CDC in two new locations with the Government announcing in September 2017 that the CDC would be delivered to the Goldfields region of Western Australia and also to the Hinkler Electorate (Bundaberg and Hervey Bay Region) in Queensland.³ Subsequently, the *Social Services Legislation Amendment (Cashless Debit Card) Act 2018* received royal assent on 20 February 2018. The amendments restricted the expansion of the CDC, with the cashless welfare arrangements continuing to 30 June 2019 in the current trial areas of East Kimberley and Ceduna, with one new trial site in the Goldfields.

Rationale for undertaking the audit

4. Recent ANAO audits have highlighted the need for entities to articulate mechanisms to determine whether an innovation is successful and what can be learned to inform decision making

¹ The *Northern Territory National Emergency Response Act 2007* was passed and given royal assent in August 2007. The Act outlined measures to address child abuse and other issues in Indigenous communities in the Northern Territory.

² Department of Human Services, *How Income Management Works* [Internet], DHS, February 2018, available from <https://www.humanservices.gov.au/individuals/enablers/how-income-management-works> [accessed March 2018].

³ The Minister for Human Services announced the roll-out of the CDC to the Western Australian Goldfields region on 1 September 2017 and to the Hinkler Electorate on 21 September 2017.

regarding scaling up the implementation of that innovation. The CDCT was selected for audit to identify whether the Department of Social Services (Social Services) was well placed to inform any further roll-out of the CDC with a robust evidence base. Further, the audit aimed to provide assurance that Social Services had established a solid foundation to implement the trial including: consultation and communication with the communities involved; governance arrangements; the management of risks; and robust procurement arrangements.

Audit objective and criteria

5. The objective of the audit was to assess the Department of Social Services' implementation and evaluation of the Cashless Debit Card Trial.

6. To form a conclusion against the audit objective, the ANAO adopted the following high level audit criteria:

- Appropriate arrangements were established to support the implementation of the Cashless Debit Card Trial.
- The performance of the Cashless Debit Card Trial was adequately monitored, evaluated and reported on, including to the Minister for Social Services.

Audit methodology

7. The audit methodology included:

- examining and analysing documentation relating to the implementation, risk management, monitoring and evaluation for the Cashless Debit Card Trial; and
- interviews with key officials in the departments of Social Services and Prime Minister and Cabinet and with external stakeholders including Indue Limited (Indue), ORIMA Research (ORIMA), Community Leaders, Local Partners and others in the trial sites.

Conclusion

8. The Department of Social Services largely established appropriate arrangements to implement the Cashless Debit Card Trial, however, its approach to monitoring and evaluation was inadequate. As a consequence, it is difficult to conclude whether there had been a reduction in social harm and whether the card was a lower cost welfare quarantining approach.

9. Social Services established appropriate arrangements for consultation, communicating with communities and for governance of the implementation of CDCT. Social Services was responsive to operational issues as they arose during the trial. However, it did not actively monitor risks identified in risk plans and there were deficiencies in elements of the procurement processes.

10. Arrangements to monitor and evaluate the trial were in place although key activities were not undertaken or fully effective, and the level of unrestricted cash available in the community was not effectively monitored. Social Services established relevant and mostly reliable key performance indicators, but they did not cover some operational aspects of the trial such as efficiency, including cost. There was a lack of robustness in data collection and the department's evaluation did not make use of all available administrative data to measure the impact of the trial including any change in social harm. Aspects of the proposed wider roll-out of the CDC were informed by learnings from the trial, but the trial was not designed to test the scalability of the CDC and there was no plan in place to undertake further evaluation.

Supporting findings

Implementation of the Cashless Debit Card Trial

11. Social Services conducted an extensive consultation process with industry and stakeholders in the trial sites. A communication strategy was developed and implemented which was largely effective, although Social Services identified areas for improvement in future rollouts.
12. There were appropriate governance arrangements in place with clearly defined roles and responsibilities across key departments and stakeholders for reporting and oversight of the CDCT.
13. Social Services demonstrated an integrated approach to risk management across the department linking enterprise, program and site-specific risk plans. While a CDCT program risk register was developed, the identified risks were not actively managed, some risks were not rated in accordance with the Risk Management Framework, there was inadequate reporting of risks and some key risks were not adequately addressed by the controls or treatments identified. In particular, treatments were inadequate to address evaluation data and methodology risks that were ultimately realised. Social Services managed and effectively addressed operational issues as they arose.
14. Aspects of the procurement process to engage the card provider and evaluator were not robust. The department did not document a value for money assessment for the card provider's IT build tender or assess all evaluators' tenders completely and consistently.
15. Social Services effectively established or facilitated arrangements to deliver local support to CDCT communities, although there were delays in the deployment of additional support services. As part of the CDCT, Social Services also trialled Community Panels and reviewed their effectiveness to inform broader implementation.

Performance monitoring, evaluation and reporting

16. A strategy to monitor and analyse the CDCT was developed and approved by the Minister. However, Social Services did not complete all the activities identified in the strategy (including the cost-benefit analysis) and did not undertake a post-implementation review of the CDCT despite its own guidance and its advice to the Minister that it would do a review. There was scope for Social Services to more closely monitor vulnerable participants who may participate in social harm and their access to cash.
17. Key performance indicators (KPIs) developed to measure the performance of the trial were relevant, mostly reliable but not complete because they focused on evaluating only the effectiveness of the trial based on its outcomes and did not include the operational and efficiency aspects of the trial. There was no review of the KPIs during the trial and KPIs have not been established for the extension of the CDC.
18. Social Services developed high level guidance to support its approach to evaluation, but the guidance was not fully operationalised. Social Services did not build evaluation into the CDCT design, nor did they collaborate and coordinate data collection to ensure an adequate baseline to measure the impact of the trial, including any change in social harm.
19. Social Services regularly reported on aspects of the performance of the CDCT to the Minister but the evidence base supporting some of its advice was lacking. Social Services advised the Minister, after the conclusion of the 12 month trial, that ORIMA's costs were greater than originally contracted and ORIMA did not use all relevant data to measure the impact of the trial, despite this being part of the agreed Evaluation Framework.
20. Social Services undertook a review and reported to the Minister on a number of key lessons learned from the 12 month trial of the CDC. Learnings about the effectiveness of the Community Panels were based on the number of applications received and delays in decision making, rather than

from the evaluation findings that noted a delay in the establishment of the Community Panels and a lack of communication with participants. The 12 month trial did not test the scalability of the CDC but tested a limited number of policy parameters identified in the development of the CDC. Many of the findings from the trial were specific to the cohort (predominantly indigenous) and remote location, and there was no plan in place to continue to evaluate the CDC to test its roll-out in other settings.

Recommendations

Recommendation no.1

Paragraph 2.20

Social Services should confirm risks are rated according to its Risk Management Framework and ensure mitigation strategies and treatments are appropriate and regularly reviewed.

Department of Social Services' response: *Agreed.*

Recommendation no.2

Paragraph 2.31

Social Services should employ appropriate contract management practices to ensure service level agreements and contract requirements are reviewed on a timely basis.

Department of Social Services' response: *Agreed.*

Recommendation no.3

Paragraph 2.36

Social Services should ensure a consistent and transparent approach when assessing tenders and fully document its decisions.

Department of Social Services' response: *Agreed.*

Recommendation no.4

Paragraph 3.14

Social Services should undertake a cost-benefit analysis and a post-implementation review of the trial to inform the extension and further roll-out of the CDC.

Department of Social Services' response: *Agreed.*

Recommendation no.5

Paragraph 3.47

Social Services should fully utilise all available data to measure performance, review its arrangements for monitoring, evaluation and collaboration between its evaluation and line areas, and build evaluation capability within the department to facilitate the effective review of evaluation methodology and the development of performance indicators.

Department of Social Services' response: *Agreed.*

Recommendation no.6

Paragraph 3.69

Social Services should continue to monitor and evaluate the extension of the Cashless Debit Card in Ceduna, East Kimberley and any future locations to inform design and implementation.

Department of Social Services' response: *Agreed.*

Summary of the Department of Social Services' response

21. The Department of Social Services was provided with a copy of the proposed audit report for comment. A summary of the department's response is below.

The Department of Social Services (the department) welcomes the ANAO's conclusions and agrees with the six recommendations. The department notes there are a number of areas it needs to focus on including in relation to Risk Management, contract management arrangements and utilising available data to measure performance.

22. An extract of the proposed report was provided to the organisations mentioned in the proposed report: Indue Limited; ORIMA Research; Boston Consulting Group; Maddocks; Clayton Utz; Deloitte Access Economics; and Colmar Brunton.

Key learnings for all Australian Government entities

23. Below is a summary of key learnings and areas for improvement identified in this audit report that may be considered by other Commonwealth entities when trialling new initiatives and designing, implementing and evaluating programs.

Performance and impact measurement

- When designing and implementing a trial of a policy, program, technology or service delivery approach, there should be clear objectives identifying success factors and mechanisms to capture lessons learned to inform further implementation. In particular,
 - Designing and implementing a trial is different to the design and full-scale implementation of policy. A trial will require greater focus and resources directed to its design and performance measurement so that early decisions can be made regarding the need to adapt, exit or expand implementation.
 - It is important to place a greater emphasis on the capture of baseline data, documenting expected outcomes, capturing lessons learned, impact measurement and enabling feedback mechanisms at regular intervals.
- Success of a trial should be measured based more on what is learned to inform the next phase of re-design or implementation, and less on whether the actual implementation worked according to expectations.

**Administration of the Data Retention Industry Grants Program
No.2 2018 – 19
Attorney General's Department**

Background

1. Telecommunications data is important to law enforcement and national security investigations. The *Telecommunications (Interception and Access) Amendment (Data Retention) Act 2015* (the Act) introduced a mandatory data retention scheme applying to telecommunications service providers. The Act was introduced to address:

- a long-term decline, and inconsistency, in industry retention of data;
- a long-term increase in the importance of access to data; and
- an increasingly high-risk operational environment.

2. The nature of the data required to be retained¹ differs depending on the type of telecommunications services offered. Service providers are required to secure the retained data by encrypting it and protecting it from unauthorised interference or access.

3. The data retention obligations came into effect on 13 October 2015. Providers that were fully compliant by that date were able to submit a Statement of Work outlining the steps they had taken to become compliant. Otherwise, an 18 month implementation period enabled service providers to apply for approval of a Data Retention Implementation Plan, or obtain an exemption from, or variation to, the data retention obligations.

4. In October 2014, when deciding to legislate for a mandatory data retention regime, the government decided to pay a 'reasonable portion' of industry's implementation costs.² After receiving further advice from departments, in April 2015 the government decided to establish a demand-driven grants program that would fund 50 per cent of the mid-point of an estimate of industry's capital cost of implementing a mandatory data retention regime. The program had a budget of \$131.3 million.³

5. The program was intended to make a one-off contribution towards existing service providers' costs in adjusting to meet the new obligations, supporting the industry to adjust to a new regulatory baseline. New entrants to the market were expected to be compliant and, as such, ongoing funding was not considered necessary.

6. Program guidelines were issued on 8 December 2015. Applications were able to be lodged between 7 January 2016 and 23 February 2016. A total of 210 applications were received. Of those, 15 applications were later withdrawn and 15 were assessed as ineligible.⁴

1 The data retention obligations relate to information about a communication, not the content or substance of a communication.

2 Operational costs for telecommunications service providers responding to requests for data are to continue to be met on a no-profit no-loss basis by requesting agencies.

3 Comprising \$128.4 million in grant funding and \$2.9 million for program administration costs.

4 Seven were assessed as ineligible because they did not submit an implementation plan or submitted it late, another two did not have an agreed plan and a further six applicants were assessed to not meet other eligibility criteria, including not having an eligible service.

7. In August 2016, 180 grants totalling \$128.4 million were awarded by the Attorney-General. Grant agreements were subsequently signed with 175 of the 180 successful applicants, involving a total grant value of \$127.9 million. As at the beginning of June 2018:

- a. the amount of grant funding had been reduced in aggregate by \$4.4 million for 19 providers⁵ (resulting in a revised total program value of \$123.5 million);
- b. \$122.7 million in grant payments had been made, of which \$736,149 was later recovered from two providers (as their reported costs were less than the first instalment payment they had received) with a further \$467,000 yet to be recovered (from two providers that have gone into liquidation – see footnote 5);
- c. grant reporting had been finalised and final payments made to 170 providers. One payment of \$22,089 remains to be made.

8. The implementation period ended on 13 April 2017. From that date all service providers must be fully compliant with their data retention obligations (except to the extent that they have an approved exemption from, or variation to, those obligations).

9. The Attorney-General's Department (AGD)⁶ was responsible for the design and implementation of the Data Retention Industry Grants Program (DRIGP). AGD was assisted by:

- a Data Retention Implementation Working Group established in 2014 to support engagement between the telecommunications industry and the Government on the implementation of data retention obligations;
- the Business Grants Hub within the Department of Industry, Innovation and Science (DIIS) whose responsibilities included promotion of the program, provision of contact services to handle inquiries from telecommunications providers, application receipt and assessment, funding agreement negotiation and management, grant payments and compliance activities; and
- PricewaterhouseCoopers (PwC), with whom AGD entered into various consulting contracts.

10. In May 2018 responsibility for the DRIGP was transferred from AGD to the Department of Home Affairs (DHA). DIIS retained responsibility for administering the grant funding agreements (at the time of the transfer, this consisted of two remaining grant payments). The findings, conclusions and recommendations made in this performance audit report are directed at AGD as: the program was designed and implemented under the grants administration framework of that department; and AGD was responsible for the approval of \$122.4 million in grant payments under the program.

Rationale for undertaking the audit

11. The program was selected for audit to examine subsidies for industry to comply with new statutory obligations as well as due to Parliamentary interest. Specifically:

- the Joint Committee of Public Accounts and Audit has indicated an interest in ongoing scrutiny of Attorney-General's Department's (AGD) grants administration practices following earlier Australian National Audit Office (ANAO) audits of two grant programs administered by AGD (Safer Streets, Report 41 of 2014 – 15, and Living Safe Together, Report 12 of 2016 – 17); and

5 This was due to providers reporting actual implementation costs being less than the grant amount (16 providers), two providers being investigated for defrauding the Commonwealth in respect to the funds they had already been paid and a reduction in the grant amount due to a change in one provider's business that substantially reduced its data retention obligations.

6 The Administrative Arrangements Order of December 2017 moved responsibility for national security and law enforcement policy and operations from AGD to the Department of Home Affairs.

- the Parliamentary Joint Committee on Intelligence and Security's February 2015 advisory report on the Bill to implement mandatory data retention included a recommendation on the design of the model for awarding grant funding to service providers.

Audit objective and criteria

12. The objective of the audit was to assess the effectiveness of the Attorney-General's Department's design of the Data Retention Implementation Grants Program, including its performance monitoring, reporting, evaluation and assurance arrangements.

13. To form a conclusion against the audit objective, the Australian National Audit Office (ANAO) adopted the following high level criteria:

- Was an appropriate design process established to support the achievement of the Government's objectives?
- Were sound performance monitoring, reporting, evaluation and assurance arrangements established?

Conclusion

14. The design of the Data Retention Industry Grants Program by the Attorney-General's Department was not fully effective. While funding was provided to each eligible provider that applied, in aggregate the department has funded 79 per cent of provider costs, substantially above the 50 per cent level identified as reasonable when the decision was taken to establish the program, with some providers having all their costs paid for by the government.⁷

15. A single round grants program was established to give effect to the decision that the Australian Government pay a reasonable portion of the telecommunications industry's costs of implementing the legislated mandatory data retention scheme. The design of the program exposed the Australian Government to the risk that it would make a more generous contribution than the 50 per cent of total industry costs the government had considered reasonable. This risk was realised:

- the amount of funding awarded represented 65 per cent of the aggregate of providers' cost estimates included in their applications for grant funding (involving increased grant funding of \$28 million compared with funding 50 per cent of estimated industry costs); and
- the proportion of costs being met by the Australian Government increased to 79 per cent compared with that expected when funding was awarded as a result of actual costs reported by providers being, in aggregate, \$39.9 million less than had been estimated by providers when they applied for funding. This included 26 providers where the Australian Government fully funded the data retention implementation costs reported by those providers (involving \$23.0 million in funding) notwithstanding that the program guidelines had stated that the Australian Government would not fully fund any provider. On average, the Australian Government contributed 82 per cent towards each provider's reported actual costs.

16. Implementation of the program was not to an appropriate standard having regard to the risks involved and the policy outcomes being sought. In particular:

- conflicts of interest were not well managed;
- there were significant errors and delays in the development and signing of grant agreements; and

⁷ The program guidelines approved by the Attorney-General stated that the Australian Government would not fully fund any provider.

- the grant reporting arrangements, and their administration, provide a low level of assurance.

Supporting findings

Program design

17. Options considered for providing funding to industry were a grants program, licence fee reductions, concessional loans or taxation changes.

18. The Attorney-General's Department contracted a consultant to estimate the capital costs to industry of implementing mandatory data retention. A February 2015 estimate (of between \$188.8 million and \$319.1 million, with a mid-point of \$254 million) informed a decision that the Australian Government would implement a grant program to support 50 per cent of the mid-point estimate. Better data was obtained from industry in early 2016 through the grant application process. Implementation estimates provided by eligible providers totalled \$198.5 million, or \$55.4 million lower than the mid-point of the earlier estimate. The Attorney-General's Department decided that the consultant should not reflect this data in its final report and the amount of grant funding made available was also not revised. The data from eligible providers that applied for funding would have supported a reduction of \$28 million (22 per cent) in program funding whilst still meeting 50 per cent of estimated industry costs (as earlier agreed by the government).

19. Clear and comprehensive program guidelines were developed and issued.

20. In a number of respects, the departmental advice on the program funding model was well considered. The advice addressed the risks associated with basing grant amounts on provider cost estimates, and proposed that these risks be managed by obtaining data from applicants that would allow 'typical' implementation costs to be estimated as a key input to determining individual grant amounts. A key risk that was not adequately addressed related to the potential for government estimates of typical implementation costs for individual providers to be greater than the provider's own estimate of those costs.

21. The program funding model was not used to determine each individual grant. Application of the funding model would have seen many telecommunications service providers receiving grant amounts well in excess of their estimated costs. Minimum (\$10,000) and maximum (80 per cent of the provider's cost estimate) grant parameters were established to prevent this result. An iterative process was then employed to re-allocate \$88.4 million in grant funding to other eligible applicants.

22. Eligible telecommunications services providers were awarded \$128.4 million in grant funding. This represented 65 per cent of the aggregate of those providers' cost estimates included in their applications for grant funding. There was no documented consideration, or departmental advice to the Attorney-General, about the merits of constraining the amount of grant funding awarded to 50 per cent of estimated costs (on an industry-wide basis). Limiting grant expenditure to 50 per cent of the aggregated estimated costs of industry applicants would have saved \$28 million in Australian Government expenditure.

23. As at the beginning of June 2018, reporting from providers awarded grant funding is that the cost to industry of implementing mandatory data retention was \$154.7 million. The Australian Government paid grants of \$122.7 million to those providers, meaning the Australian Government has met 79 per cent of industry's reported upfront capital costs of achieving compliance with the data retention obligations.

Program implementation

24. There was no probity plan in place for the program. An assurance plan was prepared, but it was not implemented in full. In addition, the risks associated with conflicts of interest were not well

managed, particularly in relation to the consulting firm contracted to assist with the design of the program and with the assessment of applications for funding.

25. The program risk assessment concluded that the program represented a medium risk and a low risk grant agreement was used, this was not inconsistent with guidance. At an individual provider level, one-sixth of providers were identified as presenting a higher risk, to be managed through additional reporting.

26. There were considerable delays in the execution of funding agreements, resulting mainly from the re-issuing of incorrect funding agreements. It took 10 months for all funding agreements to be executed, and all first instalment grant payments to be made. Some funding recipients received first instalment grant payments after data retention obligations came into effect on 13 April 2017, while other providers entered into funding agreements after this date. Delays were incurred due to the need to rectify the issuing of incorrect funding agreements.

27. The reporting arrangements, and their administration by the Department of Industry, Innovation and Science, relied heavily on statements made by funding recipients, and therefore provide a low level of assurance.

28. There is insufficient evidence yet available to demonstrate that the providers awarded grant funding are meeting their data retention obligations such that law enforcement agencies are now able to obtain the data they need. An effectiveness review is to be conducted in 2019.

Recommendations

Recommendation no.1 Where the Australian Government decides to make a contribution to project costs (rather than fully fund costs) AGD design and administer grant programs in a way that reflects and preserves the intended cost sharing arrangements.

Paragraph 2.41

Attorney-General's Department response: *Agreed.*

Department of Industry, Innovation and Science response: *Agreed.*

Recommendation no.2 AGD design grant programs for probity, including putting in place appropriate mechanisms for identifying and actively managing conflicts of interest.

Paragraph 3.20

Attorney-General's Department response: *Agreed.*

Department of Industry, Innovation and Science response: *Agreed.*

Recommendation no.3 When employing a grants hub to contract with entities to deliver grant programs on its behalf, AGD agree with the department providing the hub service performance indicators relating to the accuracy and timeliness with which grant agreements will be drafted, negotiated and finalised.

Paragraph 3.33

Attorney-General's Department response: *Agreed.*

Department of Industry, Innovation and Science response: *Agreed.*

Recommendation no.4 AGD determine the nature, content and frequency of reporting requirements for grant programs proportional to the risks involved and policy outcomes being sought.

Paragraph 3.47

Attorney-General's Department response: *Agreed.*

Department of Industry, Innovation and Science response: *Agreed.*

Summary of entity responses

29. A copy of the proposed audit report was provided for comment to AGD, DIIS and DHA. Comments on the proposed report were provided by the three departments. Summary responses were also provided by AGD and DIIS, as follows.

Attorney-General's Department

The Attorney-General's Department welcomes the ANAO's audit report into the Data Retention Industry Grants Program. The department accepts the four recommendations relating to program design and delivery, and the management of conflicts of interest. The department is committed to best practice in grants administration, and to continuous improvement in our delivery of such programs. We have commenced implementation of the recommendations and will continue improvements for any future grants programs.

Department of Industry, Innovation and Science

The Department of Industry, Innovation and Science (the department) acknowledges the ANAO's report on the *Administration of the Data Retention Industry Grants Program*. The department notes that the program presented a number of challenges given that key design decisions had already been reflected in legislation prior to this department's involvement. This placed a number of constraints on our delivery of the program, required complex administrative processes to be put in place to support its delivery, and reduced opportunities for streamlining and adoption of standard business processes that exist through the Business Grants Hub.

30. An extract of the proposed report was provided to PwC.

Key learnings for all Australian Government entities

31. Below is a summary of key learnings, including instances of good practice, which have been identified in this audit that may be relevant for the operations of other Commonwealth entities.

Program design

- Grant funding is provided to achieve desired outcomes. It is important that advice to decision-makers identify any opportunities to achieve the desired outcomes for less funding than has been budgeted, including in circumstances where the budgeted amount was based on early estimates that are later able to be refined.
- When engaging consultants to assist with key design and/or implementation aspects of a program, put in place mechanisms to identify and actively manage probity, including conflicts of interest.

**Award of Funding under the Community Development Grants Program
No.3 2018–19
Department of Infrastructure, Regional Development and Cities**

Background

1. The Community Development Grants Program (CDGP/the program) originated from commitments made by the then Opposition in the lead-up to the 2013 Federal election. Its coverage has been extended over time so that it now includes commitments from the 2016 election as well as uncontracted projects from programs that were abolished following the 2013 election and other commitments.
2. The CDGP provides funding to construct and upgrade facilities to provide long term improvements in social and economic viability of local communities. Total funding for the CDGP is currently \$936.8 million, with a program end date of 30 June 2020. Funding has been approved for 680 projects with a total value of \$785.9 million.
3. The CDGP is administered by the Department of Infrastructure, Regional Development and Cities (DIRDC/the department).

Rationale for undertaking the audit

4. During an election campaign candidates may undertake to provide certain funding, services or facilities if their party is elected or re-elected to government. Election commitments are often implemented through a grant. All grants are required to be awarded through processes that comply with the Commonwealth Grants Rules and Guidelines (CGRGs). The CDGP was selected for audit due to Parliamentary interest in the award of program funding, including compliance with the CGRGs and the proposed benefits from projects that have been awarded funding.

Audit objective and criteria

5. The objective of the audit was to examine the design and conduct of the award of funding under the CDGP.
6. To form a conclusion against this audit objective, the ANAO adopted the following high level criteria:
 - Is the design of the CDGP consistent with the Commonwealth Grants Rules and Guidelines?
 - Have the processes implemented to award CDGP funding complied with the Commonwealth Grants Rules and Guidelines?

Conclusion

7. The department effectively designed and conducted the award of funding under the CDGP other than its assessment of, and briefing on, proposed project outcomes.
8. The design of the program was consistent with the Commonwealth Grants Rules and Guidelines. Establishing a non-competitive grants program with relevant and appropriate eligibility requirements and appraisal criteria was a sound approach. It balanced the expectations of governments seeking to deliver upon their election commitments with the requirements of the grants administration framework. The design of the program also placed the department in a position to provide well-informed advice to the relevant Minister on whether funding should be awarded to candidate projects.

9. In most respects, the processes implemented to award funding complied with the Commonwealth Grants Rules and Guidelines. There were two shortcomings:

- the department's approach to one of the three appraisal criteria (that relating to outcomes/project benefits) was inadequate as it repeated claims by the project proponent as to what would be achieved, rather than providing the Minister with an assessment by the department as to how well the project aligned with the program outcome, and whether the achievement of the claimed project benefits could be measured; and
- briefings provided to Ministers recommending that funding be approved for candidate projects did not inform the decision-maker whether the three appraisal criteria for the program had been met in full, in part or not at all.

Supporting findings

Program design

10. Two ways of providing funding for the identified projects were considered. This was a non-competitive grants program (as had been used successfully following earlier elections to deliver project-specific regional commitments) and National Partnership Agreements with state governments.

11. Clear and comprehensive program guidelines were developed and issued in accordance with the requirements of the grants administration framework.

12. The program guidelines clearly outlined the program governance arrangements and the planned selection and decision-making processes.

13. Relevant and appropriate program eligibility requirements and three appraisal criteria were established and effectively communicated to project proponents through the program guidelines.

14. The department designed and implemented a process to gather relevant and appropriate information from project proponents to inform the assessment of projects and the provision of funding recommendations to decision-makers.

Award of funding

15. Consistent with the design of the program, only projects identified by the Australian Government were considered for funding. These projects have principally been various commitments made in the context of the 2013 and 2016 Federal elections.

16. Eligibility checking focused on whether the project proponent was a legal entity and the consistency of the project with the intent of the original funding announcement. This work led to some election commitment projects initially allocated to the program being transferred out of the program.

17. The appraisal criteria relating to project viability and sustainability and proponent viability were demonstrably applied by the department to inform its assessment of the value for money of each candidate project. The department's approach to the outcomes/project benefits criterion was inadequate. Specifically, the material provided by the department to the relevant Minister in support of its recommendations that funding be approved outlined the project proponent's view of the outcomes it claims would be achieved from the project rather than recording a departmental assessment of the proponents' claims.

18. The department provided written advice to the Minister for all projects where an assessment was completed. The briefing addressed a range of relevant considerations, including most of the requirements of the Commonwealth Grants Rules and Guidelines. A key omission in the advice provided to Ministers was that the department did not state whether the three appraisal criteria for the CDGP were fully met, partially met or not met at all.

19. Clear funding recommendations were provided by the department. There were no instances where the department recommended that funding not be awarded. The briefing packages for recommended projects included a summary of the department's assessment and a recommendation that grant funding be approved.

20. The reasons for the award of funding were recorded in briefing packages that the department prepared for each grant that was recommended to, and approved by, a Minister. There were no instances where a Minister declined to award funding to a project recommended by the department, or where funding was awarded to a project the department had not recommended for funding. The funding decisions were appropriately recorded.

21. The assessment and decision-making processes were timely, once information had been provided by project proponents for assessment. The department's approach was not to provide a funding recommendation on a project to the decision-maker until sufficient information had been provided to enable an informed assessment to be undertaken.

Recommendations

Recommendation no. 1 The Department of Infrastructure, Regional Development and Cities clearly identify in advice it provides to a Minister on the award of grant funding whether the proposed grant has been assessed as fully meeting, partially meeting or not satisfactorily meeting the program criteria.

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Department of Infrastructure, Regional Development and Cities response:
Agreed.

Summary of entity response

22. The proposed audit report was provided to the Department of Infrastructure, Regional Development and Cities. The department response is reproduced at Appendix 1, and is summarised below.

Department of Infrastructure, Regional Development and Cities

The Department welcomes the ANAO's conclusions and agrees with the recommendation.

Key learnings for all Australian Government entities

23. Below is a summary of key learnings, including instances of good practice, which have been identified in this audit that may be relevant for the operations of other Commonwealth entities.

Grants

- Developing clear and comprehensive grant program guidelines and governance arrangements, that are consistent with the grants administration framework, assists in managing a grants program which meets its time and impact objectives and drives quality decision making.
- Grant appraisal criteria and eligibility requirements that are shared openly and in a timely manner with applicants, can enable better quality grant applications and transparent, thorough and consistent assessment processes, including consideration of value for money.
- To ensure the best possible outcomes and value from Australian Government grants, it is important that departments scrutinise:

- proponent claims as to what benefits will result from the award of a grant;
- whether the grant funding is needed to secure those benefits; and
- whether the claimed benefits are sufficient given the amount of funding that is being sought.

**Operational Efficiency of the Australian Commission for Law Enforcement Integrity
No.4 2018–19
Australian Commission for Law Enforcement Integrity**

Summary and recommendations

Background

1. The role of the Australian Commission for Law Enforcement Integrity (ACLEI) is to support the Integrity Commissioner to provide independent assurance to the Australian Government about the integrity of prescribed law enforcement agencies and their staff. The office of the Integrity Commissioner, and ACLEI, are established by the *Law Enforcement Integrity Commissioner Act 2006* (LEIC Act).
2. ACLEI's stated purpose is to make it more difficult for corruption in law enforcement agencies to occur or to remain undetected.¹ ACLEI undertakes a range of detection, investigation and prevention activities to deliver on its purpose and fulfil requirements under the LEIC Act.
3. Since its establishment in 2006, ACLEI's jurisdiction and resources have expanded considerably. There are currently five prescribed law enforcement agencies within the jurisdiction of the Integrity Commissioner. In 2016–17 ACLEI's total funding from government was \$10.8 million and ACLEI's average staffing level was 46.8.
4. A key requirement on the Integrity Commissioner, as the accountable authority of ACLEI under the *Public Governance, Performance and Accountability Act 2013*, is to promote the proper management and use of public resources for which the Commissioner is responsible.² This entails managing and using ACLEI's resources efficiently as well as effectively, ethically and economically.
5. The Joint Parliamentary Committee on the Australian Commission for Law Enforcement Integrity was established under the LEIC Act to oversight ACLEI.³

Rationale for undertaking the audit

6. This topic was selected for audit as part of a series of performance audits focussing on the efficiency of entities. ACLEI plays an important role in the Australian Government's law enforcement framework and has undergone various changes to its funding and jurisdiction over the past 10 years. ACLEI has not previously been the subject of an ANAO performance audit.

Audit objective and criteria

7. The objective of this audit was to examine the efficiency of ACLEI in detecting, investigating and preventing corrupt conduct. To form a conclusion against the audit objective, the following high level criteria were adopted:

- Has ACLEI established appropriate arrangements to assess its efficient use of resources?

¹ See ACLEI's 2017–18 Corporate Plan at <https://www.aclei.gov.au/corporate-plan-2017-18>.

² See sub-section 15(2) of the *Public Governance, Performance and Accountability Act 2013*.

³ See section 213 of the *Law Enforcement Integrity Commissioner Act 2006*.

- How well does ACLEI's efficiency compare with comparable entities and its own previous performance?
8. The audit objective and scope does not include assessing ACLEI's operational effectiveness and no conclusions are made on this issue. The audit also did not seek to form a conclusion on the adequacy of ACLEI's resourcing.

Conclusion

9. As ACLEI has not measured, benchmarked or reported on its efficiency in detecting, investigating and preventing corrupt conduct the ANAO has not been able to conclude whether ACLEI has been operating efficiently. The ANAO's analysis and work that is underway within ACLEI indicates that improving case management and prioritisation practices is key to improving ACLEI's operational efficiency as well as aligning its resource allocation with the legislative obligation to focus on serious and systemic corruption.

10. ACLEI has not established appropriate arrangements to enable an assessment of its operational efficiency to support the risk-based prioritisation of resources. While ACLEI measures the timeliness of assessments completed, a wider focus on the final outputs to be produced from its operational activities would provide a more robust indicator of performance.

11. ACLEI does not assess its operational efficiency against its own past performance or other organisations. The ANAO's analysis indicates that the efficiency of ACLEI's investigation activities requires particular improvement, including to address growth in the number of investigations commenced compared to the number of investigations completed.

Supporting findings

Measuring and supporting operational efficiency

12. ACLEI has not established appropriate performance measures to inform itself, the Parliament and stakeholders (including law enforcement agencies) of how efficient its activities are in detecting, investigating and preventing corrupt conduct.

13. ACLEI has implemented systems and processes to capture some input and output data which can be used to calculate basic measures of its efficiency, including proxy measures. There is scope for ACLEI to improve its data collection and analysis to support a wider range of efficiency indicators.

14. ACLEI's case selection and prioritisation decisions have not fully supported the efficient use of resources. Case selection decisions have resulted in significant growth in investigations commenced, but prioritisation of cases and resources have not led to a commensurate increase in the number of investigations being concluded.

15. ACLEI has implemented and sought to extend information sharing and shared services arrangements to support the efficiency of its operations. The impact of these arrangements is not clear due to a lack of relevant performance information.

Comparing operational efficiency

16. ACLEI does not measure changes in the efficiency of its detection, investigation and prevention activities over time. The ANAO's analysis indicates that the efficiency of ACLEI's investigation activities may have deteriorated over time, while the timeliness of its assessment process has improved. When investigations have been concluded and resulted in the preparation of a brief of evidence, a high proportion of briefs have been accepted by the prosecuting authority with convictions then secured in the significant majority of cases.

17. ACLEI has not benchmarked its operational efficiency against other organisations, including State-based anti-corruption agencies. The ANAO's analysis of ACLEI's operational efficiency against four anti-corruption agencies in Australia indicated that the efficiency of assessments completed by ACLEI has improved and is comparable to other agencies, while ACLEI is relatively less efficient in concluding investigations.

Recommendations

Recommendation no. 1
Paragraph 2.21 ACLEI develop performance measures focussed on the efficiency of its operations and collect additional data to report on its performance against those measures.

ACLEI's response: *Agreed with qualifications.*

Recommendation no. 2
Paragraph 2.41 ACLEI investigate whether it could introduce a more structured review process to support the prioritisation of available resources on a risk basis to the highest value investigations, including time or milestone based intervals to trigger decisions on the ongoing allocation of resources.

ACLEI's response: *Agreed.*

Recommendation no. 3
Paragraph 3.38 ACLEI periodically compare and benchmark its operational efficiency against comparable organisations including other anti-corruption bodies, and with its own performance over time, to determine whether changes to its current processes are required.

ACLEI's response: *Agreed.*

Summary of entity responses

18. ACLEI's summary response is reproduced below. The four State agencies whose data was used as part of the benchmarking analysis for this audit elected not to provide a formal response.

Australian Commission for Law Enforcement Integrity

The Australian Commission for Law Enforcement Integrity notes the results and thanks the Australian National Audit Office for the opportunity to respond.

Key learnings for all Australian Government entities

19. Below is a summary of key learnings, including instances of good practice, which have been identified in this audit that may be relevant for the operations of other Commonwealth entities.

Measuring and comparing efficiency

- Efficiency involves making the best use of available resources to achieve required outputs. Selecting performance measures that focus on the final outputs to be produced, rather than interim processes, is likely to provide a more robust indicator of performance.
- An appropriate set of efficiency measures can help to inform accountable authorities on the allocation of entity resources in pursuit of the best outcomes for government and the community. Including efficiency measures in Annual Performance Statements supports transparency and accountability for entity performance.
- Efficiency can be relative rather than absolute. Identifying suitable comparators to assess efficiency against provides a useful indicator of performance. Comparators can include: past performance; organisations with comparable functions or processes; or appropriate targets and benchmarks.

Statistical Business Transformation Program – Managing Risk

No.5 2018–19

Australian Bureau of Statistics

Summary and recommendations

Background

1. The Australian Bureau of Statistics (ABS) is an independent statutory body, providing official statistics on a wide range of economic, social, population and environmental matters. The primary functions, duties and powers of the ABS are set out in the *Australian Bureau of Statistics Act 1975*, the *Census and Statistics Act 1905* and the *Public Governance, Performance and Accountability Act 2013*.

2. The Statistical Business Transformation Program (the Program) is a major business re-engineering program to address a significant risk of statistical system failure resulting in an inability to deliver quality, relevant and timely data to ABS customers. It is intended to replace a large number of disparate systems and processes with an integrated, enterprise-wide business architecture solution that would reduce the risk of system failure, increase efficiency and improve access to data. In December 2014, the Government approved \$257 million to implement the Program. An additional \$13 million was provided in the 2018–19 Budget.

Rationale for undertaking the audit

3. The 2016 Australian Census of Population and Housing highlighted the need for the ABS to have a strong risk management framework. The Statistical Business Transformation Program represents a significant investment of public resources and there are major risks involved with such a large and complex program of work. The audit will provide assurance regarding the adequacy of risk management arrangements underpinning the delivery of the Program. Any suggestions for improvement or recommendations from the audit could usefully inform the delivery of the remaining elements of the Program and assist the ABS to improve its approach to risk management.

Audit objective and criteria

4. The objective of the audit was to examine whether the ABS has established effective risk management arrangements to support the implementation of the Statistical Business Transformation Program.

5. To form a conclusion against the audit objective, the Australian National Audit Office (ANAO) adopted the following high level criteria:

- Has the ABS established an effective enterprise-level risk management framework?
- Are identified Program risks being effectively managed?

Conclusion

6. Risk management arrangements to support the implementation of the Statistical Business Transformation Program are effective except for the requirement to monitor and assess risk

treatments and take corrective action. The ABS enterprise-level risk management framework is not fully effective.

7. The ABS has established an enterprise-level risk management framework that partly meets the minimum requirements set out in the Commonwealth Risk Management Policy. The framework has not been fully embedded into business processes and procedures. The ABS cannot demonstrate that it actively manages its strategic risks or provides regular executive oversight of strategic risk.

8. The ABS has established an appropriate risk management framework for the Statistical Business Transformation Program, which outlines the strategy and processes for managing risk within the Program. Program risks have been identified and assessed and treatments planned in accordance with the framework. The ABS has not always met the requirement to monitor the effectiveness of treatments and take action where responses do not meet expectations. The ABS has taken steps to improve risk management capability within the Program.

Supporting findings

Establishing an effective enterprise-level risk management framework

9. The ABS has developed a risk management framework that partly meets the requirements of the Commonwealth Risk Management Framework. The ABS cannot demonstrate that it actively manages its strategic risks and has not implemented recommended improvements to the risk management framework.

10. Reviews of the ABS have identified that its risk management framework is embedded into some parts of the organisation. However, inconsistencies in risk management guidance and work practices, and limited executive level oversight of strategic risk indicates that the framework is not fully embedded into all business processes and procedures.

11. The ABS has identified a target level of risk management capability and, in 2018, assessed that it meets that target level. However, key risk management activities relating to capability have been identified that have not yet been completed.

Managing Statistical Business Transformation Program risks

12. Sound Program governance arrangements have been articulated in the Program governance plan. Risk is primarily the responsibility of the Program Delivery Board, which regularly addresses risk related matters.

13. The ABS has developed an appropriate Program risk management framework and implementation is largely effective, but treatments are not always managed in accordance with the framework. The ABS has not updated the Program risk appetite statement since 2015.

14. The risk that the ABS will not have sufficient funds to fully implement the Program has not been managed effectively. The ABS has not quantified the scale of funding issues or revised the Program costs to reflect changing circumstances.

15. The ABS has identified a shortage of project and program management capability within the Program and taken steps to increase the level of skill in this area.

16. The ABS has arrangements in place to communicate with stakeholders and report on Program risks. Internal reporting includes detailed information about the status of risks and issues. Communication to external stakeholders is more general in nature and focuses on broader ABS transformation and associated risks.

Recommendations

- Recommendation no.1**
Paragraph 2.26
- The ABS:
- (a) finalise its risk management framework and ensure that the revised 'framework complies with the Commonwealth Risk Management Policy and is embedded into its processes and procedures; and
 - (b) implement an effective process to manage strategic risks.
- Australian Bureau of Statistics response:** *Agreed.*
- Recommendation no.2**
Paragraph 3.49
- The ABS update the total Program cost estimate, incorporating all work yet to be completed in accordance with the revised Program schedule, and effectively manage the Program budget to ensure that the Program achieves the intended benefits and meets Program outcomes.
- Australian Bureau of Statistics response:** *Agreed.*
- Recommendation no.3**
Paragraph 3.51
- The ABS monitor Program risk treatments and take action when treatments are not effective.
- Australian Bureau of Statistics response:** *Agreed.*

Summary of the Australian Bureau of Statistics' response

17. A summary of the ABS' response is below and the full response is at Appendix 1.

The ABS has been managing risk over its 113 year history with external expectations that we deliver perfect statistics with perfect processes. The challenge for the ABS has been to maintain this standard of delivery for around 500 statistical releases a year using increasingly complex technical solutions in the face of tightening resourcing. The threats associated the new technologies are themselves growing at an accelerating rate. The ABS has meanwhile been assiduous in managing the risks associated with its Statistical Business Transformation Program. The Department of Finance Gateway review of December 2017 found that "the Program is proceeding well. Significant progress has been made in many areas including governance, transition planning, risk management, benefits management and change management. The Program is well placed to meet its original outcomes ... Since the last review some risks have been effectively resolved while some new risks have emerged. The ABS has recognised these risks and is working to mitigate them as far as possible." The Gateway Review noted in relation to the Independent Assurer for the program that "the external assurance provided by KPMG continues to contribute to effective Program risk management".

The Statistical Business Transformation Program will be an important enabler for the future of ABS. The Program is the subject of unrelenting vigilance at every level of governance, not least the ABS Executive Board itself where risk is inherently the focus of every decision within the Program. The challenge throughout has been to balance the technical challenge of business transformation with resources — a matter of ongoing concern, constant revision, and regular consultation with Government - and the inevitable uncertainties associated with migrating from aged legacy systems to new platforms while managing statistical risk. ABS will continue to manage the budget for the Statistical Business Transformation Program, consulting closely with Government, and to monitor and manage the broader suite of risks associated with the Program.

At the same time ABS has taken steps to formalise its enterprise level management of risk in accordance with the Commonwealth Risk Management Policy and will continue its efforts to improve. This follows action in preceding years to improve our management of statistical risks for Australia's essential national statistics, starting with our main economic and population statistics and progressing through our statistical program.

Key learnings for all Australian Government entities

18. Below is a summary of key learnings, including instances of good practice, which have been identified in this audit that may be relevant for the operations of other Commonwealth entities.

Governance and risk management

- Entities should have in place a risk management framework that complies with the Commonwealth Risk Management Policy, and:
 - is reviewed regularly;
 - includes a formal mechanism to ensure enterprise-level and strategic risks are monitored and reported to the executive;
 - establishes an appropriate level of risk management capability; and
 - is embedded in the entity's business practices.

Program Implementation

- Entities should regularly update overall cost estimates for complex programs so that appropriate, timely action can be taken to address the risk of insufficient funding to meet program objectives.

**Army's Protected Mobility Vehicle–Light [Hawkei]
[No.6 2018–19]
Department of Defence**

Summary and recommendations

Background

1. The Protected Mobility Vehicle–Light project aims to provide the Australian Defence Force with highly mobile field vehicles that are protected from ballistic and blast threats. The Department of Defence (Defence) commenced the acquisition process in 2006, and in 2008 adopted a strategy to procure the Joint Light Tactical Vehicle (JLTV) being developed by the United States. The vehicle ultimately selected in 2015 was the Australian-developed Hawkei vehicle designed by Thales Australia (Thales).

2. In October 2015, Defence entered into a contract with Thales to acquire and support 1100 Hawkei vehicles and 1058 trailers. Total budget and related funding for the Protected Mobility Vehicle–Light capability, as estimated by the ANAO, is \$2.2 billion.¹ Defence has expended \$463.1 million of project funds to 30 June 2018, as well as \$293.9 million on related costs. The first Low-Rate Initial Production vehicles were scheduled for delivery in February 2018.

Rationale for undertaking the audit

3. This project was selected for audit because of the materiality of the procurement, the adoption of a sole-source procurement strategy, the time taken to select a vehicle, and the risk involved in manufacturing a relatively small run of vehicles when the United States was beginning a similar but much larger program.

Audit objective and criteria

4. The objective of the audit was to assess the effectiveness and value for money of Defence's acquisition of light protected vehicles, under Defence project Land 121 Phase 4. To form a conclusion against the audit objective, the ANAO adopted the following high-level criteria:

- Defence conducted an effective procurement process that achieved value for money.
- Defence has established effective project governance and contracting arrangements.

Audit methodology

5. The audit method involved:
- fieldwork at Defence's Land Systems Division in Melbourne, Defence's vehicle testing facility at Monegeetta (Victoria), Defence's explosives testing facility at Graytown (Victoria), the Thales facility in Bendigo (Victoria) and the Thales computing laboratory in Rydalmere (New South Wales);
 - analysis of information from Defence systems covering the period 2006–18; and
 - interviews with Defence project personnel and contractors.

¹ Comprising approved project funding of \$1.9 billion and related costs of \$293.9 million. Defence's acquisition contract with Thales is for \$1328.5 million.

Attorney-General's certificate

6. Information has been omitted from this performance audit report following a decision by the Attorney-General, under paragraph 37(1)(b) of the *Auditor-General Act 1997* (the Act), that in his opinion the disclosure of certain information would be contrary to the public interest for one or both of the reasons set out in paragraphs 37(2)(a) and 37(2)(e) of the Act. The Attorney-General issued a certificate to this effect on 28 June 2018. The Auditor-General received the certificate on 29 June 2018. A copy of the Attorney-General's certificate is included as Appendix 5 to this audit report. The specific information required to be omitted by the certificate has been omitted. Where information has been omitted from this report on this basis, that omission is signalled by a grey redaction square together with the words 'Omitted—certificate' and the relevant ground under subsection 37(2).

7. The Attorney-General's requirement under the certificate, that the Auditor-General omit part of his audit conclusion relating to the effectiveness and value for money of this acquisition, has resulted in a disclaimer of opinion, set out in paragraph 10.

8. Under subsection 37(3) the Act, the Auditor-General cannot be required and is not permitted to disclose information omitted under subsection 37(1) to a House of the Parliament, a member of a House of the Parliament, or any committee of the Parliament. The Act further provides that if the Auditor-General omits information because of subsection 37(1) from a public report, the Auditor-General may prepare a report under paragraph 37(5)(b) that includes the information concerned, and must give it to the Prime Minister, the Minister for Finance and any responsible Minister. The Auditor-General provided a confidential report to the Prime Minister, Minister for Finance and the Public Service, the Minister for Defence and the Minister for Defence Industry on 6 September 2018.

9. Defence's procurement of Hawkei vehicles has continued during the Attorney-General's considerations regarding a certificate, and the ANAO's performance audit engagement has also continued in accordance with the ANAO Auditing Standards. This report has been updated to reflect material events in the procurement until July 2018.

Disclaimer of Conclusion

10. Because of the significance of the matter described in the Basis for Disclaimer of Conclusion section of my report, I have not been able to prepare a report that expresses a clear conclusion on the audit objective in accordance with the ANAO Auditing Standards. Accordingly, I am unable to express a conclusion on whether the Department of Defence's acquisition of light protected vehicles under Defence project Land 121 Phase 4 was effective and achieved value for money.

Basis for Disclaimer of Conclusion

(a) On 29 June 2018 I received correspondence from the Attorney-General which constituted his certificate under section 37(1)(b) of the *Auditor-General Act 1997* (the Act). The Attorney-General advised that in his opinion disclosure of certain information in my proposed performance audit report would be contrary to the public interest for one or both of the following reasons set out in section 37(2) of the Act:

- it would prejudice the security, defence or international relations of the Commonwealth;
- it would unfairly prejudice the commercial interests of any body or person.

(b) Under section 37(1)(b) of the Act, I am thereby prevented from including particular information in this report. The information to be omitted included part of my overall conclusion in respect of the objective of the audit.

(c) The overall conclusion included in my proposed performance audit report stated:

Defence has invested significant effort into developing a capable light protected vehicle, including through an extensive test and evaluation program, and is procuring a design (Hawkei)

that meets the majority of the requirements.

Omitted--certificate--s 37(2)(a) and s 37(2)(e); see paragraph 6.

Defence has established appropriate arrangements for project governance, but has accepted additional risk by entering Low-Rate Initial Production while reliability issues are still being remediated.

- (d) The conclusion that I included in my proposed performance audit report was formed on the basis of sufficient appropriate audit evidence. The ANAO Auditing Standards require my audit report to contain a clear expression of the conclusion against the objectives of the audit. If I were to include the conclusion from the proposed performance audit report after omission of the information required by the certificate, I would not be expressing such a conclusion, and therefore it would not be in compliance with the ANAO Auditing Standards.
- (e) As the certificate amounts to a limitation on the scope of my audit, because I am unable to table a report in the Parliament that contains a clear expression of my conclusion against the audit objective, there are two options available to me under the ANAO Auditing Standards: to withdraw from, or reduce the scope of, my audit; or publish a report including a Disclaimer of Conclusion. I decided to publish a report containing a Disclaimer of Conclusion because it is in the public interest for me to present information to the Parliament, in accordance with the Act and the ANAO Auditing Standards, to the largest extent possible in the circumstances.

Key findings

11. Defence developed six fundamental requirements for the Protected Mobility Vehicle–Light by 2009, and these have remained relatively stable. The Hawkei is a developmental vehicle, and Defence has conducted a large amount of test and evaluation covering its technical performance and useability.

12. At First Pass in 2008, a financial partnership with the United States in its JLTV Program was adopted as the primary acquisition strategy, at a cost of \$43 million. In 2009, Defence sought approval to commence a parallel investment in Australian-based options that it had previously decided to be high-risk and high-cost. At Interim Pass in December 2011, Defence recommended and received approval for further development of the Thales Hawkei, because Defence considered it had the best prospect of meeting future needs, despite assessing it as the least developed Australian option. At the same time, Australia’s financial partnership in the JLTV Program was discontinued amidst uncertainty as to the program’s future, but it was retained as a possible alternative option for Second Pass. Within days of the Interim Pass decision, the United States decided to continue the JLTV Program. Defence did not reconsider its Interim Pass recommendations in the light of this significant change. The 2011 decision to discontinue Australian financial participation in the JLTV Program eroded Defence’s ability to benchmark its procurement of the Hawkei against a comparable vehicle. In the absence of reliable benchmark information, there was a reduction in Defence’s ability to evaluate whether procurement of the Hawkei clearly represented value for money.

13. Defence did not provide robust benchmarking of the Hawkei and Joint Light Tactical Vehicle options to the Government at Second Pass, to inform the Government’s decision in the context of a sole-source procurement. At Second Pass, Defence advised the Government that the Hawkei would be approximately 23 per cent more expensive to acquire than the Joint Light Tactical Vehicle but would also be more capable. Without robust benchmarking of cost and capability, Defence was also unable to apply competitive pressure in its negotiations with Thales. Defence did not inform the Minister appropriately when material circumstances changed immediately after Second Pass and before contract signature.

Omitted--certificate--s 37(2)(a) and s 37(2)(e); see paragraph 6.

14. Defence has established appropriate oversight arrangements for the project. However, Defence postponed the May 2017 Gate Review, with the result that the project passed the major

milestone of entry into Low-Rate Initial Production without the scrutiny offered by these reviews. Test and evaluation activity remains ongoing, as Defence entered Low-Rate Initial Production without retiring risk to the extent that it had planned. Defence has amended its contract with Thales to manage the related delays and cost increases. The project remains within the government-approved and contracted budget and scope, but reliability issues have led to schedule delays.

Supporting findings

Initial requirements and testing

15. Defence recognised early that its initial required number of vehicles (Basis of Provisioning) was unaffordable within the budget that it had been allocated, and its advice to Government consistently made this point. In 2008, Defence advised the Government that it required 1300 protected vehicles and associated trailers. In 2015, the acquisition contract provided for 900 fully protected and 200 baseline (less protected) vehicles and 1058 trailers.

16. Defence did not complete a fully developed Function and Performance Specification until July 2010, after the Request for Proposal for an Australian-manufactured option was released in June 2009. The six fundamental requirements (survivability, mobility, payload, advanced communications, useability and sustainability) have remained relatively stable during the remainder of the project, and the detailed requirements underpinning them have been refined through developmental test and evaluation. Some requirements, such as weight and reliability, have been amended in the course of development. Defence decided in 2017 to remove the exportable power requirement, which had a contracted value of \$30 million. As at July 2018, Defence was considering the return of funds from Thales following removal of that requirement.

17. Readiness for an advanced communications and control system is one of the six fundamental requirements. Defence did not have a detailed specification for this aspect of the vehicle until September 2014, and two rounds of requirements definition were conducted in 2016.

18. To manage the risk of this developmental project, Defence conducted a two-stage test and evaluation program of the Land 121 Phase 4 vehicle options between 2011 and 2013, including: user tests; landmine blasts; side blasts; ballistics testing; and air transportability testing. This program has contributed to Defence procuring a design (Hawkei) that meets the majority of its requirements.

19. By late 2013, the Hawkei design still represented a high risk. Defence amended some requirements as a result of the findings of the test and evaluation program, and conducted an additional Risk Reduction Activity during 2014, reducing the design risk to medium. Defence did not expect to achieve a stable design before signing the acquisition contract in late 2015.

The procurement process (First Pass and development contracts)

20. At First Pass in 2008, Defence adopted what it considered the least risky option of partnership in the United States JLTV Program, at a cost of \$43 million, while also retaining the option of a military-off-the-shelf option. After extensive industry lobbying, Defence sought approval to commence a parallel investment in Australian-based options that it had previously decided to be high-risk and high-cost and had not presented for government consideration at First Pass.

21. Between July and November 2011, Defence received strong indications and advice from the United States Government that the JLTV Program was likely to experience lengthy delays, and possibly be cancelled. In November 2011, the Defence Minister directed that no further Australian investment in the program be made without his approval.

22. At Interim Pass in December 2011, Defence recommended, and received approval for, the Thales Hawkei as the primary Australian acquisition option following the Stage 1 test and evaluation process conducted during 2010–11. Defence considered that this design had the best prospect of

meeting future needs, although it was the least developed Australian vehicle design. Defence noted that all three Australian options it had tested exceeded the project's budget. Defence did not make the Government aware of the results of an economic study it commissioned that found there would be limited regional economic benefits from, and a substantial premium paid for, the Hawkei build.

23. Defence records indicate that a significant driver of the Hawkei project schedule was the retention of production capacity at Bendigo after Bushmaster production ceased in late 2016. Defence recommended further production of Bushmasters at Bendigo to keep the facility in operation pending possible Hawkei approval. This was funded at a cost of \$221.3 million, representing more than a ten per cent increase to Defence's expenditure related to acquiring the Hawkei capability. This expenditure was not taken into account in assessing the overall cost and value for money of the Hawkei project at Second Pass.

24. Defence did not reconsider its Interim Pass recommendations after new and potentially material information became available regarding the JLTV Program soon after Interim Pass governmental approval, and did not seek ministerial approval to continue Australian participation in the JLTV Program. The decision not to seek ministerial approval to continue in the JLTV Program reduced Defence's ability to benchmark its procurement of the Hawkei and apply competitive pressure, and together with the decision not to factor-in related expenditure, reduced Defence's ability to evaluate whether procurement of the Hawkei clearly represented value for money.

The procurement process (sole-source tender and Second Pass acquisition decision)

25. Defence decided to release a sole-source Request for Tender for the Hawkei in 2014. In this context, Defence usefully sought benchmarking analysis from a consultancy in 2014. The benchmarking analysis had to rely on 2011 open-source information for the Joint Light Tactical Vehicle for both price and capability (as Defence was no longer a partner in the JLTV Program). The analysis also compared the Joint Light Tactical Vehicle's 2011 compliance with requirements with the Hawkei's expected 2023 compliance with requirements.

26. Defence's assumptions as to government support for ongoing vehicle production at Thales' Bendigo facility and workforce continuity at the facility led Defence to maintain its schedule to Second Pass, rather than seeking consideration of a delay to obtain reliable benchmarking data.

27. Although the Government decided in 2011 that the Joint Light Tactical Vehicle would be the alternative option to the Hawkei, Defence's comparison of this vehicle with the Hawkei at Second Pass in August 2015 was not based on up-to-date information. As discussed above, Defence's consultancy advice provided to the Government at Second Pass—that the Hawkei would be 23 per cent more expensive to acquire than the Joint Light Tactical Vehicle, but would be a more capable vehicle—relied on 2011 open-source data for the Joint Light Tactical Vehicle for both price and capability.

28. Defence did not advise the Minister of the full implications of new and potentially material information—which included cost information—when the Joint Light Tactical Vehicle manufacturer was selected by the United States one week after Second Pass. Defence did not subsequently use the information available after the Joint Light Tactical Vehicle announcement to strengthen its negotiating position. Defence records indicate that Thales refused to negotiate anything of significance after it knew that the Australian Government had approved the acquisition of Hawkei vehicles. Defence advised the Minister that negotiations had been successfully concluded. The final negotiation report, completed one day after this advice to the Minister, drew to Defence's attention significant shortcomings in the negotiation strategy and outcomes.

29.

Omitted--certificate--s 37(2)(a) and s 37(2)(e);
see paragraph 6.

[REDACTED]

Defence advised the ANAO in December 2017 that a number of non-financial benefits of the Hawkei capability contributed to the overall value-for-money proposition of the Hawkei, including: the leading-edge protected vehicle and the Integral Computing System; the ability to adapt the capability to meet emerging threats; and the Commonwealth's Intellectual Property rights and potential royalties. These issues were mentioned in the 2015 Second Pass advice to Government, which supported the Hawkei acquisition and outlined the 23 per cent price difference of the Hawkei over the Joint Light Tactical Vehicle.

Governance and contracting arrangements

30. Defence has established appropriate oversight arrangements for the project. Senior leadership is updated on a monthly basis about key project issues. Regular contract progress meetings are held between senior project staff from Defence and Thales. The minutes of the meetings show a detailed presentation of information from Thales, ranging across the breadth of the project, and probing questioning from Defence that shows active management.

31. The 2016 Gate Review of the project raised concerns about the major challenges facing the project office and the risk of major failure by the contractor. The Gate Review scheduled for May 2017 was postponed until October 2017. This decision meant that the project passed the major milestone of entry into Low-Rate Initial Production without the scrutiny offered by these reviews.

32. Defence has generally effective contracting arrangements, but the contractual off-ramps did not represent a practicable risk mitigation strategy, because Defence has not maintained the market knowledge required to inform an exit strategy. Relevant market knowledge would enable capability and value-for-money comparisons to be made of the Hawkei and comparable vehicles.

33. The project has conducted a series of reliability trials, and the test and evaluation period has been extended as part of this process. Defence approved entry into Low-Rate Initial Production in September 2017 while reliability issues were still being remediated through a Reliability Remediation Plan and a Reliability Demonstration Test. In compensation, Thales provided a one-year extension of the vehicle warranty and a \$3 million discount on materials costs. Defence advised the ANAO in December 2017 that the core Integral Computing System—inclusive of all hardware, operating software, and the Battle Management System—is included on Low-Rate Initial Production vehicles (currently being produced). The project remains within the government-approved and contracted budget and scope, but reliability issues have led to schedule delays.

Responses to the audit

34. The proposed public and confidential reports were provided to the Department of Defence (Defence). Extracts from the proposed public report were provided to Thales Australia Limited (Thales) and to Elbit Systems of Australia (Elbit).

35. Formal responses were received from Defence, Thales and Elbit. The summary responses from Defence and Thales are provided below.

Department of Defence

The Department notes the ANAO's findings regarding the acquisition of the Hawkei – Protected Mobility Vehicle – Light and appreciates the work undertaken by the ANAO to consider Defence's feedback in preparing the Final Report. The identified Key Learnings are acknowledged and will support Defence's approach to capability acquisition.

The Hawkei provides Australia with a domestically developed and sovereign capability that can be modified to meet emerging threats and protect Australian Defence Force personnel.

Defence is also confident that the Hawkei has the potential to be modified to meet the requirements of our security partners and provide these nations with a highly effective capability.

Thales Australia

Thales Australia welcomes the engagement with industry in the preparation of this report, resulting in the exclusion from publication of sensitive information that could have endangered soldiers' lives or unfairly prejudiced commercial interests.

By adopting the Australian designed and developed Hawkei the Australian Army has maintained a critical sovereign capability in protected vehicle design, engineering and manufacture in Australia. It is a capability advantage developed in the Bushmaster program that has been proven to save lives. This decision has delivered the world's best vehicle of its type, developed and manufactured in Australia, and supporting more than 400 Australian jobs directly in the assembly and manufacturing supply chain.

ANAO comment on Thales Australia's summary response

36. The treatment of sensitive information arises regularly in the context of Defence auditing. The ANAO has long-established processes for working with Defence to manage potential risks relating to the disclosure of sensitive information. These processes include the provision of consultation drafts to Defence, an exit interview, regular officer-level interactions, and seeking formal advice from Defence. In this audit, Defence and the ANAO worked together through an iterative process to identify and manage potential risks.

Key learnings for all Australian Government entities

37. The ANAO has not made recommendations in this audit report, but rather has focused on the key learnings flowing from the audit for Defence and other Australian Government entities.

Procurement

- Effective benchmarking of cost and capability provides a basis for assessing value for money in sole-source procurements and maintaining competitive pressure in the negotiation and contracting phases.
- Effective benchmarking should provide the information needed to assess and explain differences in the price, quality and quantity of goods and services purchased.

Governance and risk management

- Contractual risk mitigation strategies such as off-ramps should be practicable, particularly in a sole-source procurement.
- When circumstances external to a project materially change and may affect the interests of the Commonwealth, entities should return to the Minister with updated advice.
- All the key drivers for an acquisition project should be transparent—including in the planning, advice and selection/assessment criteria relating to the project.

**Management of the Regional Network
No.7 2018–19
Department of the Prime Minister and Cabinet**

Summary and recommendations

Background

1. On 2 March 2015, the Department of the Prime Minister and Cabinet (PM&C or the department) operationalised its Regional Network (the Network). Unlike the previous state-based model, the Network consists of 12 geographic regions and two support branches. The Network was expected to ‘simplify reporting structures and enable decisions to be made closer to the people and communities that are impacted’.¹
2. The Network is expected to play a central role in achieving the department’s purpose of ‘improving the lives of Indigenous Australians’, and is responsible for the delivery of Indigenous affairs policies and programs and engagement with Indigenous communities. The intent of the model was that intelligence gathered by the Network could be fed to policy areas located centrally in the Indigenous Affairs Group within PM&C to support continual improvements to policy and program design. The Network’s strategic activities are: stakeholder collaboration; policy advice and coordination; contract management and delivery; enhancing internal capability; event coordination; support and advice; and monitoring and implementation.
3. The Government has allocated \$1.93 billion for Indigenous-specific programs in 2018–19, with an intended focus on the priority areas of school attendance, employment and community safety. This allocation includes \$1.24 billion for the Indigenous Advancement Strategy (IAS), which is distributed through grants administered by officers in the Network. In 2018–19, the Network’s budget is \$68.77 million to support the delivery of Government’s Indigenous affairs priorities.

Rationale for undertaking the audit

4. The Network operates as an important on-the-ground presence for the Australian Government – to oversee the delivery of government programs and to engage with local communities. It is fundamental to the Government’s ‘commitment of doing things “with”, not “to” Indigenous people’.² The Network is also a key mechanism for liaison with other Australian Government and state government departments that operate in similar arenas.
5. The audit was proposed following the ANAO’s performance audit of the IAS (Auditor-General Report No. 35 of 2016–17). The IAS audit found that opportunities for community involvement in early rounds of the strategy (conducted during 2014 and 2015) had been limited, and recommended that administrative arrangements be revised to allow greater opportunity for the Network to work in partnership with Indigenous communities and deliver local solutions. The IAS audit also found that

¹ The Department of the Prime Minister and Cabinet, *Annual Report 2014–15*, PM&C, Canberra, 2015, p. 147.

² Turnbull, M, 2018, ‘Closing the Gap report 2018’, speech, presenting the Closing the Gap Prime Minister’s Report 2018 for tabling in the House of Representatives, Canberra, 12 February.

reports to the Minister provided a 'reflection of activity within the regions, but do not meaningfully report on the performance of the regional network'.³

Audit objective and criteria

6. The objective of the audit was to assess whether the department effectively manages the Regional Network. To form a conclusion against the audit objective, the ANAO adopted the following high level criteria:

- Was the Regional Network designed to support the achievement of the Government's policy objectives?
- Is the Regional Network operating as designed?
- Does the department effectively monitor and report on the performance of the Regional Network?

Conclusion

7. The effectiveness of the department's management of the Regional Network is mixed.

8. The design of the Network aligned to the Government's policy objectives. The department engaged with a variety of stakeholders and the final design of the Network was influenced by these consultations.

9. The department's governance arrangements are largely effective. PM&C has established an appropriate committee structure, and there is alignment between the key planning documents. The department's management of Network risks is partially effective.

10. The full potential of the Network to facilitate the design and delivery of local solutions to local problems by leveraging its understanding and connection to communities is not being maximised. The department, through the Network, has not effectively embedded arrangements to coordinate with key stakeholders, input into policy is inconsistent, and Network officers have limited authority to make decisions that impact on local Indigenous communities.

11. The department has established appropriate reporting arrangements. Performance monitoring is compromised by shortcomings in the performance measurement framework and the department has not evaluated the performance of the Network.

Supporting findings

Design of the Regional Network

12. The design of the Network aligned to the Government's objectives. The implemented Network met some of the agreed objectives, such as establishing a single network and appointing senior personnel. At that time, it did not incorporate other key elements, including devolved decision-making and effectively establishing the leadership role of the Network in remote communities.

13. When designing the Regional Network, the department drafted two implementation plans: the Network's structure; and the Commonwealth leadership role. The Network structure was in place by March 2015, and the principles for the leadership role were endorsed in October 2015.

³ Auditor-General Report No. 35 2016–17, *Indigenous Advancement Strategy*, p. 34.

14. The department consulted with a range of stakeholders including staff, an experts group, Australian Government departments and all state and territory governments. Changes to the proposed approach resulted from these discussions.

Governance arrangements for the Regional Network

15. The department has established appropriate executive structures to support the operations of the Regional Network.

16. There is consistency and alignment between the department's Corporate Plan, Divisional Plan for the Regional Network and the Branch Plans. The Regional Blueprints, and other relevant plans, are aligned with and address the Government's priorities of employment, education and community safety.

17. The Regional Network's management of risks has been partially effective. Branches have not documented their approach to risk as required. Under the new risk arrangements there will be a broader range of risks captured at the divisional level.

The Regional Network in operation

18. The Regional Network engages with a large number of key internal and external stakeholders, but has not developed or implemented a communication framework or protocols that embed this engagement in practice. As acknowledged by the Indigenous Affairs Group Executive Board, the absence of an overall engagement framework and plan risks key stakeholder confusion and consultation fatigue.

19. The department's delegation framework supports the Government's objective to have senior Network staff making local decisions. In practice, Network officers have limited decision-making authority, with the Minister for Indigenous Affairs approving the majority of funding decisions.

20. The Network was designed to actively engage with and gather intelligence from Indigenous communities. However, the Network has inconsistent input into Indigenous policy and program development and the value of the Network is not being effectively leveraged. The Network's progress against the strategy to improve its linkages with National Office is mixed, with five of the ten components not commenced.

21. The department has established adequate support for Regional Network officers. Guidance is generally clear and staff have access to a range of training options. The department has commenced a number of strategies to identify and develop capability in the Network, but this work is incomplete. The department has taken initial steps to address the issue of operating on dual ICT systems.

Performance reporting and evaluation

22. The department's performance measurement framework for the Regional Network is partially effective. The Network's performance measurement criteria are mostly relevant, but they are not reliable or complete.

23. The Regional Network has appropriate reporting arrangements for the ongoing administration of the Regional Network. There is extensive reporting that covers the operations and performance of the Network. Reporting would be enhanced if the performance measurement framework was improved.

24. The department has not evaluated the performance of the Regional Network, but it commenced a review of the Network in early 2018 — the Recalibration Project. The department has implemented one-off processes to incorporate lessons learnt into ongoing Network operations, but

continuous improvement processes are not systematic and feedback or lessons learnt do not always inform processes.

Recommendations

Recommendation no.1 The Department of the Prime Minister and Cabinet appropriately document, monitor and report against strategic and operational risks for the Regional Network.
Paragraph 3.33

Department of the Prime Minister and Cabinet response: *Agreed*

Recommendation no.2 The Department of the Prime Minister and Cabinet implement an effective internal and external stakeholder engagement and communication framework for the Regional Network.
Paragraph 4.15

Department of the Prime Minister and Cabinet response: *Agreed*

Recommendation no.3 The Department of the Prime Minister and Cabinet embed processes to ensure the knowledge of the Regional Network is appropriately leveraged in the development of Indigenous policies and programs.
Paragraph 4.28

Department of the Prime Minister and Cabinet response: *Agreed*

Recommendation no.4 The Department of the Prime Minister and Cabinet ensures that the performance criteria for the Regional Network is fit-for-purpose, relevant, reliable and complete.
Paragraph 5.14

Department of the Prime Minister and Cabinet response: *Agreed*

Recommendation no.5 The Department of the Prime Minister and Cabinet implement a systematic approach to capturing lessons learnt and feedback received by the Regional Network and incorporating the information into ongoing operations to improve processes and performance.
Paragraph 5.35

Department of the Prime Minister and Cabinet response: *Agreed*

Summary of entity response

25. The draft report was provided to the department, and a section of Chapter 4 was provided to the Minister for Indigenous Affairs as an extract. A summary of the department's response is below.

The Department welcomes the Audit's findings which will support ongoing work to improve the effectiveness of the Regional Network.

The establishment of the Regional Network, formalised in March 2015, has been central to the Department's approach to addressing Indigenous disadvantage across Australia. The Regional Network represents a major change to the Department's structure and operation, and continuously improving the way the Network operates remains a priority.

The Department accepts all five recommendations, noting that actions have been already taken or are underway that implement improvements consistent with those recommendations. These actions include revisions to risk management and communications processes, and the recalibration process currently underway.

Key learnings for all Australian Government entities

26. Below is a summary of key learnings, including instances of good practice, which have been identified in this audit that may be relevant for the operations of other Australian Government entities.

Program implementation

- The Government's objectives for a program should be embedded in its design and structure, as well as throughout program implementation, governance structures, risk management and performance monitoring. The Regional Network was designed to meet the Government's objective of connecting with and targeting community level service delivery, but was not fully implemented as designed. As a result, the value of the Network has not been maximised.

Program design

- When designing the Network the department consulted with a range of stakeholders, which is good practice. When re-designing a long-running program it is important to consult effectively with key stakeholders to benefit from the experience of others and understand cultural context, challenges and opportunities. Consultation, when appropriately targeted, can result in useful information that better informs program design and implementation.

Policy/program design

- A strong interaction between an entity's policy and delivery functions is necessary to ensure lessons learnt from previous program implementation and policy design are incorporated into the design of new policies or programs.

Performance and impact measurement

- When designing a performance measurement framework, performance indicators and targets should be suitable for the program or function, relevant, reliable and complete, and have an appropriate balance between quality and quantity.

**Management of Commonwealth Leased Office Property
No.8 2018–19
Department of Finance**

Summary and recommendations

Background

1. Australian Government entities use real estate such as offices, shopfronts and special purpose facilities to assist in delivering outcomes.
2. Within the non-Defence domestic property portfolio, 94 per cent of office accommodation is leased rather than owned. In 2016–17, expenditure on leased office property (excluding capital costs) was around \$2 billion.
3. Under the *Public Governance, Performance and Accountability Act 2013*, accountable authorities are responsible for the proper management and use of resources under their control. At the same time, the Department of Finance (Finance) has a broader role to administer the Commonwealth Property Management Framework. This Framework provides guidance and requirements on various aspects of leased or owned Commonwealth property in Australia.
4. Since 2014, Finance has pursued a ‘program of work’ on leased office property that has included three main activities:
 - an initiative to reduce surplus or vacant office space, focussing initially on the Australian Capital Territory (ACT) — known as Operation Tetris;
 - establishing coordinated procurement¹ arrangements for property services, which are mandatory for non-corporate Commonwealth entities (NCEs); and
 - improving the collection and use of property data to support decision-making and reporting.
5. The Minister for Finance has announced savings of \$300 million for Operation Tetris, and a further \$100 million in savings from the coordinated procurement arrangements.

Rationale for undertaking the audit

6. This topic was selected for audit because leased office property represents a significant recurrent expense to the Australian Government and due to the significance of Finance’s program of work. Key initiatives being pursued in this area of public administration are part of a broader government agenda to create a smaller, smarter and more productive and sustainable public sector. The audit was intended to provide assurance on whether significant funding on leased office property is being managed effectively at a whole-of-government level.

¹ A coordinated procurement is an initiative to establish whole-of-government arrangements for goods and services in common use to maximise market benefits and deliver efficiencies and savings.

Audit objective and criteria

7. The objective of the audit was to assess whether effective arrangements have been established by Finance to achieve value for money outcomes for Commonwealth leased office property.
8. To form a conclusion against the audit objective, the ANAO adopted three high-level criteria:
 - Was Operation Tetris executed effectively?
 - Were good processes followed and sound advice provided to government to inform the establishment of the coordinated procurement of property services?
 - Are whole-of-government arrangements supported by relevant property data and a suitable performance framework?

Conclusion

9. Finance's program of work on leased office property has reduced surplus office space, established coordinated procurement arrangements for property services and improved the collection of property data. It is evident that efficiencies and savings have been realised from this work, but Finance's approach to estimating and tracking savings was not robust.
10. Operation Tetris has been effective in delivering better utilisation of existing Commonwealth office space, mainly in the Australian Capital Territory. The reported \$300 million in savings to entities was not supported by a sound methodology.
11. For the establishment of coordinated procurement arrangements for property services, Finance's approach of informing decisions by conducting a contestability review followed by a market testing review was sound. Cost savings were a key benefit envisaged from the arrangements. Finance's advice was not supported by a sufficiently robust savings methodology during the main decision-making stages. While a more structured approach was used to allocate the \$105.3 million in identified savings after the new arrangements had been implemented, much of the savings estimated by the allocation analysis relate to changes in market conditions rather than from the aggregation of government purchasing power.
12. Finance has improved its processes for collecting property data from entities. Its analysis of data and reporting has focussed on a narrow set of performance measures and does not include cost indicators.

Supporting findings

Operation Tetris: Reducing surplus office space

13. Prior to 2015, Finance had not used property data collected from entities (since 2009) to systematically identify surplus office space and inform appropriate responses. Following the initiation of Operation Tetris in April 2015, Finance identified various proposed moves that were expected to reduce the Commonwealth's property footprint in the ACT by about 50,000 square metres by 2018.
14. In important respects, frameworks have been strengthened. In particular, changes made to the Commonwealth Property Management Framework provided greater central visibility and authority over certain lease proposals. Finance did not follow through on establishing appropriate funding arrangements to promote and support involvement by entities.
15. The methodology used to estimate and track relevant costs and benefits was not sufficiently robust or transparent. Important aspects of the methodology were not clearly documented, and the

approach followed did not include all relevant costs (including fit-out and relocation costs). Moves were tracked but the estimates were not verified or adjusted to reflect actual outcomes.

Establishing a coordinated procurement for property services

16. Options were identified and compared. The consideration of options drew on the results of a market testing review that was informed by engagement with the property services industry (including industry advice on potential savings from a changed approach).

17. Finance's advice to government was not supported by robust analysis and evidence during the main decision-making process to establish a coordinated procurement for property services. In particular, Finance did not test the savings claims made by industry against entities' property arrangements. A more structured approach for allocating the specified total quantum of savings was developed after the new arrangements were implemented, although the estimated savings used for allocative purposes relate largely to changes in market rents and reflecting the occupational density target rather than from the aggregation of government purchasing power.

Property data and reporting

18. Finance has recently improved its processes for collecting property data from entities, establishing an online system in 2017 to replace previous manual processes. This online system allows entities and selected external providers to update and analyse data in real time. While Finance did not undertake a comprehensive review of the data before the online system was developed, it has since initiated an external review to assess the usefulness of the data.

19. Finance has not yet established all the elements of a fit-for-purpose performance framework to assess and report on its program of work on property efficiency matters. Broad objectives have been set but are not well-defined, and current performance metrics are incomplete and not properly integrated — addressing occupational density but not cost or other relevant indicators.

Recommendations

Recommendation No.1
Paragraph 3.80 The Department of Finance ensure that its ongoing program of work to deliver savings and efficiencies on Commonwealth leased office property is supported by a robust and transparent savings methodology, including by:

- (a) identifying all relevant costs and benefits that apply;
- (b) providing a clear rationale for any assumptions used;
- (c) testing principles against entities' particular property arrangements; and
- (d) verifying estimates when actual data is available.

Finance's response: *Agreed.*

Recommendation No.2
Paragraph 4.22 The Department of Finance improve its framework for assessing and reporting on its program of work on Commonwealth leased office property and related activities by: setting clearly defined objectives; and better integrating performance measures, including cost indicators.

Finance's response: *Agreed.*

Key learnings for all Australian Government entities

20. Below is a summary of key learnings, including instances of good practice, which have been identified in this audit that may be relevant for the operations of other Commonwealth entities.

Policy design

- Where advice to government includes savings estimates, entities should ensure that the estimates are supported by a suitable model or methodology, and that government is advised of any limitations with the estimates as well as timeframes for receiving more robust advice.

Procurement processes and management of probity by the Moorebank Intermodal Company
No.9 2018–19
Moorebank Intermodal Company
Department of Finance

Summary and recommendations

Background

1. The Moorebank Intermodal Company (MIC) was established in December 2012 under the *Corporations Act 2001*. It is responsible for the delivery of the Moorebank Intermodal Terminal (MIT) project in south western Sydney. In December 2017, the Australian National Audit Office (ANAO) completed an audit of the contractual arrangements for the delivery of the MIT (referred to herein as the first performance audit of MIC).¹
2. MIC is governed by a board of directors, currently comprising six directors. Three of the directors, including the Chair, have been directors since MIC's establishment in December 2012.
3. MIC's first substantive Chief Executive Officer (CEO) was selected for the role in mid-2013, and resigned in April 2018. MIC's current Interim CEO joined the company in a consulting capacity in January 2018 and was announced by the MIC Chair as the Interim CEO on 11 April 2018.

Rationale for undertaking the audit

4. During the conduct of the first performance audit of MIC, the ANAO observed a number of practices in respect of MIC's operations and procurement activities that merited further examination. Under the *Auditor-General Act 1997*, as a Government Business Enterprise, performance audits of MIC can only be undertaken at the request of the Joint Committee of Public Accounts and Audit (JCPAA). A request from the JCPAA was received in December 2017.

Audit objective, criteria and scope

5. The objective of the audit was to assess MIC's achievement of value for money and management of probity in its operations and procurement activities.
6. To form a conclusion against the objective, the ANAO adopted the following high-level criteria:
 - In its procurement of consultants and advisers, has MIC employed open and effective competition, demonstrably achieved value for money and managed any conflicts of interest?
 - Has MIC effectively managed and controlled the use of credit cards and reimbursement of staff expenses for official purposes?
 - Are the risks associated with accepting and providing hospitality, gifts or benefits effectively managed?

¹ Auditor-General Report No.23 of 2017–18, *Delivery of the Moorebank Intermodal Terminal*, 19 December 2017. Available from <https://www.anao.gov.au/work/performance-audit/delivery-moorebank-intermodal-terminal>

7. The evidence and data collected by the ANAO during the fieldwork phase of this audit was for the period from MIC's establishment in December 2012 to February 2018. This audit does not examine the procurement process through which MIC selected the Sydney Intermodal Terminal Alliance (SIMTA)² as its private sector delivery partner. This process was examined in the first performance audit of MIC.

Conclusion

8. It is not evident that MIC has obtained value for money in its procurement of advisers and consultants. The company's management of probity risks associated with conflicts of interest and gifts and hospitality has not been effective.

9. MIC has engaged a range of advisers and consultants to assist it to deliver on its purpose. Open and effective competition has not been a feature of MIC's procurement practices. This has contributed to the company being unable to demonstrate that value for money has been achieved through its procurement activities. Probity risks (including conflicts of interest) have not been well managed.

10. MIC has not had in place an appropriate and effective framework to manage and control the use of corporate credit cards and reimbursement of staff expenses.

11. MIC has not effectively managed the risks associated with accepting and providing hospitality, gifts or benefits. Initially this was due to the absence of relevant policies and guidance. Subsequent to the development of policies and guidance, poor compliance and ineffective governance arrangements resulted in the acceptance of offers that should have been declined under MIC's policy framework.

Supporting findings

Procurement

12. MIC has no overarching procurement strategy and was slow to develop its procurement policies and procedures. The procurement policy was documented and approved by MIC's CEO in June 2014 in response to an internal audit recommendation that it be documented. This was some 18 months after MIC was established and after the company had conducted 19 procurements with future payments totalling \$27.8 million. It was also subsequent to the development and board approval of various other corporate policies. An additional 'Selection and Management of Consultants' procedure was developed in June 2016 for procurements specifically related to the MIC Funded Works package (under the contractual arrangements with the SIMTA).

13. MIC's procurement framework does not appropriately emphasise the important role that effective competition can play in obtaining value for money. MIC's procurement framework is also internally inconsistent. Specifically, one policy requires open tender processes for procurements over \$100,000 whereas a more recent procedure prescribes a process of select tendering and is silent on the need to achieve value for money.

14. MIC has not conducted any open tender processes when procuring advisers and consultants. Rather:

- 68 per cent of procurement processes were sole source engagements worth \$11 million; and

² SIMTA was a joint venture between Qube Holdings and Aurizon from 2012 to July 2016, when Aurizon announced the sale of its shares in SIMTA to Qube. The sale took effect from 24 January 2017, leaving SIMTA a wholly owned Qube entity.

- 32 per cent involved limited competition (seeking a proposal or quote from two to 10 respondents) worth \$21 million.

15. MIC's identification and management of conflicts of interest in its procurement activities has been ineffective. Relationships (long-term business and/or personal associations) with MIC staff were often (51 per cent of the time) the preferred basis for the sole sourcing of service providers or inviting them to participate in tender processes. While relationships with service providers were disclosed between MIC employees, there was no evidence of any formal consideration of conflicts of interest. Additionally, MIC's corporate policies contain limited guidance on conflicts of interest. No definition is provided, nor are any contextual examples of conflicts of interest articulated. This situation makes it difficult for staff to identify inappropriate practices. Situations were also identified where employees had used their position to promote their external associates to Qube and to assist associates in securing employment by MIC.

16. MIC's identification of potential candidates by way of personal or business referrals combined with its extensive use of non-competitive procurement processes significantly diminished the value for money that might have otherwise been obtained. Many of MIC's procurements have been urgent, unplanned or reactive. This inherently increases the risk of paying more. It was also difficult to be assured that there was a genuine business need for a number of MIC's procurements — particularly where the original proposal was initiated by the service provider. MIC typically has not revisited or negotiated on price, even when the opportunity has presented itself.

Credit cards and staff expenses

17. Travel expenses and studies assistance are the primary areas of focus for MIC's expenses policies. MIC was timely in the development of its expenses policy (May 2013), but slow to develop its studies support policy (April 2015). There are gaps in the policy framework with work needed to adequately address expenditure by MIC on entertainment, telephones and professional memberships.

18. MIC's credit card policy provides an appropriate framework for the issue, use and cancellation of credit cards. The first version of the policy was approved in May 2013 and had undergone few changes until June 2018. The updated June 2018 policy addressed a range of deficiencies in earlier versions of the policy relating to the separation of duties and acquittal processes.

19. MIC's controls have been ineffective in assuring compliance with its policies.

Gifts and benefits

20. MIC did not have a policy or supporting gifts and benefits register until September 2014. This was approved some 21 months after MIC was established. The policy would be significantly enhanced if it explicitly identified procurement and contracting activities as a high-risk area for the acceptance of gifts and benefits. Amendments to the policy in February 2018 have weakened controls by allowing MIC's CEO to both accept and approve his or her own receipt of gifts and benefits.

21. MIC's recording of gifts and benefits has been inaccurate and incomplete. Key factors in this situation have been:

- the lag in the development of MIC's policy material, which meant that staff were not required to record such offers until late 2014;
- poor understanding of the requirements of the policy, resulting in only three items (rather than at least 63) being recorded on the register until November 2015;
- MIC's recording only of gifts and benefits that were accepted and not those refused (evidence is that few offers have been refused) prior to February 2018; and
- poor consideration of the application of the policy towards MIC board members.

22. Where records exist, MIC has accepted most offers of hospitality, gifts or benefits. From MIC's establishment to April 2018, there were at least 43 organisations that made at least 138 offers of gifts, benefits or hospitality with an estimated total value of \$20,928 to MIC's staff. Four of these organisations accounted for 56 per cent of the quantity and 65 per cent of the total value of these offers. These entities were MIC's three key advisers and Qube. MIC accepted all but eight of these offers.

23. MIC has, on occasion, provided entertainment or hospitality to its paid consultants and Qube. It has been less common for MIC to provide gifts or benefits. Since it was established, MIC has provided a total of \$56,250 in donations or sponsorships to six different entities. Two of these predated the development of MIC's policy and the remaining four were not approved in accordance with the policy.

24. MIC has not adequately considered the risks involved in providing or accepting offers of hospitality, gifts or benefits. This has resulted in the acceptance (and provision) of gifts, benefits or hospitality that, had the risks been properly considered, should have been declined.

Summary of entity responses

25. The proposed report was provided to MIC and the Department of Finance (Finance). Finance provided a summary response, set out below.

Department of Finance

Finance notes the recommendation of the Report. Finance will provide the key learnings to Government Business Enterprises and consider the key learnings when reviewing the *Commonwealth Government Business Enterprises—Governance and Oversight Guidelines*.

Recommendations

Recommendation no.1 The Moorebank Intermodal Company promptly implement the recommendations made in its June 2018 internal reviews in a way that addresses both the findings of those reviews and the findings of this ANAO performance audit.

Paragraph 4.37

Moorebank Intermodal Company response: *Agreed*

Key learnings for all Australian Government entities

26. Below is a summary of key learnings, including instances of good practice, which have been identified in this audit that may be relevant for the operations of other entities.

Governance and risk management

- For newly established entities, priority should be given to the development and approval of those policies and procedures that are essential to delivering on the organisation's purpose. For corporate government entities, the *Public Governance, Performance and Accountability Act 2013* and associated guidance provides a sound framework which can be used to develop these policies.
- When engaging consultants and advisers, entities should put in place mechanisms to ensure, where possible, competitive processes are used to maximise value for money. In addition, entities should identify and actively manage probity risks, including conflicts of interest.
- Entities should ensure that their policies include effective processes for identifying the gifts and benefits offered and/or accepted by its employees. The maintenance of a central register may assist entities in implementing these policies and meeting their accountability and

transparency obligations. These aspects would be further enhanced by the publication of entity gifts and benefits registers on the internet.

Procurement

- Obtaining value for money through open and competitive procurement processes is aided by the early development of an overarching procurement strategy, the scope of which includes the engagement of advisers and technical consultants and enables adequate planning for tender processes.
- Public disclosure of the planned scope and timeframe of procurement activities, and providing capacity for potential candidates to register their interest, assists to maximise competitive pressure in selection processes and, consequently, with achieving value for money for taxpayer funds.