



Auditor-General for Australia

**SUBMISSION No. 1**  
**Inquiry into National Funding Agreements**



8 April 2011

Mr Robert Oakeshott MP  
Chair  
Joint Committee of Public Accounts and Audit  
PO Box 6021  
Parliament House  
CANBERRA ACT 2600

Dear Mr Oakeshott

I refer to Mr Brunoro's letter of 24 February 2011, seeking submissions to the Joint Committee of Public Accounts and Audit Inquiry into National Funding Agreements. The Australian National Audit Office (ANAO) welcomes the opportunity to make a contribution to the inquiry and provides the attached submission for the Committee's consideration.

The new federal financial relations framework is still at a relatively early stage and the processes surrounding the underpinning national funding agreements are being continuously reviewed and refined at all levels. In preparing our submission, we have drawn on the findings of some of our recent audits, including: ANAO Audit Report No.33, 2009–10 *Building the Education Revolution - Primary Schools for the 21<sup>st</sup> Century*; Report No.3 2010–11, *The Establishment, Implementation and Administration of the Strategic Projects Component of the Regional and Local Community Infrastructure Program*; and Report No. 30, 2010–11, *Digital Education Revolution Program – National Secondary Schools Computer Fund*.

The ANAO submission focuses on four areas that we consider warrant particular consideration:

- agencies establishing appropriate risk-based monitoring and assurance arrangements that strike a balance between accountability and delivery responsibility, where these are not currently in place;
- better aligning the interaction of the enhanced grants administration framework and the new federal financial relations framework;
- agencies reporting to Parliament on the outcomes being achieved under the new arrangements; and
- an appropriate mandate that allows the Auditor-General to examine the operation of the arrangements (this would also be complemented by the inclusion of explicit references to access and audit powers in national funding agreements). In this regard, we note that the legislation before the Parliament proposing amendments to the *Auditor-General Act 1997* contains provisions that would form the basis for amending the mandate.

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I look forward to further discussing the ANAO's submission with the Committee.

Yours sincerely

Ian McPhee  
Auditor-General

# **Joint Committee of Public Accounts and Audit**

**Inquiry into National Funding Agreements**

**SUBMISSION**

**Australian National Audit Office**



8 April 2011

## Introduction

1. A new federal financial framework has been in place since 1 January 2009, following the signing of the Intergovernmental Agreement on Federal Financial Relations. Described as the 'most significant reform of Australia's federal relations in decades'<sup>1</sup>, the new framework is:

aimed at improving the quality and effectiveness of government services by reducing Commonwealth prescriptions on service delivery by the States, providing them with increased flexibility in the way they deliver services to the Australian people. In addition, it provides a clearer specification of roles and responsibilities of each level of government and an improved focus on accountability for better outcomes and better service delivery.<sup>2</sup>

2. As part of the Intergovernmental Agreement, the Council of Australian Governments (COAG) introduced six National Agreements in areas such as education, housing and Indigenous reform. The National Agreements outline objectives, outcomes, outputs, performance indicators and roles and responsibilities among other things. Under the framework, the Commonwealth provides three types of payments to the states and territories: National Specific Purpose Payments, which are aligned to five of the National Agreements<sup>3</sup>; National Partnership Payments (supported by National Partnership Agreements<sup>4</sup>); and general revenue assistance, such as the GST payments.

3. In supporting the change to the arrangements, the Australian Government noted that in the past, 'blurred' roles and responsibilities between levels of government, as well as duplication and overlap, had been costly aspects of Australia's federal system, particularly where they had undermined accountability through cost shifting.<sup>5</sup> The move to a new model was seen as a recognition that 'the old ways of doing things have obviously not worked'.<sup>6</sup>

4. While the changed federal financial relations landscape is still relatively new, the Australian National Audit Office (ANAO) has examined some of the arrangements through recent performance audits. The following provides some insights on the operation of the new arrangements, based on our work.

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<sup>1</sup> Commonwealth of Australia, *Budget 2009–10 (Budget Paper No.3-Part 1: Australia's Federal Relations)*, Canberra, 2009, p. 3.

<sup>2</sup> Council of Australian Governments website. Can be accessed at: [http://www.coag.gov.au/intergov\\_agreements/federal\\_financial\\_relations/index.cfm](http://www.coag.gov.au/intergov_agreements/federal_financial_relations/index.cfm).

<sup>3</sup> The National Indigenous Reform Agreement does not have a related specific purpose payment.

<sup>4</sup> National Partnership Agreements define the objectives, outputs and performance benchmarks related to the delivery of specified projects, to facilitate reforms or to reward those jurisdictions that deliver on national reforms or achieve service delivery improvements.

<sup>5</sup> Commonwealth of Australia, *Budget 2009–10*, op. cit., p. 11.

<sup>6</sup> Swan, The Hon. Wayne, MP, Treasurer of Australia, *Federalism and the Engine Room of Prosperity*: speech to the Australia and New Zealand School of Government Annual Conference, Melbourne, 11 September 2008, available from [www.treasurer.gov.au](http://www.treasurer.gov.au).

## Operation of the new arrangements

5. The Commonwealth prescribes four principles that must be met in order to promote the proper use of resources, including the expenditure of Commonwealth funds. Proper use is described as 'efficient, effective, economical and ethical use that is not inconsistent with the policies of the Commonwealth'.<sup>7</sup> By virtue of being Commonwealth expenditure, these principles extend to Commonwealth funding provided to the states and territories under national funding agreements.<sup>8</sup>

6. Historically, Commonwealth funding to the states and territories has been orientated to input controls and a compliance regime. This model imposed conditions on how Commonwealth funding could be used by the states and territories, and was considered to constrain flexibility and innovation in service delivery. It also meant that there was a greater administrative burden on all parties through the monitoring and reporting requirements.<sup>9</sup>

7. Under the new framework, the Commonwealth is directing funding to the achievement of outcomes and outputs through partnership arrangements, with the expectation that the states and territories will be afforded a greater degree of flexibility in determining how to deliver the outcomes and outputs. Under such an approach, traditional accountability mechanisms need to evolve as a shift to outcomes measurement requires performance indicators that link directly to outcomes, and a greater focus on the capture of robust and timely performance data. Further, given the nature of national funding agreements and multi-jurisdictional arrangements, the success of the new arrangements also relies on all parties reaching a common understanding of not only roles and responsibilities, but also issues such as how value-for-money will be determined. In this context, Commonwealth agencies need to establish arrangements that balance the respective roles envisaged under the new framework, with the need for agencies to have access to sufficient information to allow an assessment of the principles underpinning the proper use of Commonwealth resources.

8. Often, an Australian Government agency will be the principal or lead agency for a program under a national funding agreement. There are two key aspects in developing the underpinning arrangements that bear on the accountability of the lead agency:

- There should be a clear understanding of the responsibilities of the various parties, with the lead agency carrying the responsibility for assessing the risks to successful performance by its partner agencies or other parties. This recognises that, if one of the partners fails to deliver, the risk will almost certainly be carried by the Australian Government in some manner.

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<sup>7</sup> *Financial Management and Accountability Act 1997*, subsection 44(3).

<sup>8</sup> In this submission 'national funding agreements' is used as a generic term for any payments made by the Commonwealth to the states and territories that extend from the new federal financial relations framework.

<sup>9</sup> Swan, The Hon. Wayne, MP, Treasurer of Australia, loc. cit.

- The lead agency should maintain a clear focus on the arrangements in place to assess the value-for-money being achieved from the Australian Government funds and identify opportunities to enhance performance.<sup>10</sup>

9. An added practical complexity of the new arrangements is that the policy position underpinning a program may override the general approach outlined in the framework. For example, the Building the Education Revolution – Primary Schools for the 21st Century program was one measure, adopted by the Commonwealth, to stimulate the economy in response to the global financial crisis. In this case, the Australian Government determined that a more prescriptive approach was required and consequently, tighter input controls and more prescriptive guidelines were established. This contrasts with other programs in the same policy area, such as the Digital Education Revolution – National Secondary Schools Computer Fund, where a greater emphasis has been given to the partnership and outcomes approach envisaged under the new framework. In practice, the ANAO has observed a general, but not universal, move by the Commonwealth to focus on the achievement of outcomes and outputs, with less prescription on how these are to be achieved.<sup>11</sup>

10. The new arrangements provide for this flexibility in approach, however, they can also make it difficult to determine the clear lines of accountability proposed by the framework. The Chairman of the COAG Reform Council<sup>12</sup> has noted ‘my sense of this is that there have been some good first steps, but that the extent to which roles have been clarified is variable across the different parts of the agenda’.<sup>13</sup> The ANAO has also noted this variability and its impact on governance structures (roles, responsibilities and accountabilities). This has resulted in a range of implementation challenges for the Commonwealth including:

- different approaches within the same program being adopted across jurisdictions, making it difficult to compare performance and understand the overall progress being made towards the desired outcomes<sup>14</sup>; and
- instances where Commonwealth officials have assumed key jurisdiction-based management and implementation positions.<sup>15</sup> Such arrangements have the potential to blur, rather than clarify, the responsibilities.

11. The framework outlined by the Intergovernmental Agreement has established a new model for Commonwealth, state and territory arrangements. However, as mentioned above, there will always be some situations where governments, through the policy parameters established, decide to depart from the general model. It is important in all circumstances, but particularly these situations, that the risks and consequences are

<sup>10</sup> McPhee, Ian, PSM, Auditor-General for Australia, *Public Sector Accountability*: speech to the CPA Australia International Public Sector Convention, Melbourne, 11 March 2011, available from [www.anao.gov.au/Publications/Speeches](http://www.anao.gov.au/Publications/Speeches).

<sup>11</sup> *ibid.*

<sup>12</sup> Refer paragraph 20.

<sup>13</sup> McClintock, Paul, AO, Chairman, COAG Reform Council, *Renewing the mandate: COAG and its reform agenda in 2011*: speech to CEDA, Sydney, 9 February 2011, available from [www.coagreformcouncil.gov.au/media/index.cfm#speeches](http://www.coagreformcouncil.gov.au/media/index.cfm#speeches).

<sup>14</sup> For example, the Building the Education Revolution Implementation Taskforce concluded in its interim report that ‘in practice the different education authorities have applied the Commonwealth BER Program Guidelines differently’. *Building the Education Revolution Implementation Taskforce: Interim Report*, 6 August 2010, p. 37.

<sup>15</sup> For example, Commonwealth officials involved in the Northern Territory component of the National Partnership Agreement on Remote Indigenous Housing.

commonly understood and, at the Commonwealth level, the relevant agencies put in place administrative arrangements that appropriately mitigate significant risks. The COAG Reform Council also has a role to play in this area through highlighting to COAG the impact of any arrangements that depart from the general model.

### ***Interaction of the federal financial relations framework with the enhanced grants administration framework***

12. As of 1 July 2009, a new policy framework was introduced for the administration of grant programs by agencies subject to the *Financial Management and Accountability Act 1997*. In addition to defining a grant, the *Financial Management and Accountability Regulations 1997* (the FMA Regulations) stipulate a number of arrangements that are taken not to be grants and to which, therefore, the Commonwealth Grant Guidelines do not apply. In this context, a payment to a state or territory that is made for the purposes of the *Federal Financial Relations Act 2009*, including general revenue assistance, other general revenue assistance, National Specific Purpose Payments and National Partnership Payments, is defined as not being a grant to which the enhanced grants administration framework applies.

13. Where the Commonwealth is providing funding for the achievement of broad outcomes, excluding payments subject to the *Federal Financial Relations Act 2009* from the enhanced grants administration framework does not cause any difficulties. However, it is not uncommon for state and territory governments to apply for grant funding from the Commonwealth for specific projects or activities, along with local governments and/or private sector bodies and community organisations. This can lead to complex administrative arrangements whereby any grants awarded to state and territory governments may be subject to governance arrangements that are different to those applying to grants awarded, under the same program, to other types of applicants.<sup>16</sup>

14. Other inconsistencies in approach can also arise. For example, a funding agreement might be signed with an intermediary in respect to a project actually being delivered by a state government, rather than a National Partnership Agreement being negotiated with the state.<sup>17</sup> In addition, the time required to negotiate a National Partnership Agreement with the various states and territories, rather than signing a standardised funding agreement, can present challenges to the achievement of intended outcomes.<sup>18</sup>

15. Accordingly, there could be benefit in the Department of Finance and Deregulation considering and, as appropriate, advising the Finance Minister, on the merits of re-examining the interaction of the new grants framework and the types of grant payments to states and territories made through mechanisms established under the *Federal Financial*

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<sup>16</sup> For example, the National Partnership Agreement to Support Local Government and Regional Development provides a framework under which individual projects will be delivered for certain programs. The individual project details (including the budget, milestones and reporting requirements) are to be outlined in Implementation Plans under the Agreement. To date, three such Implementation Plans have been approved. Other funding recipients under the relevant program have been required to sign a funding agreement.

<sup>17</sup> ANAO Audit Report No. 3 2010–11, *The Establishment, Implementation and Administration of the Strategic Projects Component of the Regional and Local Community Infrastructure Program*, p. 208. In that example, in addition to the funding agreement with the local government funding recipient, a deed was also signed between the Commonwealth and the state government entity outlining how the state would perform the development envisaged by the funding agreement.

<sup>18</sup> This has been the case, for example, in respect to the provision of economic stimulus through state-delivered projects.

*Relations Act 2009*.<sup>19</sup> Improving the interaction of the two frameworks would also assist to achieve greater commonality in the treatment of similar payments.

## Performance reporting

16. Within the new arrangements comes an implicit value-for-money proposition. That is, in defining the agreed outcomes and outputs, there is an expectation that value-for-money will be achieved in their delivery. The model recognises that the 'appropriate government is accountable to its community'<sup>20</sup>, however, this can be complicated when the relative funding contributions by the Commonwealth, states and territories are different to their respective responsibilities for delivering the outcomes. While often removed from the direct delivery of outcomes, the challenge for the Commonwealth (which in many cases is at least an equal if not dominant provider of funding) is how to satisfy itself that the principles underpinning the use of Commonwealth resources are being adhered to, and value-for-money outcomes are being achieved.

17. The Building the Education Revolution – Primary Schools for the 21st Century program is one such example of this. While the Commonwealth was the sole funder of the program<sup>21</sup>, education authorities within each state and territory jurisdiction were responsible for service delivery, which included achieving value-for-money for the buildings constructed in each school under the program. Despite this arrangement, publicly, the Commonwealth was still seen as having a central accountability role for the program. The absence of consideration and agreement on how value-for-money would be determined during the National Partnership Agreement negotiation phase, meant that the lead Australian Government agency developed program administration arrangements that did not provide it with sufficient information to effectively advise on the matter. This view was supported by the Building the Education Revolution Implementation Taskforce, which found that the reporting and monitoring arrangements for the Building the Education Revolution – Primary Schools for the 21st Century program did 'not provide visibility over value-for-money'.<sup>22</sup>

18. Under the new arrangements there are two primary mechanisms that the Parliament can use to gain an understanding of the operation of national funding agreements and, particularly, the progress being made towards achieving the agreed outcomes. These are reporting to the Parliament through publications such as portfolio budget statements and annual reports, and the information gathered and reported by the COAG Reform Council.

19. Reporting requirements for portfolio budget statements and National Partnership Agreements do not intersect as their focus can often be different. There is also currently no guidance for agencies on how to assess and report in portfolio budget statements or annual reports on the performance of programs funded under National Partnership Agreements.

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<sup>19</sup> A similar suggestion was made by the ANAO in Audit Report No. 30 2009–10, *Management of the Strategic Regional Program/Off-Network Program*. The ANAO understands that Finance's work in this area has not yet been completed.

<sup>20</sup> Intergovernmental Agreement on Federal Financial Relations, section 14, 1 January 2009, available from [www.coag.gov.au/intergov\\_agreements/federal\\_financial\\_relations/index.cfm](http://www.coag.gov.au/intergov_agreements/federal_financial_relations/index.cfm).

<sup>21</sup> Education authorities were able to supplement Commonwealth funding to deliver more substantial projects.

<sup>22</sup> *Building the Education Revolution Implementation Taskforce: Interim Report*, 6 August 2010, p. 41.

While the funding provided for National Partnership Agreements is included in Treasury's Portfolio Budget Statements, with a link to the relevant agency's program, there is variability in whether agencies include performance indicators for those programs in their own publications. As such, reporting is often either at a very high level or, in some cases, is non-existent.

20. The COAG Reform Council is the key accountability body for the COAG reform agenda. The Intergovernmental Agreement outlines that the 'COAG Reform Council will report to the Prime Minister, as chair of COAG, on National Agreements and National Partnerships'.<sup>23</sup> As part of the role, the COAG Reform Council monitors, assesses and publicly reports on the performance of the Commonwealth and states and territories in achieving the outcomes and performance benchmarks specified in the six National Agreements. The COAG Reform Council is accountable to COAG and not the Australian Parliament. Nevertheless, the information gathered and reported by the Council, particularly through their annual reports on National Agreements, can provide insights for the Parliament on the overall progress towards outcomes under national funding agreements.

21. The Chairman of the COAG Reform Council has noted that while progress is being made with performance reporting there remain issues with the availability of adequate and timely data, which in turn impacts on the Council's ability to monitor and report on performance and changes over time.<sup>24</sup> Recently, the Council Chairman noted 'all our reports contain recommendations to improve the data quality of the areas being monitored, and call for refinement of the linkages between the data being assessed and the policy objectives sought'.<sup>25</sup> Further, the Council has found that all National Agreements have examples of performance indicators which have no data or inadequate data to report on progress.<sup>26</sup>

22. The impact of limited reporting by Commonwealth agencies and the data quality issues being encountered by the COAG Reform Council have flow-on effects for the Parliament in being able to discharge its responsibilities. Without clear, adequate and consistent reporting against meaningful performance measures, the Parliament is constrained in its ability to understand and assess how Commonwealth funding is contributing to the achievement of value-for-money outcomes in areas covered by national funding agreements. In this respect, in its recent report on the *Primary Schools for the Twenty First Century Program* (P21 program), the majority view of the References Committee of the Senate Education, Employment and Workplace Relations was that the 'inability to access sufficient information to properly scrutinise the P21 program is indicative

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<sup>23</sup> Intergovernmental Agreement on Federal Financial Relations, section 18, 1 January 2009, available from [www.coag.gov.au/intergov\\_agreements/federal\\_financial\\_relations/index.cfm](http://www.coag.gov.au/intergov_agreements/federal_financial_relations/index.cfm).

<sup>24</sup> McClintock, Paul, AO, Chairman, COAG Reform Council, *Statistics, public accountability and the federation*: speech to the NatStats Conference, Sydney, 16 September 2010, available from [www.coagreformcouncil.gov.au/media/index.cfm#speeches](http://www.coagreformcouncil.gov.au/media/index.cfm#speeches).

<sup>25</sup> McClintock, Paul, AO, speech, 9 February 2011, loc. cit.

<sup>26</sup> McClintock, Paul, AO, speech, 16 September 2010, loc. cit.

of broader accountability gaps associated with the granting of Commonwealth funding under partnership agreements'.<sup>27</sup>

## Role of the Auditor-General

23. The Auditor-General plays a unique role in providing an independent assurance to the Parliament on the efficiency and effectiveness of the administration of Australian Government programs and entities. As recognised by the Joint Committee of Public Accounts and Audit in Report 419, *Inquiry into the Auditor-General Act 1997*, the assurance role of the Auditor-General is an important consideration under the new arrangements. However, there exist barriers to the Auditor-General being able to carry out this role and help inform the Parliament on the operation and outcomes of the new arrangements.

24. While progress has been made to include explicit references to the access powers of the Auditor-General as part of bilateral agreements under National Partnership Agreements, it is not a requirement and may be subject to negotiation during the course of establishing the agreements.<sup>28</sup> Further, even if access powers are explicitly provided for in agreements, this does not overcome the current limitations of the mandate of the Auditor-General under the *Auditor-General Act 1997*, with regard to the ability to undertake an assessment of how Commonwealth resources are ultimately used. This limitation, combined with the issues encountered with the application and reporting of the new framework, highlights the importance of the 'follow the money' provisions proposed in the *Auditor-General Amendment Bill 2011*, which is currently before the Parliament.

25. Extending the power of the Auditor-General to follow the money is not unprecedented in Australia. Both the Victorian and the Tasmanian Auditors-General have the power to examine the use of grant funding by third-party recipients. Also, a recent inquiry by the Queensland Public Accounts and Public Works Committee into the Queensland Audit Office recommended that, similar to the arrangements in Western Australia and Tasmania, the Queensland Auditor-General have the power to investigate any matter relating to 'public money, other money or statutory authority money to public property or other property'.<sup>29</sup> These individual state and territory arrangements, however, are aimed at their respective jurisdictional arrangements and cannot be expected to provide sufficient information to the Australian Parliament on the Commonwealth's role and the outcomes being achieved (including value-for-money considerations).

26. Given the multi-jurisdictional nature of the national funding agreements, the ANAO is well placed to examine arrangements across jurisdictions and provide Parliament with information on the performance of Australian Government agencies and the expenditure of Commonwealth funds. While respecting the different legislative mandates of

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<sup>27</sup> Senate Education, Employment and Workplace Relations References Committee, *Primary Schools for the Twenty First Century Program*, Canberra, March 2011, p. 9. ref 2.22.

<sup>28</sup> Joint Committee of Public Accounts and Audit, *Report 419 Inquiry into the Auditor-General Act 1997*, Canberra, December 2010.

<sup>29</sup> Legislative Assembly of Queensland, Public Accounts and Public Works Committee, *Inquiry to formally review the 'Report of the 2010 Strategic Review of the Queensland Audit Office'; to consider the recommendations made and comment on other findings where appropriate*, Report No. 7, March 2011, p. viii.

Auditors-General, as part of this arrangement, the work of the offices in this area could also be assisted by the judicious sharing of certain information where permitted and relevant.

27. The ability of the Auditor-General to undertake audit work in this area should not be seen as either duplicating or diminishing the responsibility of agencies or the COAG Reform Council. Agencies should still be expected to appropriately report on performance and outcomes from national funding agreements through existing accountability structures such as portfolio budget statements and annual reports. Further, the COAG Reform Council has its important role to report to COAG on the operation of the arrangements and the progress being made towards meeting the COAG agenda.

## Conclusion

28. The measurement and assessment of performance against program objectives sits at the heart of public administration accountability. The Joint Committee of Public Accounts and Audit has noted that 'measuring key aspects of an agency's performance is a critical part of the Government's Outcomes Framework'.<sup>30</sup> While the nature of the partnership arrangements under national funding agreements means that there is a broad range of factors that can contribute to the achievement of value-for-money outcomes, the Parliament should have access to clear and reliable information that provides insights to the success or otherwise of the programs funded under these agreements.

29. The new federal financial framework and underpinning national funding agreements provide a model to facilitate the relationship between Commonwealth, state and territory governments in the delivery of outcomes and services. It will be important that in due course these arrangements be reviewed and compared against the expectations so as to determine whether the anticipated benefits are being realised. Ultimately, the success of the arrangements will rely on all parties being able to practically adopt the changes envisaged when the new framework was agreed. In this context, from the Commonwealth perspective, the current arrangements for national funding agreements could be improved by:

- agencies establishing appropriate risk-based monitoring and assurance arrangements, which strike a balance between accountability and delivery responsibility, where these are not currently in place;
- better aligning the interaction of the enhanced grants administration framework and the new federal financial relations framework so that there is no diminution in the accountability and governance arrangements adopted for grants awarded to state and territory governments;
- agencies being required to provide clear and consistent reporting to Parliament on the outcomes being achieved under national funding agreements; and
- the Auditor-General being provided with an appropriate mandate that allows the operation of the arrangements to be examined (this would also entail the inclusion

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<sup>30</sup> In this area, the JCPAA has recommended that the *Auditor-General Act 1997* be amended to: 'enable the Auditor-General to review an agency's compliance with its responsibilities for a sub-set of performance indicators' to provide 'assurance around the integrity of performance information attached to programs or areas the Parliament sees as a priority'. Joint Committee of Public Accounts and Audit, Report 419, *Inquiry into the Auditor-General Act 1997*, December 2010, p. 20.

of explicit references to access and audit powers in national funding agreements). In this regard, it is noted that the legislation before the Parliament proposing amendments to the *Auditor-General Act 1997* contains provisions that would form the basis for amending the mandate.