

HC Coombs Policy Forum

## Background paper

# Commonwealth financial accountability

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Background paper provided by Stein Helgeby, Department of Finance and Deregulation

## Introduction

The Commonwealth's financial framework provides overarching rules for the financial activities of the Australian Government. It takes into account requirements contained in the Australian Constitution, and its legislative dimensions can be seen as an agreement between the Parliament and the Government on the Commonwealth's use of public resources.

The financial framework needs to support high quality financial management, including by shaping the behaviour of users, being simple to understand and providing appropriate transparency. It also needs to be flexible to meet the operational requirements of Government now, and into the future.

The Minister for Finance and Deregulation has announced a review of the financial accountability arrangements for the Commonwealth as part of a broad agenda for Better Government. The agenda covers a range of activities to improve delivery of Government services, policies and programs and upgrade the public management framework generally. The Finance Minister notes that "only by ensuring the legislative foundations are sound, will the other reform areas be successful".<sup>1</sup>

The Commonwealth Financial Accountability Review (CFAR) is fundamentally considering the requirements of a contemporary and flexible financial framework. CFAR's aim is to develop the framework so that: it comprehensively addresses the needs of modern government; improves governance practices and risk management; has the flexibility to cover diversity in government operations and accommodate future changes; and is user-friendly to support accountability and compliance.

## Changes in Australian Government Operations

The Australian Government is a significant operating entity. In 2009-10, it spent \$334.8 billion<sup>2</sup>, employed 243,700 people<sup>3</sup>, and conducted operations not only across Australia, but across the globe. People outside the Government typically see it as one entity; however, it is actually a complex collection of structures, finances and people. For example, the Australian Government encompasses some 932 bodies and governance relationships (as at 1 October 2009), including departments of state, government agencies, individual office holders, companies and joint ventures.

Citizens expect the Government to act in a coordinated way, despite its diversity. They expect more streamlined and simpler interactions with Government. Citizens also expect the Government to respond to increasingly complex issues efficiently and effectively. Governments are therefore seeking greater flexibility to address these issues and meet citizens' expectations. The different levels of government in Australia are more joined up than they were a generation ago, pooling their efforts and resources on various initiatives. The Commonwealth has also increased its partnership with other parties, including commercial partners and the third sector.

These trends, together with new technologies like the internet, have changed the delivery of services and goods from government to the community. For example, nearly two-thirds of those who contacted Government in 2009 used the

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<sup>1</sup> Finance Minister's speech to the CAC Act Forum, 8 December 2010.

<sup>2</sup> Commonwealth Government expenditure (sum of GGS, PNFC and PFC expenditure) in 2009-10 (taken from Consolidated Financial Statements for the year ended 30 June 2010 p. 33)

<sup>3</sup> ABS, Employment and Earnings, Public Sector, Australia, 2009-10

internet to do so on at least one occasion (up from 39 per cent in 2004-05).<sup>4</sup> New technology has also changed systems to manage budgeting, reporting, banking and payment arrangements (like debit cards) in the Commonwealth. More changes to Government operations are likely in the coming years, with new technologies improving processes and further increasing expectations of Government.

Much of the thinking behind the current financial framework is nearly 20 years old. There have been a number of major changes in Government operations since the commencement of the framework in 1998. For example, significant budgeting and reporting reforms were introduced in 1999 and funding arrangements between the Commonwealth and the States and territories were fundamentally redesigned under the *Federal Financial Relations Act 2009*.

The *Financial Management and Accountability Act 1997* (FMA Act) and the *Commonwealth Authorities and Companies Act 1997* (CAC Act) are the key legislation for the current financial framework.<sup>5</sup> The Acts contain many robust and valuable provisions, and they have provided a framework for Government that in many ways continues to be leading edge. Both the FMA Act and CAC Act have been regularly updated, but in their essential content and structure, they remain largely unchanged.

Since the Acts were passed, expectations about the transparency of Government operations have increased. Government decisions are regularly scrutinised by the Parliament as well as those outside the Commonwealth, such as the media, academia, special interest groups and individual citizens. They judge whether it performs effectively, uses resources efficiently and economically, and operates to appropriate ethical standards. The financial framework needs to be able to stand up to this scrutiny based on today's standards.

While regular changes have been made to update the Commonwealth's financial framework, it has not been reviewed fundamentally in over a decade. Since the 1990s, various other jurisdictions have modernised their financial frameworks and there have been developments in private sector governance.<sup>6</sup> Some consider that Australia is falling behind in terms of reform: "As a pioneer, Australia pushed ahead with budgetary reforms, at times at breakneck speed. But of late, Australia's momentum has waned, and its enthusiasm for carrying through the reforms to deliver more meaningful performance information has diminished..."<sup>7</sup>

## Supporting Collaboration

An evolving challenge for effective government administration and service delivery is the growing trend in Government for more joined-up operations. This includes partnership with state and territories and other parties, such as commercial partners and the third sector. However, it also involves entities within Government working more collaboratively to achieve whole-of-government priorities. To be effective, Government needs to be able to look beyond the traditional stovepipe models. Achieving effective delivery and governance in these circumstances is difficult.

While the financial framework is structured around individual agencies, it does not prevent agencies working collaboratively to achieve whole-of-government outcomes. However, mechanisms for supporting whole-of-government operations and cross-agency activities are not explicit. While this does not preclude collaboration, it can hinder it. In particular, there can be concerns around accountability for shared activities. Collaboration can also be hindered by engrained cultures/behaviours such as people focussing solely on their entity and themselves.

Experience indicates that the key drivers for effectively implementing joined up initiatives include:

- > Strong leadership to maintain strategic focus and momentum to achieve objectives
- > Defined responsibility and accountability for specific objectives, including reporting and funding arrangements
- > Flexibility and willingness to reprioritise to meet overarching goals, balanced against the need to meet individual agency priorities.

The financial framework can be made to provide better support for the successful implementation of joined-up activities. Doing so would build on the success of established working arrangements such as in the areas of border protection and indigenous disadvantage.

<sup>4</sup> Department of Finance and Deregulation, *Interacting with Government 2009*, December 2009, p24

<sup>5</sup> Further details on the FMA Act and CAC Act are provided in Attachment A

<sup>6</sup> Attachment B provides further details on reforms in other jurisdictions and sectors.

<sup>7</sup> Hawke, L. & Wanna, J. "Australia after budgetary reform: a lapsed pioneer or decorative architect", in *The Reality of Budgetary Reforms in OECD Nations*, Wanna, Jensen and de Vries (eds.), (2010), p. 65

## Attachment A: The Current Arrangements – FMA Act and CAC Act

The key laws of the financial framework are the *Financial Management and Accountability Act 1997* (FMA Act) and the *Commonwealth Authorities and Companies Act 1997* (CAC Act). These Acts, together with the *Auditor-General Act 1997*, commenced in 1998,<sup>8</sup> replacing the *Audit Act 1901* (which was seen as “unable to accommodate the demands of modern public sector management”).<sup>9</sup> The three Acts work alongside the enabling Acts for numerous statutory bodies, and with annual and special appropriations. In short:

- > The FMA Act regulates public money and public property, applying to agencies that are financially part of the Commonwealth. It is based on an executive management structure, with a chief executive at an agency's apex, and covers entities such as Departments, regulators and various service providers.
- > The CAC Act regulates bodies corporate that are financially separate from the Commonwealth. It is based on a board of directors (with directors' duties applying) at the apex of an organisation, covering Commonwealth authorities and Commonwealth controlled companies (including government business enterprises).
- > The Auditor General Act establishes the independence of the Auditor General and the Australian National Audit Office (ANAO), enabling the Auditor General to conduct comprehensive financial statements and performance audits of Commonwealth entities.<sup>10</sup>

The FMA and CAC Acts were partly developed to reduce overly-prescriptive financial governance rules for Commonwealth entities. This was to let managers better deliver efficient outcomes in a principles-based framework<sup>11</sup>, a model that has since been followed in other jurisdictions. To allow decision-making in a consistent framework, the Acts placed various obligations on chief executives and directors for managing public resources. However, the reality has involved a mixture of requirements, some principles-based and others rules-bound or highly prescriptive.

This is not to deny the significant reforms brought about by the Acts. For example, the FMA brought clarity to the responsibilities of Chief Executives for the financial performance of their agencies, and the CAC Act helped achieve contemporary best practice in officers' duties through a single law, rather than through amending individual enabling Acts and company constitutions.<sup>12</sup>

## Attachment B: Reforms in Other Jurisdictions and Sectors

In 2004, New Zealand significantly amended its *Public Finance Act 1989*, being the first major change to its public management system in a decade, to improve performance and integration across New Zealand's public sector.<sup>13</sup>

In 2006, Canada introduced the *Federal Accountability Act* and Action Plan to improve accountability and transparency, including for procurement, auditing and accountability within departments. These changes sought to balance oversight with flexibility, while streamlining management policies.

Domestically, State governments have worked on their financial frameworks. In 2009, the Queensland Treasury decided the *Financial Administration and Audit Act 1977 (QLD)* was overly prescriptive and, in cases, did not allow sufficient flexibility for effective management. Western Australia and Victoria have undertaken similar activities to modernise their frameworks.

There have also been significant developments in private sector governance, including the Council of the Australian Stock Exchange's (ASX) *Corporate Governance Principles and Recommendations* (2003) and *Good governance principles* by Standards Australia (2003).

The private sector recognises the need to periodically review corporate governance practices to ensure they continue to reflect local and international developments and promote high standards of transparency.<sup>14</sup> The ASX Board annually reviews its own corporate governance codes, policies and charters “to ensure practices are in place to encourage the growth of shareholder value, while making certain ASX's market activities are properly managed and overseen”.<sup>15</sup>

8 These Acts were developed after the Joint Committee of Public Accounts (JCPA) Report 296, *The Auditor-General: Ally of the people and Parliament*, para 18.24 recommended in 1989 that the *Audit Act 1901* be repealed, and be replaced by two new laws, a *Financial Administration Act* and an *Audit Act*.

9 JCPA Report 331, *An Advisory Report on the Financial Management and Accountability Bill 1994, the Commonwealth Authorities and Companies Bill 1994 and the Auditor-General Bill 1994, and on a Proposal to Establish an Audit Committee of Parliament*, 2004, p. 5.

10 Under sections 16 and 17 of the *Auditor-General Act 1997* there are limitations on the circumstances where a performance audit may occur for a Government Business Enterprise.

11 Management Advisory Board, *Beyond Bean Counting*, December 1997: “The performance culture is one in which line managers are held directly accountable for financial and operational performance”, p. 2.

12 JCPA Report 331, *Chairman's Foreword*.

13 New Zealand Treasury, *A Guide to the Public Finance Act*, August 2005, pg 1

14 ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations with 2010 Amendments*, 2010, p.4.

15 ASX, *ASX Limited 2010 Annual Report*, 2010, p.43