



PARLIAMENT OF WESTERN AUSTRALIA

THIRTEENTH REPORT

OF THE

**STANDING COMMITTEE ON ESTIMATES
AND FINANCIAL OPERATIONS**

IN RELATION TO

**FINANCIAL ADMINISTRATION AND AUDIT LEGISLATION
IN AUSTRALIA AND NEW ZEALAND: IMPLICATIONS FOR
WESTERN AUSTRALIA**

Presented by the Hon Murray Montgomery (Chairman)

STANDING COMMITTEE ON ESTIMATES AND FINANCIAL OPERATIONS

The Standing Committee was established on December 21 1989 with the following terms of reference:

1. There is hereby appointed a Standing Committee to be known as the *Estimates and Financial Operations Committee*.
2. The committee consists of 5 members.
3. The functions of the Committee are to consider and report on:
 - (a) the estimates of expenditure laid before the Council each year; and
 - (b) any matter relating to the financial administration of the State.
4. The Committee shall report on the estimates referred under clause 3 by or within one sitting day of the day on which the second reading of the *Appropriation (Consolidated Revenue Fund) Bill* is moved.
5. For the purposes of clause 3(a), the House may appoint not more than 6 members at any stage of its examination.
6. A reference in clause 3 to "estimates of expenditure" includes continuing appropriations, however expressed, that do not require annual appropriations.
7. The Committee may initiate investigations under clause 3(b) without prejudice to the right of the Council to refer any such matter.

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1. OVERVIEW

During the past decade, governments in a number of jurisdictions have re-evaluated the role and structure of the public sector. Public sectors at state and national level in a number of industrialised countries have subsequently undertaken a series of similar and significant reforms. In essence, the reforms direct the administrative effort to focus on outputs and outcomes, as opposed to traditional public sector concern with inputs and processes. This outputs orientation has provided for alternatives to traditional inhouse delivery, including contracting out of public services, corporatisation of government agencies, internal benchmarking and contestability, and privatisation. These reforms represent the most fundamental changes to public sector administration since the introduction of bureaucratic discipline early this century.

Such fundamental organisational change has ramifications for the financial management structures and processes which underpin the administration of public resources. Indeed, a number of jurisdictions in Australia and New Zealand have either recently or are currently reviewing their financial administration and audit frameworks in the context of prevailing public administration trends. While respective Western Australian governments have also demonstrated initiative in implementing such reforms, particularly the programme management initiative of recent years, it remains that the existing public sector financial administration structure in Western Australia is predicated on the traditional internal provision of public goods and services. The Committee is of the opinion that the concurrent reform of public financial administration is central to the success of public sector reform and believes that the state would benefit from a comprehensive review of the current framework.

To this end, the Committee has reviewed financial administration frameworks in jurisdictions in Australia and New Zealand that represent different stages of progress in implementing public sector reform. The Committee noted a number of common areas of change addressed by different jurisdictions. These areas guide the structure of this paper. The paper is not intended as a definitive statement of the direction and content of future financial administration legislation in this state, nor does it presume to provide an exhaustive critique of the issues that might be addressed by legislative review. Rather, the paper addresses broad issues that illustrate the impact of prevailing public sector reforms on the financial administration structure. The Committee hopes that the paper will stimulate discussion regarding reform of the state's existing legislative framework, and intends to meet with interested parties in both the public and private spheres to facilitate this discussion.

2. BACKGROUND

2.1 PUBLIC SECTOR REFORM

The Committee's review is predicated on the assumption that organisational support functions, such as personnel management and financial administration, must be appropriately structured to meet an organisation's needs. In the case of financial administration, an absence of "fit" may result in an organisation either being tied down by inappropriately bureaucratic controls, or having inadequate mechanisms to account for expenditure. Changes in the public sector over this century provide an important background to understanding the public sector's current financial administration needs.

The Public Sector in the 20th Century

The method of organisational control that has dominated both public and private sector administration during the latter part of this century is the bureaucratic model developed by the German sociologist Max Weber (Weber, 1947). Together with technical forms of control, the model provided the basis for the giant industrial and public bureaucracies that developed during the period of post-war growth in western capitalist countries (Hoggett, 1991). Weber patterned the model at the turn of the century after the vaunted Prussian army, using principles of rationality and efficiency, and held that four factors - division of labour; hierarchy of authority; a framework of rules; and administrative impersonality (Kreitner and Kinicki, 1989) - would contribute to organisational efficiency.

Such mechanised systems are, by nature and intent, resistant to change. The large, slow-moving bureaucracies that developed in the post-war period proved unable to respond and adapt quickly as the pace of political, economic, market, and technological change increased in the 1970s (Hoggett, 1991). The inadequacy of the bureaucratic model was particularly visible in the public sector, which faced dual pressures to both reduce national debt and service an increasingly complex political environment (Marsh, 1994). By the late 1980s, a distinctive new form of public sector administrative control had begun to emerge in a number of western industrialised jurisdictions, including the United Kingdom, the United States, Canada, and New Zealand. These reforms have been variously titled "entrepreneurial government", "government by the market", "the contract state", and "post-bureaucratic", and are seen to represent a new phase in the organisation and management of the public sector.

"Post-Bureaucracy"

While Weber's bureaucratic reforms focussed on internal procedures, contemporary public sector reforms focus outwards, on the role of government and the purpose and performance of the public sector. The question of how much can be produced, how well, and at what cost has become more central to the public administration equation than the traditional concern with how public expenditure is controlled.

The implications of this redirected focus have been three-fold. First, work is organised on the basis of outputs as opposed to the traditional vertical integration of various functions within one department. Data processing operations, for example, may be treated as a separate entity and cost-centre. Second, the traditional vertical chain of command is decentralised. The separate identification of output areas provides for decentralised control to middle management by specifying the outputs to be produced and allowing management autonomy over the means of production. Separate identification also facilitates further forms of decentralisation, including contestability, contracting out of services, and privatisation. However, while responsibility for operational activities is decentralised to middle management or sub-contractors, policy control tends to remain with (a vastly reduced) head office (Hoggett, 1991). The creation of a "training market" through the decentralisation of operational control to TAFE colleges and the concurrent nationalisation of post-compulsory training curricula is an example of this policy-provider split.

The third feature of the post-bureaucratic model is the use of contracts. The separation of policy and operational functions requires the relationship between these two areas to be specified and controlled, most often through performance agreements or contracts that specify the outputs to be produced and the criteria by which they will be measured. These formal agreements replace the traditional bureaucratic framework of rules governing inputs and procedures as a means of control. The policy centre, or public "purchaser" of operational services, specifies desired results and performance targets, and develops frameworks for monitoring and evaluation (Hoggett, 1991). The service "providers", whether they are internal operational divisions or external sub-contractors, are, to varying extents, free to manage budgets, allocate staff, and determine how to provide the services required.

The above changes have been implemented to varying degrees in the Western Australian public sector, most notably in the Health and Transport ministerial portfolios. They also reflect the essence of the United Kingdom's "Next Steps" reforms, the principles of "reinventing government" in the United States, the massive public sector reform programme undertaken by New Zealand in the 1980s, and the recent changes implemented by the Kennett government in Victoria (See Alford and O'Neill, 1994; Boston *et. al.*, 1991; Jenkins *et. al.*, 1987; and Osborne and Gaebler, 1992).

Benefits and Risks of Contemporary Public Sector Reforms

The claimed economic benefits of the post-bureaucratic model are impressive. The Western Australian Commission to Review Public Sector Finances (McCarrey, 1993) cites the following savings:

- In 1989, the Business Council of Australia reviewed empirical evidence of cost savings from competitive tendering various functions and concluded that efficiency could be improved by 20% with no loss in quality, even if the winning tender came from the public sector.
- Studies of the benefits of competitive tendering in the United States throughout the 1970s and 1980s have revealed cost savings averaging between 30% and 40%.

- Quantitative analysis in the late 1980s of a sample of 2000 hospitals in the United Kingdom has shown that competitive tendering and contracting reduced the cost of domestic services by an average of 30%.
- A range of independent studies have confirmed cost savings from competitive tendering and contracting averaging 20% across the government sector.

The McCarrey Commission estimated that savings in excess of \$300m per year could be realised through competitive tendering in the Western Australian public sector. In his circular to Ministers (Court; 1993), the Premier adds to these efficiency claims a) improved accountability, b) improved quality, and c) increased economic development.

Certainly, such claims are not infeasible. Improved accountability may be realised out of the transparency of the contract process. Clear contractual links between purchasers and providers, output-based organisational structures, cost centres, and interagency charging can also improve accountability by linking costs to outputs. Specifying outcomes and outputs as the means of organisational control, particularly where this also involves identification of client preferences, can assist in improving the quality of goods and services. Opening up the provision of public goods and services to the private sector may enable the government to benefit from lower cost structures, new technologies, and skills, thereby facilitating the delivery of public services or the development of infrastructure that might previously have not been available. Increased opportunities for the private sector may stimulate growth and a smaller public sector may place less pressure on government finances.

Experience, however, suggests that efficiency, accountability, and quality benefits do not automatically follow implementation of the post-bureaucratic model. Recent and well publicised experience in Western Australia would suggest that the contract process does not necessarily lend itself to increased transparency and accountability. Such benefits may not automatically be realised for a variety of reasons, including the (valid) need to acknowledge some degree of commercial confidentiality. Also with respect to claims for improved accountability, New Zealand's Comptroller and Auditor-General has repeatedly warned the New Zealand government that the accountability framework established for State-Owned Enterprises does not provide sufficient information to meet legislative requirements and that "the SOEs are consequently falling short in their obligations of accountability to Parliament and to the wider public" (Controller and Auditor General, 1990). This observation is particularly relevant in view of the Western Australian Commission on Government's mandate to investigate the establishment of a similar legislative framework. Australian commentators including the Commonwealth Ombudsman, Commonwealth Auditor General, and the Chair of the House of Representatives Public Accounts Committee have joined in a veritable chorus of concerns that the post-bureaucratic model inherently undermines the administration's accountability relationship with Parliament (Uhr, 1989. See, for example, Pearce, 1989, 1989a; Taylor, 1989; Tickner, 1989). Similarly in the United Kingdom, concerns have been raised that the burgeoning growth of ministerially appointed agencies within the Next Steps programme is resulting in "a crisis of accountability" and a growing "democratic deficit" (Beavis and Nicholson, 1993).

Neither has public sector reform automatically produced efficiency benefits. The separation of the New Zealand Department of Education into policy and operational

agencies, for example, was intended to save \$100m, largely through the downsizing of the central bureaucracy. The actual results were so poor that a major review was initiated within months of the changes coming into effect (Boston, 1991).

The Committee has noted previously (Standing Committee on Estimates and Financial Operations, 1994) the importance of feasibility examination and performance monitoring in relation to the private delivery of public services. In this regard, the Committee considers comments that the superior performance of the private sector be accepted *prima facie* to be irresponsible (See, for example, Pryer, 1995). A sound financial administration framework that is appropriate to the wider administrative structure is necessary to ensure that the requisite information is available to enable the Parliament and the Executive to report confidently to the public on the expenditure of the public's funds.

2.2 THE FINANCIAL ADMINISTRATION AND AUDIT ACT 1985

In Western Australia, the *Financial Administration and Audit Act 1985 (FAAA)* underpins the state's administration by providing a framework for the expenditure and control of public money. The *FAAA* was introduced in 1985 as a result of a comprehensive review of the *Audit Act 1904*. The review concluded that the *Audit Act 1904* did not adequately provide for the modern accounting, audit, and financial management practices requisite to a high level of public sector accountability. The subsequent *Financial Administration and Audit Bill 1985* aimed to "make substantial improvements to the Law relating to financial management and year end reporting within the public sector and the role of the Auditor General with respect to the audit of departments, statutory authorities and the Treasurer's accounts" (Department of Treasury, 1985).

Self-evidently, the *FAAA* provides a framework for the administration and audit of the state's finances. The Act establishes and governs the operation of government accounts, recognises the annual supply and appropriation of public money, governs the investment of public money, creates and details the responsibilities of accountable officers and authorities, details the parliamentary reporting requirements of the Treasurer and government agencies, and establishes an Auditor General and provides for the Auditor General's responsibilities and powers.

The *FAAA* is structured on a three tier basis. Matters of principle, *e.g.*, that departments and statutory authorities keep records of an agency's financial position, are included within the Act itself. The regulations contain matters of principle below the level appropriate for primary legislation, *e.g.*, the content of the Treasurer's annual statements. Directions regarding financial practices and procedures required of departments and statutory authorities are contained in the Treasurer's Instructions. This third tier includes the specification of accounting and annual reporting standards and is intended to permit response to changes in prevailing standards without necessitating legislative amendment.

Prior legislation provided for a Consolidated Revenue Fund (*Constitution Act 1889*), a General Loan Fund, and a Trust Fund (*Audit Act 1904*). The *FAAA* broadened and re-titled the General Loan Fund to include revenue sources, other than loan funds, that are applied to capital works, with the intention of ensuring that all capital expenditure is appropriated by Parliament. The Act also introduced specifications for the creation and reporting of accounts forming part of the Trust Fund. A fourth Treasurer's account, the Treasurer's Advance Account, was also introduced. The account is operated in accordance with the *Treasurer's Advance Authorisation Act* for the relevant year. The Act specifies a monetary limit up to which the Treasurer can draw moneys from the Public Bank Account and details the purposes for which the money can be applied. Automatic authorisation of three quarters of the previous year's monetary limit for a period of two months is provided in the event of failure to proclaim a *Treasurer's Advance Authorisation Act* before 1 July.

The *FAAA* also introduced the concept of permanent heads of departments and boards of management of statutory authorities as "accountable officers" and "accountable authorities" respectively. The Act charges these accountable officers and authorities with responsibility for the services under their control and requires them to prepare and submit an annual report on the finances, efficiency, effectiveness, and operations of their organisations. Standards and time constraints for the content and presentation of

annual reports and financial statements are also specified.

Other features of the Act included incorporation of the *Public Moneys Investment Act* and extension of the Auditor General's functions to performance audits, all statutory authorities specified in Schedule One of the Act, and, where required by the Treasurer, the accounts of persons or bodies which have received grants from the Government for a specific purpose.

The *FAAA* was amended in 1986, 1990, and 1993. The 1986 amendments added and deleted statutory authorities from Schedule One in recognition of other legislative changes either creating or abolishing these authorities. The amendments also provided for direct reporting to Parliament for the administrative departments of Parliament, the Parliamentary Commissioner for Administrative Investigations, and the Office of the Auditor General. The distinction between money and property of the State as opposed to that held by statutory authorities was also clarified with a view to ensuring that statutory authorities are covered by the principal Act.

In 1990, the Act was amended to give effect to the recommendations of the Burt Commission on Accountability, provide for global appropriations, and make a number of minor amendments to reporting timeframes and criteria, definitions, and terminology. The amendments addressed two areas of concern to the Burt Commission. First, in response to concerns regarding the proliferation of entities operating under the control of departments and statutory authorities, "related" and "affiliated" bodies were defined and obligations placed on accountable officers and authorities to report on these bodies in accordance with the Treasurer's Instructions. Second, the amendments gave effect to the Commission's recommendation preventing secrecy of departmental or statutory authority operations. Under s58C, no department or statutory authority may undertake any action or contractual or other obligation which would prevent the Minister from providing to Parliament information on any conduct or operations of the department or statutory authority.

The 1990 amendments also empowered the Treasurer to approve the transfer of a central appropriation for a general purpose to another appropriation item to complement the introduction of "one line" appropriations and introducing a measure of management flexibility. Other provisions include the reporting arrangements for departments which have been abolished, the treatment of investment proceeds from the Public Bank Account, and revised reporting dates for annual reports and audit opinions.

The 1993 amendment allowed for the establishment of the Consolidated Fund, the introduction of net appropriations, and the annual reporting of certain hypothecated revenues. The creation of a single fund out of the Consolidated Revenue Fund and the General Loan and Capital Works Fund was intended to shift the focus from balancing of the recurrent budget to the total budget position. Separate Appropriation Bills are introduced for recurrent and capital expenditure out of the Consolidated Fund. The introduction of net appropriations allows for agencies to enter into agreements with the Treasurer to retain certain departmental revenues which will be credited against expenditure. The third feature of the 1993 amendments involves the reporting of general Government revenue which has been permanently appropriated to trust accounts for specified purposes. The inclusion of this hypothecated revenue is intended to provide a more extensive coverage of revenue and expenditure in the annual Estimates.

The *FAAA* is currently subject to some scrutiny within the terms of reference of the Commission on Government. The Commission was established in response to recommendations of the Royal Commission into the Commercial Activities of Government and Other Matters. The *Commission on Government Act 1994* specifies twenty four specified matters of inquiry, including five specified matters of specific relevance to the administration of public finances. These are reproduced at Appendix II. Some of these specified matters are noted in this paper. Where this is the case, particularly in relation to issues regarding the Office of the Auditor General, the Committee has not sought to duplicate the work of the Commission and has restricted its discussion accordingly.

3. THE COMMITTEE'S APPROACH TO THE REVIEW

The Committee has approached the current review by first examining public sector reforms in various jurisdictions and their varied successes and failures. In particular, the Committee noted the impact of the reforms on public sector accountability structures and the implications for financial administration legislation. The Committee sought advice on the scope of its review from the Western Australian Auditor General and the Treasury Department. The Committee has also visited a number of jurisdictions within Australia and New Zealand.

This paper encompasses the central areas and issues of review as the Committee sees them. The Committee has not attempted to draw any conclusions regarding the future direction and content of future financial administration and management legislation in this state, rather the Committee intends this paper to be used as a discussion document. To this end, the Committee has included a number of specific discussion questions at the close of each of the following sections of the paper.

4. FINANCIAL ADMINISTRATION REFORM

4.1 THE REPORTING ENTITY

Meeting [the needs of users of financial information] will require the financial reporting framework to be strong enough to handle the wide variety of detailed organisational forms now found in the public sector, and the numerous changes in these organisational forms, and in the boundaries of the public sector, that have occurred in recent years.

(Mayston, 1992)

It is generally accepted that the government reporting entity is bounded by those resources over which the government has control (McCalliff *et al*, 1994). The increasing "deregulation" of the public sector, however, has facilitated a proliferation of organisations including departments, statutory authorities, subsidiary organisations, quasi-autonomous units within departments, government owned companies, government contractors, and contractors to government. These organisations are created through a number of mechanisms, including legislative authority (both umbrella, as in the case of

the Victorian and New Zealand State Owned Enterprises Acts, and specific, for example the raft of legislation authorising the restructuring of SECWA), organisational restructure, and ministerial fiat, and may or may not be separately identified in the annual estimates of expenditure. It is becoming increasingly difficult to define where government or parliamentary control extends and where, indeed, the boundaries of the public sector lie.

The absence of a clear scheme of public sector organisations and their respective powers and responsibilities has implications for compliance with financial controls, reporting relationships with the Parliament, the extent of the responsibilities of statutory offices such as the Auditor General, and the scope of consolidated reports. It is apparent to the Committee that a primary task in examining the public sector financial administration framework is, therefore, the identification of public sector organisations and their various reporting responsibilities. In the words of the New Zealand Finance and Expenditure Committee (1991), "the Crown cannot be effectively held to account if it is not clear what it is accountable for".

The Legislative Council Standing Committee on Government Agencies addresses this issue in its report "State Agencies: Their Nature and Function" (Standing Committee on Government Agencies, 1994). The Committee noted the "amorphous mass of organisations participating in public administration" and subsequently proposed a *State Agencies Act* enabling the creation of agencies by regulation and providing for certain powers and responsibilities. The Committee's proposal is not dissimilar in intent to the New Zealand and Victorian Parliaments' *State Owned Enterprises Acts* passed in 1986 and 1992 respectively and the Queensland *Government Owned Corporations Act 1993*. These Acts provide for the establishment, operation, and accountability requirements of particular forms of state owned organisations. In New South Wales, the classification of government agencies is guided by the 1989 policy document "The Classification and Control of State Organisations" (NSW Task Force, 1989). At the Australian Commonwealth level, the *Commonwealth Authorities and Companies Bill 1994* distinguishes between agencies which "own" money in their own right and those which manage funds which remain under the control of the Commonwealth. The latter will be subject to the provisions of the *Financial Management and Accountability Bill* and required to establish processes which secure the efficient, effective, and ethical use of public resources.

The above frameworks vary in the extent to which they address the entirety of the public sector. Indeed, the Committee noted an absence across many jurisdictions of a readily accessible description of the public sector which accounted for the variety of agencies that utilise public funds. In many cases, parliamentary committees responsible for public accounts mandates were unable to clearly articulate which organisations constitute the public sector.

It is noted above that umbrella legislation for the creation of agencies has been used by a number of jurisdictions. This has, however, most often been limited to certain types of agencies, most notably commercial or trading enterprises. Other agencies, for example, New Zealand "Crown agencies", are defined within public administration legislation and listed in the schedules to that legislation. The Committee understands that the South Australian government is currently considering the proposed Commonwealth framework as a model for agency creation umbrella legislation. Similarly, the Western Australian

Royal Commission into the Activities of Government and Other Matters (1992) recommended that the establishment of umbrella legislation in this regard be investigated. The Committee also notes that the recently issued Minimum Obligatory Information Requirements (Department of Treasury, 1995) utilises the Australian Bureau of Statistics Government Finance Statistics classification of government agencies. This classification is based on the financial, financing, and market nature of agencies.

Irrespective of the mechanism selected to identify the public sector, the Committee considers that the following issues need to be pursued:

- (i) How should the agencies operating within the public sector be identified for reporting and accountability purposes?*
 - (ii) Should such a classification scheme incorporate mechanisms for the creation of various types of agencies?*
-

4.2 APPROPRIATIONS

In Western Australia, public sector expenditure is, in general, appropriated on an annual basis subject to the granting of supply and under appropriation made by an Act. It has been the practice for appropriations to be authorised by two Appropriation Acts providing for recurrent services and capital works respectively. The effect of this arrangement in terms of the *Constitution Acts Amendment Act 1899* has been the subject of continuing debate between the two Houses of Parliament. Exceptions to this process are standing or permanent appropriations. These include the appropriation of specific revenue for a specific agency or purpose, for example the Water Authority of Western Australia, and the appropriation of general revenue to a specific purpose, for example the salaries of Members of Parliament. In the first case, revenues are paid into the account of the agency concerned and do not constitute a transaction of the Consolidated Fund. In the second case, expenditure is paid from the Consolidated Fund and is included in the reporting of the Fund's transactions as "Amounts Authorised by Other Statutes".

The Committee examined four features of the appropriation process across jurisdictions. These are discussed below.

(i) Basis of Appropriation

In Western Australia, the annual Appropriation Acts traditionally tie expenditure to the purposes expressed in the Schedules to the Acts and detailed in the annual Estimates of Expenditure. This requirement notwithstanding, the *FAAA* affords agencies the flexibility to shift funds under the total allocation across programmes on objects of expenditure within Votes, effectively creating "one-line" appropriations.

Australian jurisdictions generally appropriate funds on a global or programme basis. Similar to Western Australia, in Victoria and the Commonwealth funds are appropriated for each agency as two separate items of capital and recurrent expenditure. In New South Wales, appropriations are made on a programme basis, although agencies are able to shift funds between programmes. The New Zealand *Public Finance Act 1989* represents a significant departure from these models, requiring that appropriations be made on the basis of specified outputs. The Act requires separate appropriations for

- a) each group of goods and services (class of outputs) to be produced by a department;
- b) any capital contribution being made by the Government to a department; and
- c) payments of benefits or grants by a department on behalf of the Crown.

In this way, a distinction is made between current production, capital contributions, and transfer payments on behalf of the Crown (Finance and Expenditure Committee, 1989). The Act also provides for three different types or "modes" of appropriation (See Appendix III). These represent a progression towards appropriating funds in the context of the State's changing role from a provider to a purchaser of public goods and services. That is, from the traditional appropriation method for the cash cost of inputs, to appropriation for the full cost of purchasing goods and services. Agencies were to have in place the necessary management, information, and accounting systems to enable all appropriations to be made under Mode B or C by 1 July 1991.

The New Zealand model is currently being examined by Australian governments. The South Australian Treasury is considering an output/accrual based appropriation process, and in Victoria departments and ministers are moving toward a contract appropriation model that reflects the charter of each organisation. At a meeting held in December 1994, the Heads of Australian State/Territory Treasuries discussed the issue of contract-based budgeting (or output-based budgeting) and resolved to establish a working group to further examine this issue. A report identifying the key features of contract based budgeting was considered at a State' heads of treasuries meeting held in July 1995.

The Committee notes that tying appropriations to specific classes of output provides for less operational flexibility than the outcomes basis currently used in Western Australia. Similar to Western Australia, the New Zealand model incorporates some flexibility by providing for funds to be shifted across allocations. The New Zealand Governor General may direct that funds be transferred between specified classes of outputs within a statutory limit. Further, during the course of the financial year, the Minister of Finance may approve expenditure in excess of an appropriation and to a statutory limit. Such expenditure is included in the Crown's financial statement and the relevant agency's financial statements for the relevant year and in an Appropriation Bill for the following financial year.

(ii) Length and Frequency of Appropriations

A number of jurisdictions in Australia and New Zealand have introduced provisions for expenditure outside of the traditional annually-based appropriation. These encompass provisions to carryover unspent funds into the following financial year, borrowing against the following year's appropriation, and appropriations for multiple years.

In New South Wales, carryover of unspent funds amounts to an administrative carryover of savings to certain limits (2%). At the Commonwealth level, a carryover provision of up to 10% must similarly be "reappropriated" each year. The Victorian *Financial Management Act 1994* allows for unspent appropriations to be carried forward into the succeeding financial year, as determined by the Minister. Such expenditure is carried forward either directly or by way of payment into a Trust Account, and must be shown in the statement of expenditure for the succeeding financial year. Unspent appropriations in this case do not include services and purposes that remain unpaid at the end of the financial year: similar to Western Australian practice (s27, *FAAA*; TI323), funds required for such payments may be transferred to a suspense account within the Trust Fund for that purpose and are subsequently deemed to have been a payment from the Consolidated Fund in that year.

The Victorian *Financial Management Act 1994* also authorises the Governor in Council to approve departmental borrowings against future appropriations. Such borrowings must not exceed 3% of the amount appropriated to the department in the current year and must, to the Minister's satisfaction,

- a) be for the purpose of expenditure considered prudent and advantageous in the current financial year; and
- b) accrue or continue benefits in the next financial year.

The New South Wales Treasurer is afforded broader powers in this regard. Section 22 of the *Public Finance and Audit Act 1983* empowers the Treasurer to make payments from the Consolidated Fund, notwithstanding appropriations already approved by the Parliament, and to include such payments in the appropriation for the succeeding year. This does not, however, effectively constitute a borrowing against the succeeding financial year as no requirement exists to deduct the expenditure from that year's budget. The provision also differs from the Western Australian Treasurer's Advance Account in that the Western Australian practice is to appropriate such payments for the financial year in which the payments were made.

With regard to appropriations extending over multiple years, the Committee noted that the New Zealand *Public Finance Act 1989* provides for appropriations for a period of up to five years. In Victoria and New South Wales, although the notion of extended appropriations has not been specifically addressed, forward estimates are treated as presumptive allocations. The Committee also noted that the South Australian Treasury is considering the implementation of extended appropriations.

(iii) *Annual Estimates of Expenditure*

The Estimates of Expenditure provide the detail of the annual appropriation for the purposes of parliamentary scrutiny of the Appropriation Bills. In Western Australia, this information is presented at a programme and sub-programme level, and is supported by the Programme Statements which state the sub/programme objectives, allocation of finances and FTEs, significant issues and trends, major achievements for the previous year, major planned achievements. The information that agencies are to include in the Estimates of Expenditure and Programme Statements is specified in annual guidelines and summarised in the Treasury Department's Minimum Obligatory Information Requirements (1995). In addition to the Budget Papers, the timing of the introduction of the budget

into the Parliament allows for unaudited financial statements and performance indicators to be utilised by parliamentary committees in the scrutiny process.

The information requirements for the New Zealand Estimates of Expenditure are detailed in the *Public Finance Act 1989*. This information includes, among other things, the mode or modes of appropriation applicable to each vote; the classes of outputs to be supplied, their associated expenditure and expected revenue, and their link with the Government's desired outcomes; other expenditure however appropriated; comparative figures for the previous year; statements of estimated/financial position for the commencement and end of the financial year; a statement of estimated cashflows for the financial year; and the financial performance to be achieved by the department as agreed between the CEO and the responsible Minister.

The Committee noted that the South Australian Estimates hearings are conducted before the end of the financial year and without the benefit of end of year reports. The material available to the parliament for scrutinising the estimates include previous annual reports, a line by line statement of appropriations, programme papers detailing programme objectives, planned achievements, previous outcomes, and, where these are available, the performance indicators.

The Estimates material supplied to the Victorian Parliament includes programme objectives, output measures, and business and corporate plans. In the context of the purchaser-provider model, the programme statements for purchasing departments include and separately identify the related service agencies and their allocated funds. The Committee noted, however, that funds can be moved between service agencies in the same portfolio subject to the performance contract between the service agency and the head of the purchasing department.

(iv) *Net Appropriations*

Section 23A of the *FAAA* allows the accountable officer or authority of an agency to enter into agreements with the Treasurer to use receipts from the provision of services and the sale or lease of property to finance specified expenditure. Although such agreements are indicated in the annual Estimates of Expenditure in a manner which permits debate on the expenditures, they effectively remove the requirement for annual appropriation of the revenue in question. This avoidance of Parliamentary authority is of particular concern when the majority of agency expenditure is authorised by way of net appropriation. Net appropriations can, however, provide valuable incentives to agencies by enabling agencies to directly benefit from their efficient and effective use of resources. Net appropriations have also been implemented in New Zealand, Victoria, South Australia, and the Commonwealth.

Net appropriations were introduced in South Australia in 1988 and are now utilised by all agencies. Retained revenue is managed through Special Deposit Accounts approved by the Treasurer, and can be carried over into subsequent financial years. The Government contributes to the difference between retained revenues and expenses. Net appropriations are identified in the budget estimates. In Victoria, the *Financial Management Act 1994* allows for funds received from non-compulsory service charges or by way of Commonwealth specific purpose payment to be applied without further appropriation. Such transfer of funds is subject to agreement between the Minister responsible for the department in

question and the Minister administering the *Financial Management Act 1994*. The Commonwealth *Financial Management and Accountability Bill 1994* also permits the federal Finance Minister to enter into net appropriation agreements with the responsible Minister or, in the case of agencies for which the Finance Minister is responsible, the Chief Executive Officer of the agency.

The New Zealand *Public Finance Act 1989* allows for revenue obtained from the supply of outputs pursuant to appropriation Mode B and from the sale of capital assets to be allocated to specified classes of outputs or capital assets respectively without further appropriation. According to the type of appropriation particular to the class of outputs in question, the department may or may not be required to signal the net appropriation in the Appropriation Act for that year and may or may not be required to seek the approval of the Minister for incurring such costs.

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- (i) *Should funds be appropriated on an outputs basis in Western Australia?*
- (ii) *What would be the advantages of introducing appropriation provisions for the carryover of unspent funds, borrowing against future appropriations, and multi-year appropriations? With what authority should such provisions be implemented? How and when should such practices be reported to the Parliament?*
- (iii) *What information should be made available to the Parliament for the purposes of considering the annual appropriation bills? What form should this information take? Where should this information requirement be specified?*
- (iv) *Should Parliament have a role in approving net appropriations? On what basis should such approval be made?*
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4.3 PUBLIC FINANCE ADMINISTRATION

The Committee noted a number of financial administration initiatives implemented across jurisdictions which underpin prevailing public sector administration trends. These included decentralisation of public accounts systems and devolution of financial management controls. These two issues are discussed in depth below. As anticipated, public officials across jurisdictions perceived the implementation of accrual accounting to be the central financial reform initiative implemented during the past decade. Most jurisdictions in Australia and New Zealand now operate on an accrual basis, with statutory authorities having introduced accrual systems in the mid-eighties and departments following suit in the late eighties and early nineties. Implementation has tended to be slower in major government departments such as the health and education sectors and some valuation issues, such as heritage buildings and works of art, remain outstanding.

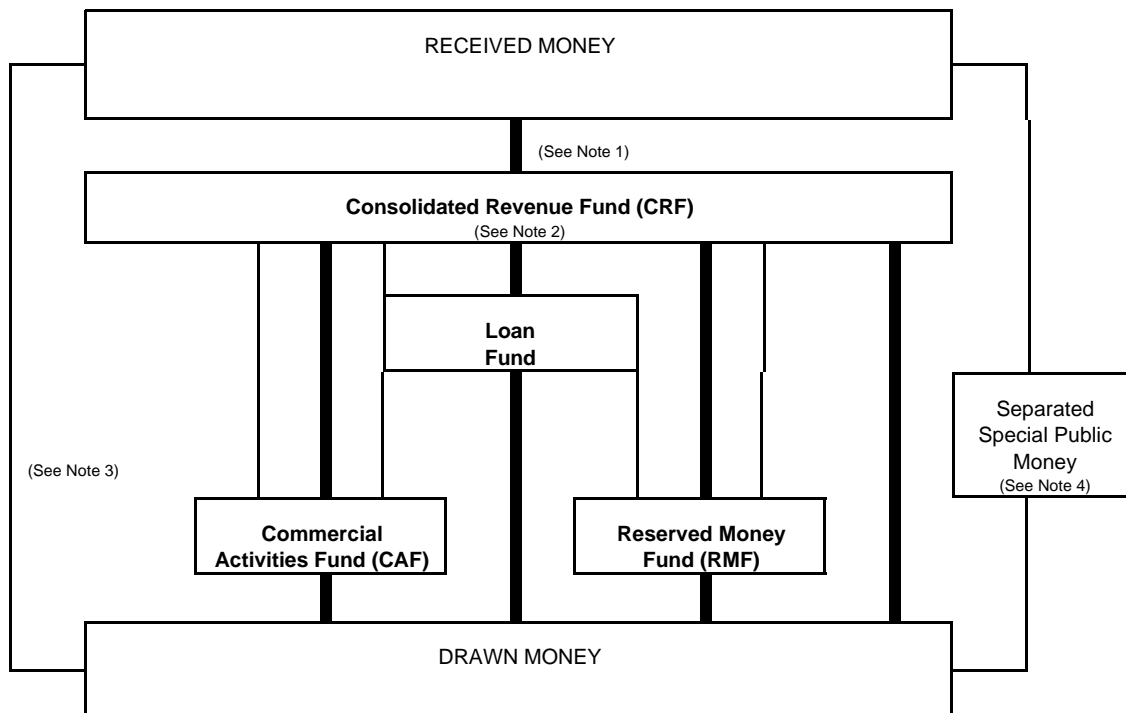
(i) *The Public Accounts*

The legislative basis for the system of public accounts in Western Australia is the *FAAA* and the *Constitution Act 1889*. All public money and money of a statutory authority in Western Australia is held in investments, the Public Bank Account, or other bank accounts opened by a department (in limited numbers) or a statutory authority as authorised by the Treasurer pursuant to an Act. The Treasurer is required to open and maintain a Public Bank Account, which incorporates moneys credited to the Consolidated Fund and the Trust Fund, but does not include bank accounts held by departments and statutory authorities. The third Treasurers' account, the Treasurer's Advance Account, represents an overdraft authority on the Public Bank Account. Money cannot be withdrawn from the Public Bank Account except after the granting of supply and under appropriation made by an Act, and in accordance with a warrant signed by the Governor.

The Committee noted that jurisdictions vary in the extent to which revenues and expenditures are recorded in centralised accounts. The federal government, under the Australian Constitution, is required to credit all money received by the Commonwealth to the Consolidated Revenue Fund. The government also retains a Trust Fund and Loan Fund. The *Financial Management and Accountability Bill 1994* currently before the Parliament recommends expanding the number of central accounts to incorporate the Consolidated Revenue Fund, a Loan Fund, a Reserved Moneys Fund (which includes genuine trustee moneys), and a Commercial Activities Fund (See Figure One). Under the proposed system, and consistent with the Constitution, all public money must be credited to the Consolidated Revenue Fund as soon as practicable unless it is subject to a Special Instruction. If the money is borrowed money (excluding credit card cash advances), it is then transferred to the Loan Fund. A component of the Reserved Money Fund may be established by the Finance Minister or by Act to enable the transfer of funds from the Consolidated Revenue Fund or the Loan Fund for specified purposes. The Finance Minister may also establish a component of the Commercial Activities Fund for agency activity that the Minister considers should be accounted for as if it were a commercial activity. This allows funds derived from a commercial activity to be transferred from the Consolidated Revenue Fund or Loan Fund to the component and to be debited from the component for

specified purposes related to the activity.

Unlike the *FAAA* and the *Commonwealth Financial Management and Accountability Bill 1994*, the *New Zealand Public Finance Act 1989* makes no reference to central funds such as a Consolidated Fund or Trust Fund. Neither does the *New South Wales Public Finance and Audit Act 1983* require the New South Wales government to establish central accounts. The New Zealand Treasury, under direction from the Minister for Finance, is required only to open and operate a Crown Bank Account. Unlike Western Australian practice, all departments may open and operate Departmental Bank Accounts at the direction of the Finance Minister or Treasury. All public money is required to be credited to either the Public or Departmental Bank Accounts. Public money does not include money held by Crown agencies, which may open and operate bank accounts at their discretion. This accounts structure also differs from the provisions of the Australian federal *Financial Management and Accountability Bill 1994* in that the Bill clarifies the position of the federal Finance Minister as the custodian of all commonwealth public money by affording the Minister exclusive authority to open and operate public bank accounts. That is, unlike New Zealand agencies, Australian agencies respondent to the Bill may not hold money in their own right. Similarly in South Australia, agency accounts may only be opened by the Treasurer. The Committee noted that South Australian legislation also requires the Treasurer to notify the creation of such accounts in the Government Gazette, stating the purpose for which the account is opened.



- Indicates a common type of transfer
- Indicates a less common type of transfer
- 1. All received money must be credited to the CRF as soon as practicable after receipt (unless a Special Instruction applies).
- 2. The following transfers pass through the CRF: transfers between components of the CAF or the RMF; transfers between the CAF and the RMF; transfers from the CAF or RMF to the Loan Fund.

3. An example of this transfer is an unused advance on expiry of the relevant appropriation.
4. Separated special public money is special public money that is subject to a Special Instruction.

Figure One: Commonwealth Fund Accounting System.

Permitting agencies to hold money in their own right has obvious advantages in a managerialist climate. A decentralised structure permits agencies to draw their own cheques as opposed to working through a central authority, and facilitates an administrative environment where the financial benefits arising from efficiencies can be directly realised by agencies. Holding public money in separate accounts limits, however, the government's scope for cashflow management and correspondingly increases the need for short term borrowings. The loss of a centralised pool of investment funds also limits the government's investment powers. In New Zealand, this is overcome by a system of "sweeping" the cash reserves in agency accounts on a daily basis for investment purposes. Devolving financial administration authority to agencies also requires that sufficient personnel with requisite skills are available in each agency. While this is likely to be the case in New South Wales, where the public sector includes only seventeen departments, the comparatively fragmented structure of the Western Australian public sector, where it is estimated that 20-50% of agencies employ less than 20 staff, is unlikely to have available and skilled personnel distributed across all agencies.

(ii) Financial Administration

The FAAA, its regulations, and Treasurer's Instructions include principles and specific procedures for the administration of public finances. These include the locus of accountability for each agency, agency accounts, agency accounting manuals, investment, write-offs, and recoveries. The Committee considers that, while the current provisions are sound in principle, the degree of control is not consistent with general public sector administration trends toward increased management flexibility. The following discussion centres on two aspects of financial administration controls that impact on this issue.

First, the Committee noted the extent to which different jurisdictions have incorporated accounting standards into their financial administration structure. Two of the more advanced jurisdictions in terms of public sector and financial administration reform - New Zealand and Victoria - have both adopted a purist approach to generally accepted accounting standards. Neither jurisdiction has established separate government accounting standards. The Victorian public sector observes the Australian Accounting and Audit Standards established by the Australian Accounting Research Foundation. Consistent with wider public sector reforms, this approach is intended to align the public sector with private practice. Although New South Wales incorporates Australian Accounting Standards into its reporting requirements, the Treasury may grant exemption to particular agencies. Exemptions are not disallowable by the Parliament and are reported in the Department of Treasury annual report. In Western Australia, observance of Australian Accounting Standards is incorporated into the Treasurer's Instructions. In some cases, these are adopted in modified form.

The Committee has noted the argument that direct public sector observance of Australian

Accounting Standards impinges on parliamentary sovereignty. The Australian Accounting Standards are developed by the Australian Accounting Research Foundation, a body jointly established by the Australian Society of Certified Practising Accountants (ASCPA) and the Institute of Chartered Accountants in Australia (ICAA) in 1966. The Foundation is funded by and answerable to the ASCPA and the ICAA. The Foundation also works closely with the Australian Accounting Standards Board, a commonwealth statutory authority answerable to the federal Attorney General, and is partly funded by that department. Requirements that Western Australian public sector agencies directly observe the standards constitute, it is argued, an effective delegation of the Western Australian Parliament's legislative authority.

The Committee notes, however, that by the very notion of Parliamentary sovereignty, adoption of the standards, and the means by which this is managed, is at the Parliament's discretion. The Parliament may, for example, legislate to adopt the standards as they are promulgated, but provide for exemptions and modifications which may or may not be subject to disallowance. Further, requirements with regard to the adoption of accounting standards may be placed within the regulations to the Act, enabling their timely removal if, again, the Parliament so chooses.

Second, the Committee noted the changing nature of Treasurer's Instructions and their equivalents. In Western Australia, the Treasurer's Instructions form the "third tier" of the *FAAA*. The Treasurer's Instructions provide background, direction, and guidelines to agencies regarding the administration of public money and public property, are issued by the Treasurer, and are not subject to scrutiny by Parliament as a matter of course. The Treasurer's Instructions form a comprehensive document, prescribing the administration of the receipt and payment of moneys, public property, salaries and wages, accounting and financial management systems, accounting manuals, reporting requirements, and internal audit. In some cases, the Treasurer's Instructions are highly prescriptive. For example the Treasurer's Instruction regarding the information to be included in agencies' annual reports includes direction to include the postal and street address and telephone number of an agency's principal office. The Committee has noted, however, that more recently issued Instructions have tended to reflect broader guidelines. The Instructions relating to performance indicators, for example, include explanatory notes regarding the purpose and characteristics of valid and reliable non-financial performance information. The level of direction extends to a brief statement of the indicators to be disclosed and the required qualitative characteristics of those indicators.

This change in emphasis from prescription to guidance is common to most jurisdictions visited by the Committee. The Victorian Treasurer's Instructions, for example, became the Treasurer's Directions with the enactment of the *Financial Management Act 1994* and contain less prescription in accounting procedures and other controls, including the abolition of FTE controls, with the intention of devolving managerial accountability. The South Australian Treasurer's Instructions are currently under review, and the New South Wales Best Practice Financial Initiative programme includes a review of the Finance Minister's Directions with a view to producing a statement of best practice and broad guidelines. Not all of the New South Wales statements will be compulsory. Similarly, the commonwealth *Financial Management and Accountability Bill 1994* will replace the Finance Minister's Directions with the Finance Minister's Orders. These will provide broad guidelines to be observed by agency officers. Accounting procedures will be addressed by "Chief Executive Officer's Instructions" which will be developed by individual agencies.

The New Zealand Treasurer's Instructions have also been simplified and set at a higher level to reflect broader statements of policy. The Committee noted that the need to consolidate agency accounts was considered in the development of this delegation framework.

The Committee has also considered the role and authority of the various parliaments with respect to the Treasurer's Instructions, and the use of penalties for breaches of accounting requirements. It is noted above that the Western Australian Parliament does not scrutinise the Treasurer's Instructions as a matter of course. The Finance Minister's Orders currently proposed by the Commonwealth *Financial Management and Accountability Bill 1994* will, however, be disallowable, as will the regulations to the Act. At state level, the Treasurer's Instructions or equivalent are not disallowable in South Australia, Victoria, and New South Wales.

The *FAAA* incorporates some monetary penalties for breaches of sections of the Act relating to the powers and responsibilities of the Auditor General and the provision of information. No penalties apply to breaches of the regulations or the Treasurer's Instructions. Similarly, Victorian legislation contains no penalties for failure to comply with accounting specifications. New South Wales includes penalties for breaches of the *Public Finance Act 1983*. These do not, however, distinguish between criminal and civil offences. This distinction will be addressed in the current review of the Act. At federal level, penalties will apply to breaches of the Act only. Regulations to the Act, which are to be observed by Ministers, will include their own penalties. In New Zealand, compliance requirements are established between the Treasury and agencies via a "relationship letter". Non-compliance is reported by the Treasury to the State Services Commission.

While the Committee noted support by Auditors General for a less prescriptive environment in terms of the provision of broad accounting guidelines, it was observed across jurisdictions that this gives managers more opportunity to mismanage. The Committee also noted concerns across jurisdictions that a less prescriptive financial administration environment will have implications for human resource issues. In particular, appropriate skill development was considered to be central to the success of a more flexible managerial environment. For example, it was considered unlikely that the current review of the South Australian Treasurer's Instructions would result in a significantly less prescriptive framework as it was felt that appropriate skills are not currently available in the South Australian public sector to support a move toward broad statements of principle. The Committee also noted that the staff of the Auditor General in that state rely on the prescriptive nature of the Instructions for audit purposes. In recognition of the devolved managerial environment embodied in the Victorian *Financial Management Act 1994*, the Victorian Treasury provides information support to agencies and actively encourages accounting and financial skills training. This includes a cross-agency graduate recruitment programme for accounting and finance students. The Victorian government also recognises the unique nature of the public sector accountability requirements by limiting recruitment from the private sector to one third of all recruitments and sources heads of departments only from the public sector. The Committee was also presented with the thesis that a lack of appropriate financial management skills within the public sector can be attributed to the relative value placed on policy and managerial skills in remuneration scales. It was observed that policy positions tend to represent a larger proportion of higher public service levels than do managerial

positions, providing greater incentive for public servants to develop policy rather than managerial skills.

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- (i) *Should the public sector observe the Australian Accounting Standards in their pure form? Are additional, sector specific requirements necessary?*
- (ii) *Should the Treasurer's Instructions be subject to comprehensive review to continue with the shift to broad guidelines across all instructions? Should such a shift be supported by agency specific instructions?*
- (iii) *What role should the Parliament assume in the ratification of the Treasurer's Instructions or equivalent?*
- (iv) *Should breaches of the Treasurer's Instructions or equivalent be subject to penalties?*
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4.4 PARLIAMENTARY REPORTING

The FAAA requires a range of financial and non-financial information to be provided to Parliament. This includes

1. quarterly statements of the Treasurer's accounts;
2. audited annual statements of the Treasurer's accounts;
3. audited annual financial statements of departments and statutory authorities;
4. audited annual performance indicators of departments and statutory authorities;
5. annual reports on the operations of departments and statutory authorities;
6. reports of the Auditor General regarding the efficiency and effectiveness of departments and statutory authorities; and
7. reports of significant matters under s95, which includes item 6 above.

The presentation requirements of the above information is specified in the Regulations (in the case of the statements of the Treasurer's accounts) and the Treasurer's Instructions (in the case of agency financial statements, performance indicators, and annual reports). Only two areas of the Parliament's primary source of information regarding the performance of government agencies - the annual report - are audited.

In his submission to the Commission on Government regarding the FAAA, the Auditor General reiterated the comments of the Public Accounts and Expenditure Review Committee (1991) regarding the need for clarification of the Executive's responsibility to ensure compliance with legislated reporting requirements (Pearson, 1995). It was noted that, first, a clearer commitment to the annual reporting process from the Parliament was required. This would include clearly defined annual reporting guidelines, monitoring

systems to ensure legislative compliance, and an evaluation system to ensure the review of annual reports. Second, central agency responsibility for the reporting, monitoring, and evaluation of annual reports should be clarified. The Committee notes that in 1993, highly prescriptive requirements for the production of annual reports were introduced in the Treasurer's Instructions (TI903). The Committee is not aware, however, of any initiatives undertaken by the executive to address the Public Accounts Committee's other recommendations noted above.

Financial and non-financial reporting requirements in most jurisdictions examined by the Committee is specified in financial administration legislation, for example, Victoria's *Financial Administration Act 1994*. Currently in New South Wales, annual reporting requirements are specified in separate annual reporting acts, however the Committee understands that these requirements will be incorporated into a single financial administration act currently under review. For New South Wales government trading enterprises, contracts between an enterprise, the Treasurer, the portfolio Minister specifies the financial and non-financial information to be reported. The contract also a statement of the agency charter, business plan, and risk management procedures. A similar statement will be required of the budget sector in the near future. These statements will not be public documents, but may be reflected in summary form in the annual reports. It is not anticipated that these statements will be audited.

(i) *Financial Information*

Financial accounting and reporting in the public sector can be seen to serve two purposes:

- a) to provide information for ex post monitoring of past performance, and
- b) to provide information for making economic, managerial, and political decisions (Mayston, 1992).

Traditionally, the purpose of financial reporting by governments has been to demonstrate departmental compliance with Parliamentary appropriations. Public sector end of year reports have, therefore, been based on cash. In recent years, as economic and political pressures have forced increased examination of the efficiency, effectiveness, and role of the public sector, governments, including Western Australia, have begun to implement accrual based reporting and accounting in order to identify the full cost of delivering goods and services. Micallef *et al* (1994) note that this is consistent with the view that governments should be accountable for all the assets (or economic resources) they control, all the liabilities they incur, and the results of activities during the period on those assets and liabilities. Further, the information provided by this level of disclosure facilitates more efficient and effective resource management, provides a longer term focus for government decisions, and underpins a growing public sector focus on a more competitive approach to the provision of services (OECD, 1993).

Conceptual frameworks for financial reporting generally appear to be predicated on the identification of users and user needs. Micallef *et al* (1994) have observed a general consensus across jurisdictions internationally that the main categories of users of public sector financial information are Members of Parliament; the public, including special interest groups; the media; and other groups including analysts, lenders, creditors, and investors. On the basis of the needs of these user groups, Micallef

concludes that public sector financial reports should be prepared in accordance with a specifically developed Australian Accounting Standard and include the following information:

- a) revenues and expenses, in aggregate and by major programme or function group;
- b) assets by major category, and changes therein, in aggregate and by major programme group;
- c) liabilities, the cost of financing those liabilities and contingencies;
- d) cash inflows and outflows; and
- e) compliance with spending and other financial mandates.

In Western Australia, departments and statutory authorities are required to present audited financial information to the Parliament on an annual basis. Unaudited cash statements of the Treasurer's Accounts are required quarterly. In addition, the Treasurer is required to table audited statements of the Treasurer's Accounts annually. It should be emphasised, however, that these statements relate only to the Treasurer's Accounts, that is, the transactions and operations against the Public Bank Account, and do not incorporate moneys held outside the Public Bank Account by some statutory authorities, but also include loan liabilities, contingencies, and the like.

Currently some private sector organisations and public sectors in other jurisdictions are moving from yearly to half yearly and quarterly reporting. In New South Wales, semi-annual statements are produced for the budget sector and Government Trading Enterprises produce quarterly information. Half-yearly financial statements are produced in New Zealand. This requirement does not, however, extend to Crown agencies. The concept of truncated and unaudited half yearly financial statements is supported by the South Australian Treasury. It was noted that new financial information systems which are currently being introduced in that state would facilitate such a reporting regime. The Committee notes that the recently issued Western Australian Treasury Minimum Obligatory Information Requirements foreshadow future quarterly reporting of comprehensive balance sheet, operating statement, and statement of cashflow data from all agencies.

(ii) Non-Financial Information

In the current outputs-oriented climate of public sector administration and accountability, financial information forms only part of the public sector's reporting relationship with its constituents. Flexibility in the allocation of financial inputs places greater pressure on measuring and reporting on the achievement of outputs and outcomes. Non-financial performance information indicating performance against stated objectives has become an integral component of government agency reporting requirements. The production and audit of non-financial performance indicators has been a legislated requirement in Western Australia since 1986. In Victoria, the production of non-financial performance information is a legislative requirement, however this information is not audited. Although non-financial performance information is not a legislative requirement of the federal or the New South Wales governments, it is produced on an annual basis by agencies in both jurisdictions.

Non-financial performance information requirements in Western Australia comprises two elements:

- report on operations,
- performance indicators.

In Western Australia, this information is presented to the Parliament within the annual reports of departments and statutory authorities. Annual reporting requirements are specified in the Treasurer's Instructions. The report on operations is required to include two areas of information. First, the report must provide general information regarding the agency's enabling legislation, location, structure, objectives, programmes, subsidiary bodies, and publications. Second, the report must include a review of the agency's operations for the year, incorporating significant operations; changes in objectives, policies, laws, or other factors affecting agency or subsidiary body operations; Ministerial directives; human resources information; research and development, marketing, pricing, and capital works activities; and any other significant matters.

Performance indicators are the second element of non-financial reporting requirements in Western Australia. Performance indicators are intended to enable the assessment of agency performance in discharging established objectives (TI904). Agencies are required to disclose for each programme the programme objectives and key efficiency and effectiveness indicators. The indicators are required to be relevant, verifiable, free from bias, and quantifiable; and encompass the operations of the agency and its subsidiary bodies. In its Tenth Report on Performance Indicators (Standing Committee on Estimates and Financial Operations, 1994b), the Committee observed that agencies in Western Australia have made significant progress in the past decade in the development and reporting of performance indicators. The Committee also noted the difficulty experienced by agencies in identifying discrete objectives and developing valid and reliable performance indicators, and a lack of central agency leadership in the development of performance information.

In examining non-financial performance information across jurisdictions, the Committee noted that the distinction between outputs and outcomes remain a subject of some debate. In Western Australia, outputs and outcomes are conceptualised respectively as:

- a) the goods and services produced or provided by a programme or sub-programme; and
- b) the behaviour or circumstances the agency wants to occur or the needs the agency wants to satisfy.

Western Australian agencies are required to report on agency efficiency in terms of the production of outputs and agency effectiveness in terms of the realisation of outcomes/objectives. In Victoria, however, performance information does not extend to outcomes, and is currently moving toward the development and reporting of performance information, or "output measurement specifications", for service agencies. Similar to Western Australia, the New Zealand *Public Finance Act 1989* requires information regarding the achievement of both outputs and outcomes, but draws a clear separation of responsibility between Ministers and agencies. Outputs are seen to be the responsibility of the chief executive officer of an agency, and the realisation of outcomes the responsibility of Ministers. With respect to agency responsibility, this distinction overcomes issues of policy and measurement. The mechanism for Ministerial reporting on the responsibility for outcomes is not, however, addressed in the Act. This

accountability gap was highlighted by the Finance and Expenditure Committee (Finance and Expenditure Committee, 1989) in its review of the *Public Finance Bill 1989*. The Committee observed that the lack of such a provision was "a significant omission from the Bill". Rather than recommending changes to the Act, however, the Finance and Expenditure Committee felt that the matter was best addressed in the Standing Orders relating to the estimates procedures. This amendment notwithstanding, Ministers have yet to appear before the Finance and Expenditure Committee regarding the achievement of outcomes within the context of the estimates.

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- (i) *Should the current audit requirements for non-financial performance indicators be extended to encompass the entire annual report?*
 - (ii) *What level of specification should govern the information requirements of the annual report?*
 - (iii) *Should agencies continue to be responsible for the achievement of both outcomes and outputs?*
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4.5 AUDIT

Public concern regarding the increasing size and expenditure of government during the 1960s and 1970s has contributed to a refocussing of the audit effort on the efficiency and effectiveness of government agencies. Value for money and performance audits have become an integral part of the Auditor General's role. This more comprehensive audit approach has implications for the scope and powers of the Auditor General. The changing face of public administration compounds this issue by raising the question of access to private sector organisations in receipt of public funds.

(i) Ambit

The scope of the Auditor General's role needs to be considered across a number of dimensions:

- (a) Agencies to be encompassed by the audit mandate.
- (b) Performance audit.
- (c) Government policy.

In regard to the first issue, the *FAAA* currently requires the accounts of the Treasurer, statutory authorities and their subsidiaries, and government departments to be audited annually by the Auditor General. The Auditor General is also required, upon request by the Treasurer, to audit the accounts of any person in receipt of a specific purpose grant and advance.

The increasing use of competitive tendering and contracting out of services to the private sector has raised debate regarding the audit of private sector contractors. The Committee observed general opinion across jurisdictions in favour of the audit mandate

extending to verification that the terms of the contract had been performed, the quality of the contract, and the manner in which the contract had been managed. In at least one jurisdiction, comment was made to the Committee that the heads of government agencies appear to believe that their responsibilities toward a service end when the contract has been let. Audit of the contract management process would reinforce the responsibility of government agencies to ensure that services are performed as agreed.

Second, it is generally accepted that the expanded scope of Auditors General to performance audit is a legitimate and valuable role. At present, this role is acknowledged in Western Australia by way of the requirement to produce and audit performance indicators and the Auditor General's authority to conduct performance examinations under s80 of the *FAAA*. In South Australia, with the exception of those organisations noted above, the audit mandate extends to efficiency, effectiveness, and legal compliance, and will soon incorporate full audit of annual reports. In New Zealand, non-financial performance information is audited for quantity, quality, and timeliness of information, including performance indicators, presented in the estimates. For policy and measurement reasons, New Zealand performance audit extends only to outputs, not outcomes.

The Committee also noted that at least one state has experienced conflict between the Auditor General and private sector boards of government trading enterprises with regard to performance audits. In arguing for the removal of barriers to competition with the private sector, the boards have moved to appoint private sector auditors which observe only a compliance audit mandate. The impact of performance audit on the commercial confidentiality of government commercial enterprises was also an expressed concern in most jurisdictions. In this regard, the Committee noted with interest that the downfall of the South Australian State Bank was attributed, in part, to the bank's failure to take advantage of the public auditor's wider mandate to examine effective, efficient, and ethical use of public funds. The South Australian Parliament currently grants (public) audit exemption to Workcover and the Meat Corporation.

Third, the Committee observed broad consensus across jurisdictions that Auditors General should not comment on government policy and that their mandate should be limited to the way in which policy is implemented. This position notwithstanding, Auditors General in most jurisdictions argued in favour of access to cabinet documents for the purposes of gaining a full understanding of the intent of government policy.

The Committee also noted that some jurisdictions afford the Auditor General a role in the process of making payments out of official bank accounts. In both New Zealand and Victoria, money may not be paid out of the New Zealand Crown Bank Account other than pursuant to a warrant signed by the Governor-General and certified by the Audit Office to the effect that each payment out of the Crown Bank Account is in terms of the Governor General's warrant and that there is an appropriation or other authority available against which it may be properly charged. Finally, the Committee observed that the *FAAA* is silent on the responsibility for monitoring the implementation of audit recommendations. In Western Australia, the Legislative Assembly Public Accounts and Expenditure Review Committee pursues attest and performance audit recommendations as a matter of routine. There is, however, no requirement that the audit office or the executive report to the Parliament on agencies' responses to audit recommendations.

(ii) Access

The *FAAA* currently provides for access by the Auditor General to accounts, information, documents, records, moneys, and property, and to compel the production of information and the appearance of persons. This privilege is unclear with respect to the private sector; is silent on the question of self-incrimination, legal professional privilege, and cabinet documents; and may be restricted in terms of commercial confidentiality.

The Western Australian Auditor General has stated that access to information by Auditors General should be guided by the principle of expediting the purposes of the enabling Act (Pearson, 1995). Accordingly, access should not be restricted on the grounds of self-incrimination, legal professional privilege, or commercial confidentiality, and should include cabinet documentation. With respect to competitive tendering and contracting out, the Auditor General notes that access should be limited to the information held by the purchasing public sector. The Auditor General recommends, however, that the office retain "reserve powers" to compel, in exceptional circumstances, the provision of information by persons outside the public sector. This would include instances where the information held by the government agency awarding the contract did not possess sufficient information to enable the Auditor General to form an audit opinion.

The Committee noted broad agreement with this position across jurisdictions. With respect to reserve powers of access, it was suggested to the Committee that an alternative investigative route in the event that agencies do not hold sufficient information may be inquiry by parliamentary committee, with appropriate subpoena powers. The Committee also noted general agreement that reserve powers of access to private contractors, where such powers are afforded, should be signalled in the performance contract.

The issue of access to information has also been addressed giving concurrent consideration to the reporting of that information. The Commonwealth *Auditor General Bill 1994*, for example, while affording the Auditor General wide powers of access to information, also enables the Attorney General to prevent the Auditor General from including information in a public document that the Attorney General believes to be sensitive. While representatives of the various jurisdictions visited by the Committee were generally agreed that the need exists to prevent the publication of some sensitive information, opinion was divided over the authority to prevent such disclosure. For example, the view was presented to the Committee that, just as private sector auditors report to directors and not directly to shareholders, so should the Auditor General report to the executive and not Parliament. Judgement with respect to the information that should be revealed to the Parliament would, therefore, more appropriately rest with the executive and not the Auditor General. Neither New South Wales nor New Zealand afford the executive this power of veto. In New South Wales, however, the government is afforded 28 days to consider and respond to a report of the Auditor General prior to its presentation to Parliament. On a less formal level, it was noted that, where Auditors General enjoy regular and private consultation with Parliaments and parliamentary committees, such matters may be resolved without a legislated authority.

(iii) Independence

The Commission on Government is currently considering issues relevant to the

independence of the Auditor General. These include the Auditor General's reporting relationship with Parliament, the method and terms of appointment of the Auditor General, the position of the Audit Office with respect to legislation governing the management of the public sector, and the approval of the Audit Office budget.

In most jurisdictions, the Committee noted a close working relationship between the Parliament and the Auditor General. This was particularly evident in New Zealand, where a significant proportion of the Auditor General's office budget is allocated to the provision of advisory and reporting services to Parliament. This includes substantial support to parliamentary committees during the scrutiny of the annual budget. In most jurisdictions, the relationship between the Parliament and the Auditor General largely consists of the reporting and follow up of the results of attest and performance audits. Most parliamentary committees with a public accounts or financial administration term of reference follow up audit recommendations to some degree. As noted above, however, responsibility for monitoring audit recommendations is typically not formally specified. The New Zealand audit office noted some difficulty in managing the parliamentary relationship in the absence of a committee that captures the audit sphere.

The Committee noted, despite the close relationship claimed and advocated between Parliaments and Auditors General, a reluctance to support the concept of a parliamentary committee with an oversight mandate. Advantages were acknowledged with regard to appointment and resourcing, however even in the case of committees with specifically no power of direction, it was felt these benefits were outweighed by the potential for abuse in terms of directing Auditors General toward and away from politically sensitive areas of inquiry. Similarly, executive powers to direct Auditors General were rejected across jurisdictions, although it was noted that some governments may request performance audits, particularly in relation to government commercial agencies where they are not subject to routine performance audit.

Related to the issue of the Auditor General's relationship with Parliament and the executive is the Auditor General's enabling legislation. The Western Australian Auditor General advocates a separate Audit Act and the establishment of the Office of the Auditor General as a statutory authority with the primary intent of reinforcing and demonstrating the primary relationship and accountability of the Auditor General to Parliament (Pearson, 1995). Separate legislation would achieve this end by transferring responsibility for audit legislation from the Treasurer to the Auditor General. The Auditor General notes that separate Audit Acts are the accepted position for the United Kingdom and for both federal and provincial governments in Canada. Establishment of the Office of the Auditor General as a statutory authority would have the effect of removing the office from the public service, reinforcing the office's position as independent of executive government and affording the office increased flexibility with regard to employment arrangements.

The Committee was somewhat surprised to encounter general ambivalence across jurisdictions as to the merits of a separate Audit Act. The New Zealand audit office sees the principal benefit of a separate Audit Act as the separation of the audit function from legislation administered by the Executive. Similarly, the Auditor General in Canberra considers the principal, if not the sole, benefit of a separate Act as symbolic.

With regard to the status of the audit office, the Committee noted that in both the

Australian Commonwealth and New Zealand, the audit office is administered as a separate entity to the Auditor General. In New Zealand, this is achieved through administrative arrangement. Audit New Zealand provides attest audit services to the Auditor General and is funded out of audit fees paid by agencies. All other audit services are provided by the Office of the Auditor General and are funded by annual appropriation under the recommendation of the Offices of Parliament Committee chaired by the Speaker of the House of Representatives. These services include performance audits and advisory and reporting service to Parliament. The Australian National Audit Office, conversely, is to be established as a statutory authority, providing a symbolic separation from the executive and a real separation in terms of public service staffing constraints.

Relevant to the independence of the Auditor General is the issue of accountability of the office. A number of accountability measures already exist. Additional approaches may include requirements that the office track the outcomes of reports; review and follow up of reports by a parliamentary committee; and periodic external review. Audit legislation in Victoria and New South Wales requires the respective Audit Offices to be the subject of triennial independent performance audits.

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- (i) *Should the ambit of the Auditor General extend to private sector contractors and continue to include performance audit of government trading enterprises? How should access in this regard be managed?*
 - (ii) *What should be the locus of authority regarding the publication of sensitive information?*
 - (iii) *What body should be responsible for the followup of the Auditor General's recommendations and should this responsibility be legislated?*
 - (iv) *Under what legislative framework should the Auditor General and the Office of the Auditor General operate?*
 - (v) *How should the accountability of the audit office be managed?*
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4.6 FINANCIAL MANAGEMENT

The above discussions are primarily concerned with public finance administration, as opposed to the way in which governments manage the public finance. The current New Zealand government recently passed legislation which, while not dictating, for example, the level of debt the country should have, establishes guiding principles for responsible fiscal management. The essential features of the *Fiscal Responsibility Act 1994* (monetary policy is independently controlled by the Reserve Bank of New Zealand) are

1. Minimum legislative obligations for the production of key fiscal information. The budgetary, monetary policy, and fiscal responsibility process in New Zealand, therefore, becomes transparent to public and finance analysts.
2. A key set of benchmarks against which fiscal policies can be assessed. These are:

- total crown debt is to be reduced to "prudent levels" by achieving operating surpluses every year until the prudent level has been reached;
- then total Crown debt is to be maintained at the prudent level by achieving, on average over an economic cycle, balance between operating revenue and operating expenditure, ie, a cyclically-adjusted balanced budget;
- on top of this, the government is required to achieve levels of Crown net worth that provide a buffer against adverse future events;
- there is a requirement to manage prudently the fiscal risks facing the Crown (eg, earthquakes). This means that such risks must be clearly identified and measured as best as can be done;
- lastly, the government must pursue policies consistent with a reasonable degree of predicability about the level and stability of tax rates for future years.

(Bradford M, 1995)

Compliance with the provisions of the Act is not audited, as it is considered that this falls within the realm of policy. The Minister of Finance does, however, appear before the Standing Committee on Economics and Finance with respect to fiscal policy statements.

The Committee noted mixed opinions across jurisdictions regarding the perceived value of financial responsibility legislation. A Debt Elimination Bill is currently before the New South Wales Parliament. The Bill, which the Committee understands is to be retitled to reflect the broader financial responsibility scope of the Bill, includes fiscal targets (long, medium, and short term), and eight fiscal principles. The Bill focuses on requirements for government to report against fiscal standards, including reasons for any deviation from standards, rather than requiring the actual achievement of fiscal goals. The South Australian government is currently considering the establishment of similar legislation, perceiving the primary benefits to be increased transparency.

In some jurisdictions, however, the Committee noted scepticism regarding the value of financial responsibility legislation at state level. Although advantages of greater transparency and increased quality of reporting were generally acknowledged, it was observed that these can be achieved through traditional financial administration legislation. It was noted, for example, that the direction, substance, and responsibility for financial administration reforms in Victoria was made public by giving the reform programme a title, visual symbols, and an official launch. In Western Australia, major medium term fiscal objectives and strategies are published in the annual Budget Papers. The objectives and strategies published in the 1995 Budget Papers are reproduced at Appendix IV. It was also suggested to the Committee that, while such legislation may be appropriate at state level for the reasons noted above, avoidance of responsibility for subsequently unfavourable budget results would not be infeasible in the context of commonwealth-state funding relations. In essence, it was observed that such legislation may be a useful political tool, but would not be effective in its implementation.

(i) *What would be the merits of financial responsibility legislation in Western Australia?*

5. CONCLUSION

Fundamental changes to the structures and processes of any organisation, be it private or public, demand that regard be given to contingent changes to organisational support functions such as the administration of finances. While incremental changes have been made to the State's financial administration legislation over the past ten years to support the increasing pace of change in the public sector, it is timely that such legislation be afforded more comprehensive review. In this paper, the Committee has presented six general areas of consideration. The Committee has drawn on the experiences of other Australasian jurisdictions in developing specific questions for discussion. As noted previously, the Committee invites interested parties to address the specific questions raised in the paper and to raise issues with the Committee that are not included in the paper and may be relevant to the current review.

APPENDIX I

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APPENDIX II

COMMISSION ON GOVERNMENT: RELEVANT TERMS OF REFERENCE

3. *The operation and adequacy of the Financial Administration and Audit Act 1985 (particularly section 58C) with regard to providing Ministers, the Parliament, and the Auditor General with access to all information held by, or relating to, undertakings or commitments of, organisation in the public sector.*
6. *The legislation governing the functions of the Auditor General with regard to the obligations of persons to answer any question put by the Auditor General; and to produce any relevant documents, notwithstanding that the answer or the information may result in or tend towards self-incrimination.*
7. *The necessity and framework for legislation governing monitoring, control, and Parliamentary scrutiny of State-owned companies, enterprises, partnerships, and statutory authorities.*
14. *The most effective means of securing the financial independence of Parliament so as to enable Parliament to undertake its business.*
17. *The means best suited to be adopted by Parliament to bring the entire public sector under its scrutiny and review, having regard particularly*
 - (a) *to the use of parliamentary committees for the purpose,*
 - (b) *to question time, and*
 - (c) *to the manner in which the departments and agencies of government should be required to report to Parliament.*

APPENDIX III

MODES OF APPROPRIATION IN NEW ZEALAND

- MODE A(a) In the case of outputs, an appropriation of public money for the acquisition of goods and services of a non-capital nature relating to a specified class of outputs or a programme:
- (b) In the case of capital contributions, an appropriation of public money for the purchase or development of capital assets:
 - (c) In the case of benefits and grants, an appropriation of public money for the making of payments of benefits or grants on behalf of the Crown:
- MODE B(a) In the case of outputs, an appropriation for the costs to be incurred in the supply of a specified class of outputs:
- (b) In the case of capital contributions, an appropriation of public money to increase the amount of the Crown's net asset holding in a department:
 - (c) In the case of benefits and grants, an appropriation of public money for the making of payments of benefits or grants on behalf of the Crown:
- MODE C(a) In the case of outputs, an appropriation of public money for acquiring a specified class of outputs required by the Crown:
- (b) In the case of capital contributions, an appropriation of public money to increase the amount of the Crown's net asset holding in a department:
 - (c) In the case of benefits and grants, an appropriation of public money for the making of payments of benefits or grants on behalf of the Crown.

(s2 Public Finance Act 1989 (NZ))

APPENDIX IV

WA GOVERNMENT MEDIUM TERM OBJECTIVES AND BUDGET STRATEGY 1995

OBJECTIVES

- Provide an appropriate economic and financial environment which encourages growth in Western Australian business through
 - keeping tax rates and charges as low as possible;
 - privatising (including contracting out) those government functions which are more appropriately performed by the private sector; and
 - implementing efficiencies within the State's major trading enterprises including through corporatisation and commercialisation reforms;
- reduce government agencies' reliance on debt and to reduce the State's net debt;
- restore the State's AAA rating;
- maintain balanced or surplus Budgets during the Government's current term.

STRATEGIES

- the Consolidated Fund cash financing requirement has been reduced to zero in 1995/96 and the three out-years;
- further payroll tax concessions have been provided for small to medium sized businesses from 1995/96, reflecting the Government's commitment to reducing the burden of this tax;
- stamp duty rates on listed marketable security transactions have been halved from 1995/96, to protect Western Australia's business and revenue bases, in light of commensurate cuts in Queensland and other States;
- expenditure growth has been tightly held;
- surpluses projected against recurrent transactions have been used to finance the works programme, thereby eliminating the need for borrowings in 1995/96 and the three out-years; and
- accelerated debt repayment arrangements continue in 1995/96 and the out-years.

STANDING COMMITTEE ON ESTIMATES AND FINANCIAL OPERATIONS
Previous Reports

First Report: 1990/91 Budget Estimates - November 1990.

Second Report: 1991/92 Budget Estimates - November 1991.

Third Report: Leasing of Computer Equipment for the Legislative Council - February 1992.

Fourth Report: 1992/93 Budget Estimates - November 1992.

Fifth Report: Programme Undertaken During 1992.

Sixth Report: 1993/94 Budget Estimates - December 1993.

Seventh Report: Public Submissions 1993/94 - April 1994.

Eighth Report: Review of the Consolidated Fund Estimates 1994/95.

Ninth Report: The Consolidated Fund Estimates 1994/95.

Tenth Report: Performance Indicators.

Eleventh Report: Scrutiny of Financial Administration Legislation in Various Jurisdictions.

Twelfth Report: Review of the Consolidated Fund Estimates 1995/96.