

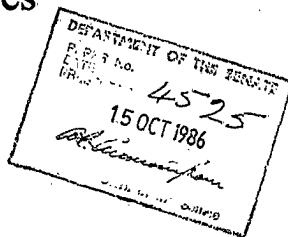


Forward Obligation of Government Expenditures

Report

256

Joint Committee of
Public Accounts



THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

JOINT COMMITTEE OF PUBLIC ACCOUNTS

REPORT 256

FORWARD OBLIGATION OF GOVERNMENT EXPENDITURES

Australian Government Publishing Service
CANBERRA 1986

JOINT COMMITTEE OF PUBLIC ACCOUNTS
FIFTEENTH COMMITTEE

SENATOR G GEORGES, (Chairman)

SENATOR J O W WATSON (Vice-Chairman)

(c) Commonwealth of Australia 1986

SENATOR THE HON DAME
MARGARET GUILFOYLE, DBE

SENATOR B COONEY

SENATOR G MAGUIRE

B J CONQUEST, MP

A J DOWNER, MP

R J KELLY, MP

H MAYER, MP

J G MOUNTFORD, MP *

G B NEHL, MP

L R S PRICE, MP

A C ROCHER, MP

P M RUDDOCK, MP

DR A C THEOPANOUS, MP

R E TICKNER, MP

SECTIONAL COMMITTEE 'A'

SENATOR G GEORGES (Chair)

SENATOR B COONEY

SENATOR THE HON DAME
MARGARET GUILFOYLE, DBE

R J KELLY, MP

G B NEHL, MP

A C ROCHER, MP

DR A C THEOPANOUS, MP

A J DOWNER, MP

*Ex-officio member being Chairman,
House of Representatives Standing Committee
on Expenditure

DUTIES OF THE COMMITTEE

Section 8.(1) of the Public Accounts Committee Act 1951 reads as follows:

Subject to sub-section (2), the duties of the Committee are:

- (a) to examine the accounts of the receipts and expenditure of the Commonwealth including the financial statements transmitted to the Auditor-General under sub-section (4) of section 50 of the Audit Act 1901;
- (aa) to examine the financial affairs of authorities of the Commonwealth to which this Act applies and of intergovernmental bodies to which this Act applies;
- (ab) to examine all reports of the Auditor-General (including reports of the results of efficiency audits) copies of which have been laid before the Houses of the Parliament;
- (b) to report to both Houses of the Parliament, with such comment as it thinks fit, any items or matters in those accounts, statements and reports, or any circumstances connected with them, to which the Committee is of the opinion that the attention of the Parliament should be directed;
- (c) to report to both Houses of the Parliament any alteration which the Committee thinks desirable in the form of the public accounts or in the method of keeping them, or in the mode of receipt, control, issue or payment of public moneys; and
- (d) to inquire into any question in connexion with the public accounts which is referred to it by either House of the Parliament, and to report to that House upon that question,

and include such other duties as are assigned to the Committee by Joint Standing Orders approved by both Houses of the Parliament.

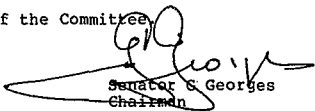
PREFACE

The inquiry into Forward Obligation of Government Expenditures was initiated by the Public Accounts Committee following the finding by the Auditor General, in his September 1985 Report, that significant weaknesses existed in the forward obligations control systems of several departments. This finding arose from audits at the Departments of Finance, Aboriginal Affairs, Local Government and Administrative Services, and Territories.

The forward obligations procedures form part of the annual budgetary process. They serve the purpose of allowing departments to enter into future capital expenditure and maintenance commitments. At the same time, they allow for control of the extent to which such commitments occur, with a view to limit budgetary 'lock-in'.

Because the Auditor General's comments had service wide implications, the Committee sought submissions from all departments. Additional information was sought from Treasury and the Department of Finance, with a view to establish whether a comprehensive review of the forward obligations system was required.

For and on behalf of the Committee


Senator S. Georges
Chairman

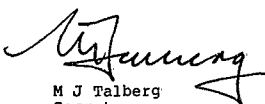

M J Talberg
Secretary
Joint Committee of Public Accounts
Parliament House
Canberra
10 September 1986

TABLE OF CONTENTS

CHAPTER	PAGE
Preface	
1. Overview	1
2. Forward obligations	4
Aims	4
Responsibilities	5
Audit findings and recommendations	8
3. Departmental submissions	10
Department of Finance	10
Other departments	12
4. Further investigations	16
Purpose of forward obligations	17
Relationship with forward estimates	18
Significance of over-commitments	18
Importance to overall budget strategy	19
Review by Finance	20
5. Conclusions and recommendations	21
Conclusions	21
Recommendations	21
APPENDICES	
A The regulatory framework	24
A1 Treasury Circular 1976/8 (1976)	25
A2 Finance Regulation 44A (1980)	28
A3 Joint Committee of Public Accounts Handbook on Financial Administration - Extract (1981)	32
B List of departmental submissions	34
C Additional material submitted by the Department of Finance	36
C1 Offsetting savings	37
C2 Devolution of responsibilities to departments	39
C3 Departments' obligation Recording Systems	41
C4 An alternative forward obligation system.	43

CHAPTER 1

OVERVIEW

Audit Findings

1.1 In his September 1985 report, the Auditor General reported on audits in four departments regarding the effectiveness of the forward obligations procedures. Audit found that:

- the departments have not kept accurate records;
- monitoring by Finance was inadequate;
- approved limits to forward obligations have been exceeded by substantial amounts on a number of occasions
- there was no mechanism through which the government could be regularly informed of such breaches; and
- there was a reluctance by departments to accept responsibility for the inadequacies discovered by Audit.

The Forward Obligations System

1.2 Procedures to secure government approval to enter into expenditure commitment against budgets of future years (ie forward obligations) have existed for some time. Such procedures are essential in cases where financial commitments cover several years. Purchase of defence equipment or property by the Commonwealth, or contractual arrangements, such as the cleaning of airports or the maintenance of computer equipment, are typical examples where the forward obligations system would be used extensively.

1.3 The forward obligations system was introduced in its current form in 1976, at a time when the Government attached particular importance to the objective of reigning in the rate of growth in government spending. The stated aim of the procedures was the application of a forward programming system to enable the Government to regulate the extent to which commitments involving future budget allocations could be made. This forward programming system was to apply across a broad range of budget expenditures to minimise the extent of budget 'lock-in'.

The Committee's Investigations

1.4 The Committee examined the Auditor-General's findings within the framework of the broad objectives set for the forward obligations system in 1976. It took account of submissions from 29 departments.

1.5 The Audit findings raised a fundamental question which has not been fully answered by departments in their submissions. This concerned the importance of monitoring by Finance to overall budget strategy. The Committee was of the view that only by answering this question could the issue of responsibilities for the inadequacies discovered by Audit, and the question of further reporting to Government, be resolved. There was general agreement that the more important the forward obligations system were to overall budget policy, the greater would Finance's interest be in monitoring departmental performance. However, the view that primary responsibility for forward obligations rested with departmental secretaries, was not shared by all.

1.6 Information obtained by the Committee through submissions, discussions with officers of the Department of Finance and further research indicated that:

- forward obligations covered less than 20 per cent of budget outlays;
- the breaches against approved limits reported by Audit had a relatively minor impact on overall expenditures. This was because, in most cases, departments have been able to find offsetting savings to the funds they needed, over and above the approved forward obligations limits;
- non-compliance tended to bear mainly on internal program management rather than overall budgetary control;
- the forward estimates system, which covered all budget outlays, had become the best available indicator of the extent of budget 'lock-ins'. The 1985-86 Budget Statements noted that, in that year, forward estimates formed the basis for individual portfolio targets for the first time, and that these targets served as guidelines in the determination of budget estimates; and
- the existing legislative and policy framework placed primary responsibility for forward obligations with departmental secretaries.¹

Conclusion

1.7 The Committee concluded that the forward obligations system, while important to departments, had limited value to overall budget strategy and control. In addition, the budgetary impact of the breaches reported by Audit were found to be relatively minor, once offsetting savings had been taken into account. These findings suggested that tighter monitoring by

1. See Section 2AB of the Audit Act and Appendix C on the policy of devolution of responsibilities.

Finance and regular reporting to Government on possible future breaches were unlikely to have a significant impact on overall budget outlays. In addition, greater involvement by Finance would not be within the spirit of the current policy of devolution of financial responsibilities to departmental secretaries.

1.8 The environment in which the forward obligations system was introduced a decade ago has changed considerably. The Committee concluded that it was time to review the purpose and the operations of the system within a broader context than that adopted by the Auditor-General in his September 1985 report.

1.9 The Committee noted that, in response to the Auditor General's findings, the Department of Finance initiated an internal review of the forward obligations system. The review proposed that Finance's monitoring activities be, in future, limited to only the major forward obligations categories. It also proposed that monitoring of expenditures against all other obligation limits should be the responsibility of departmental secretaries.

Recommendations

1.10 The Committee recommends

- that the current review of the forward obligation system by Finance be expedited.

1.11 Further it recommends that

- the new regulatory framework arising from this review:
 - specify that the system's main objective is to authorise departments to enter into forward commitments in certain expenditure categories; and
 - limit the extent of monitoring by Finance to cases where commitments could have a significant impact on overall budget outlays.

1.12 The Committee further recommends that

- in developing the details of the new regulatory arrangements, the policy of greater devolution of responsibility to departmental secretaries be given as much weight as possible. In this context, the Committee considers that monitoring arrangements by Finance which rely on global obligation limits for departments would be preferable to arrangements which monitor obligations at the program level.

CHAPTER 2

FORWARD OBLIGATIONS

Aims

2.1 Procedures to regulate forward obligations were introduced in 1976. In introducing the new system, Treasury circular 1976/8 referred to the importance the then Government attached 'to achievement of its objective of reigning in the rate of growth in government spending and reducing the relative size of the government sector'. The circular noted that this was central to the Government's economic and social strategy and that, for control of expenditure, the commitment stage was a decisive one.

2.2 The circular then went on to specify that:

In this context commitments are to be taken to include not only legislative undertakings but also actions falling within the area of Executive power... The Government has decided that, for budget planning purposes, ... it should be enabled to regulate, in a systematic way and consistently with its overall budget strategy, the extent to which commitments that would require future budget allocations might be made.

2.3 The circular noted that:

The central feature of the new procedures is the application across the broad range of budget expenditures of a forward programming system.

2.4 The circular advised that there was provision for the exemption of certain appropriations from this general system. It specified that salaries, overtime, travel, postage, telephone expenses and certain classes of standing or special appropriations were exempted at the outset. It noted that 'other categories may be exempted upon further examination or after consideration of a specific request by a department'.

2.5 In 1980, the forward obligations procedures were incorporated into the Finance Regulations (Regulation 44A), to the extent that Section 71 of the Audit Act permitted. Also in 1981 a detailed description of the forward obligation system was published by the Public Accounts Committee in its handbook on government financial administration (Appendix A.)

2.6 In its response to Audit, Finance noted that since 1976 the forward obligations system has tended to become less of a means to minimise budgetary 'lock-ins' and more of a resource management tool for departments. This was due to 3 year forward estimates becoming the primary information base for budgetary policy advice and to the forward obligations system presently covering less than 20 per cent of total budget outlays. Even within that 20 per cent, a number of obligation categories (eg Civil and Defence Buildings and Works programs; repairs and maintenance programs, etc) were explicitly regulated by budgetary procedures other than forward obligations.

2.7 The Committee notes that the above observations indicate that the contribution of the forward obligations system to limiting budgetary 'lock-in' could only be marginal.

2.8 In relation to the present day importance of the forward estimates system the Committee noted that, in the 1985-86 Budget process, forward estimates formed the basis for individual portfolio targets for the first time. These targets served as guidelines in the determination of Budget estimates.¹ For that year, the Budget estimates were \$69.1 billion, compared with forward estimates totalling \$68.1 billion. Thus the forward estimates - which relate to authorised on-going programs - only differed in 1985-86 from the actual Budget estimates by one and a half per cent.

2.9 During discussions, Finance advised the Committee that information on forward obligations was used by Departments in preparing their forward estimates. Within this overall budgetary context, forward obligations were a subset of forward estimates.

2.10 On the basis of the above, the Committee concluded that there was a lack of clarity as to the objectives of the forward obligations system in present-day circumstances and, in particular, the role of the system within the overall budgetary process.

Responsibilities

2.11 The Auditor General's September 1985 report highlighted some confusion about the relative responsibilities of the Department of Finance, as a central co-ordinating agency, and departmental secretaries, as managers of resources in their particular areas. The main points raised by Audit are as follows:

Some Departments Have Not Kept Adequate Records.

2.12 The Audit report stated that the forward obligation information provided to the Department of Finance and the Government contained inaccuracies and was incomplete. In addition, it highlighted reluctance on the part of some departments (eg Territories, Local Government and Administrative Services) to keep up-to-date, accurate and complete records of forward obligations. Reasons put forward by departments included:

1. Budget Statements 1985-86, AGPS, 1985 (p.311).

- a belief that responsibility for monitoring departmental estimates rested with the Department of Finance;
- lack of incentives to improve the system and lack of real sanctions for inadequate departmental performance; and
- the resource constraints associated with having to submit both budget (cash) and forward obligations estimates to Finance simultaneously.

Forward Obligations Limits Have Often Been Exceeded.

2.13 Audit was of the view that the failure to maintain adequate records of obligations was the principal reason why approved forward obligation limits have been exceeded for numerous items, in breach of Finance Regulation 44A. Examples of such breaches cited by Audit included:

- limits set for the Department of Territories being exceeded at 30 June 1984 by more than \$4.5 million, involving 40 items; and
- similar breaches having occurred at the other two Departments audited (ie Aboriginal Affairs and Local Government and Administrative Services).

2.14 Audit cited other instances, in which the Department of Finance had no alternative but to approve large increases to obligations limits, as a result of deficiencies in the operations of the forward obligations system:

- the 1984-85 appropriation for the ACT Commissioner for Housing Loans Scheme had to be increased by \$7.9 million because commitments had been entered into in 1983-84 without forward obligation approval;
- although the approved forward obligation limit as at 30 June 1984 for the Community Employment Program administered by the Department of Employment and Industrial Relations was \$266 million, the actual amount of obligations carried forward from 30 June was \$283.2 million, and
- in 1983-84 the Department of Aviation received Department of Finance approval for the commitment involved in a 4 year airport cleaning contract totalling \$11.25 million after the contract had been approved and notified in the Australian Government Gazette.

It is understood that similar contracts had existed in the past but had not been included in the Department's forward obligations estimates²

2.15 In total, commitments in excess of limits, as cited by Audit, amounted to around \$12 million in 1984-85 and \$28 million in 1983-84. These have emerged from selected audits at the four Departments listed in the Preface.

2.16 The administration of the A.C.T. Commissioner for Housing Loans Scheme was recently reviewed by the Committee in its 248th Report.³ The information supplied by the Department of Territories for that report and the conclusion reached had been taken into account in this inquiry.

2.17 In its 248th report the Committee said that it will continue to monitor the operation of the Scheme and subject the matter to further review.

Finance Has Not Been Effective In Monitoring The System.

2.18 In its September 1985 report, Audit noted that there was some confusion about the role Finance had in monitoring the effectiveness of the forward obligations system.

2.19 Some departments would have liked to see Finance take greater responsibility for monitoring the forward obligations processes. Audit itself implied in its report that monitoring could in future be improved by becoming 'preventive', rather than simply allowing breaches of approved limits to be detected after the event. Some departments indicated that Finance's centralised record keeping and monitoring system, the Finance Ledgers System (FLS), should be enhanced to allow for running control of forward obligations.

2.20 Finance was of the view that its role was limited to informing the Government of those breaches of the system which had possible implications for overall budgetary strategy and policy.

2.21 Finance also said that, under Section 2AB of the Audit Act⁴, departmental secretaries were responsible for the day-to-day running of their forward obligations systems. The Department, however, recognised that a facility enabling users of the FLS system to record both limits and actual obligations could

2. September 1985 Audit report (p.53).

3. Joint Committee of Public Accounts Report of the Auditor-General - April 1985, AGPS, 1986.

4. Finance noted that Finance Directions 25/15 and 24/16 unambiguously recognised the section 2AB philosophy in placing responsibility on departmental secretaries to maintain records of obligations.

lead to improvements in the operations of the forward obligations system. It advised that the necessary enhancements to the FLS have been considered, but that these could not attract high priority, because preference had to be accorded to systems for which there were statutory requirements to report to Parliament.

2.22 Finance also noted that the solution may not necessarily lie in enhancement to the FLS as such a solution could be perceived as encroaching upon departmental resource management decisions.

Audit Recommendations

2.23 The Audit findings summarised above suggest that existing controls over the level of funds obligated against Budgets for future years are deficient in several respects. In its report, Audit made several suggestions and recommendations as to how this situation could be remedied. These included that :

- the Government should be advised of departmental performance against both the original and varied approved obligation limits;
- the Department of Finance should seek the Government's decision on whether the submission of such information was desirable;
- the fundamental questions raised on the responsibilities for expenditure control were issues which needed to be addressed by Executive Government;
- the Department of Finance's ledger system should be enhanced and such a task should be accorded high priority.

2.24 Audit also suggested that the existing system could be improved through several other reforms, such as:

- preparation by the Department of Finance of consolidated and revised guidelines on forward obligations control;
the issuing of these guidelines to departments;
- revision of guidelines for Department of Finance staff to ensure that a uniform and consistent examination of forward obligation estimates was achieved by 'Supply' Divisions;
- the keeping by Finance of records of applications for limits to be approved and of the Department's action with respect to those applications;

- the initiation of systematic reviews by Finance to allow early detection of instances where approved limits might be exceeded;
- these systematic reviews would be in addition to the existing monitoring processes which rely on the bi-annual general reviews of approved obligation limits, on the examination of forward estimates, and the normal estimates cycle each financial year; and
- consideration of separating, in terms of timing, the cash bids from the forward obligations estimates

2.25 In respect of the last point Audit noted the Finance view that such a separation might be facilitated by the new approaches to Budget estimates introduced in 1985-86.

CHAPTER 3

DEPARTMENTAL SUBMISSIONS

3.1 Because the Auditor General's comments have service-wide implications, the Committee sought the views of all Departments. It received submissions from 29 out of the 30 Departments to which letters of request have been sent. A list of the Departments which sent in submissions is provided in Appendix B. Copies of the submissions themselves are available on request.

3.2 The main issues raised in submissions are summarised below.

The Department of Finance

The Forward Obligations Procedures.

3.3 Forward obligations procedures were initially promulgated by Treasury Circular 1976/8 and were incorporated in 1980 into the Finance Regulations (Regulation 44A), to the extent that Section 71 of the Audit Act permitted. The forward obligation procedures were described in Chapter 2.

3.4 The Department of Finance noted that the procedures covered purchases of major items, capital equipment or property and various contractual arrangements. Maintenance of a computer mainframe was cited as a typical forward contractual obligation.

3.5 The Finance submission stated that the procedures applied only to proposed obligations relating to already approved policies, and not to new policies. Overall, they covered 20 per cent or less of all budget outlays. They have been implemented primarily to provide flexibility at the level of individual expenditures, permitting departmental managers to enter into obligations for future financial years. Through the annual Budget process a limit was imposed, for any one year, on the maximum obligations that a particular department could enter into.

3.6 Chapter 2 of this Report described the aims of the forward obligations system as set out in the 1976 Treasury Circular. The new procedures were introduced, at that time, because of the recognition that long term obligations can reduce overall budget flexibility, and limit the Government's ability to determine and alter future expenditure priorities.

Forward Obligations and Other Budget Control Techniques

3.7 The issue of the relative roles of forward obligations and other budget monitoring and control techniques is important

to the question of the sharing of responsibilities between Finance and departmental secretaries. In essence, the question of whether the forward obligations system serves, in the current environment, a useful purpose in controlling overall budget outlays, needs to be resolved.

3.8 The Finance submission touched on this issue. It noted that the macro-economic significance of the forward obligations system has tended to decline since its introduction in 1976. Finance said that it has recently initiated a review of the forward obligations system and that the issue of whether the existing procedures should continue was one of the questions being examined.

Responses to Audit Comments

3.9 In its submission, the Department of Finance responded in some detail to the issues raised in the September 1985 Audit report.

3.10 Audit suggested that Finance's role in monitoring the performance of departments be strengthened. Finance, in response, said that such a development would be at odds with the principle embodied in the 1979 amendment of the Audit Act (Section 2AB) and with recent budget reforms initiated by the Government. Both were based on the principle of devolution of responsibility for financial management to departmental secretaries. Finance noted that, in its review of the forward obligations system, it has examined the merits and cost-effectiveness of a centralised obligations system, as proposed by Audit. At the same time, it has also considered several alternatives to a centralised system, including:

- a more detailed ex-post check by Finance;
- provision by departments of more detailed information in the context of the usual, twice annual, reviews; and
- more frequent examinations by Finance within the context of the budget monitoring processes already in place.

3.11 In relation to the suggestion that Finance seek a Government decision as to whether information on adherence to approved limits should be provided, Finance noted that mechanisms already existed to do this. Under current practice, breaches were detected in twice-annual reviews of approved obligation limits, in the examination of forward estimates and when departments sought additional funds. The breaches thus identified were then taken up either at departmental or Ministerial level, depending on their seriousness. During discussions it was also noted that, in the context of the Cabinet submission following the second

review, Cabinet is regularly presented with information on both actual obligations and the corresponding approved limits. Indeed, it was through this mechanism that Cabinet had been informed of the ACT Commissioner for Housing Loans over-commitments.¹

3.12 Most other responses in the Finance submission were similar to those already reported by Audit. Essentially, Finance referred to that Department's on-going review of the obligations system and to the discussions it had held with a cross-section of other departments within the context of that review.

Other Departments

Breaches Identified by Audit.

3.13 Departments, in which Audit had identified breaches of the forward obligations limits, indicated that these breaches had arisen from inadequate control within the departments themselves, rather than from problems in the obligations system itself.

3.14 The Committee has been advised that steps had been taken to improve control of forward obligations procedures.

3.15 The Department of Aboriginal Affairs advised that:

The Department agrees that the required control was lacking in the instances cited by the Auditor-General ... investigations have revealed that the lack of control stemmed from authorising officers not adhering to prescribed procedures ... The Department has issued a circular to authorising officers reiterating their responsibilities.

3.16 The Department of Local Government and Administrative Services stated in its submission that:

Training has been given in all aspects of estimating funds control ... to officers of all Divisions ... during October-December 1985; it included specific coverage of the forward obligations system and the Auditor-General's criticisms of this Department's administration of it. ... In September 1985 all Divisions were advised formally of Department of Finance approval limits, by appropriation item, for obligations remaining undischarged as at June 30 1986.

3.17 The Department of Territories advised that:

Monitoring of the obligations incurred against

approved limits is now performed ... as part of reporting expenditure and revenue performance. ... details of both the approved forward obligation limit and obligations currently committed have been included in the Department's monthly report (which) is examined by the ... Management Committee and is widely distributed throughout the Department.

3.18 The significant weaknesses identified by Audit in the preparation, recording and control of forward obligations by the Department of Territories appear symptomatic of the numerous financial management problems encountered within this Department over the past two years. For example:

- in 1984, there were significant delays in the preparation by that Department of a number of financial statements for audit report 2;
- in 1985, the Joint Committee of Public Accounts expressed extreme concern at the poor performance of that Department in the preparation of accounts for which it is responsible³; and
- in 1986, Audit expressed concern that, despite gradual improvements, deficiencies in the timeliness and the quality of financial statements of that Department continued to be encountered.⁴

3.19 It is within the context of these general delays and difficulties associated with financial management, that the Audit comments on the administration of forward obligations at Territories should be seen. For example Audit noted that, for 1984-85, estimates of forward obligations for the Department of Territories were formulated by the Department of Finance due to resource constraints and organisational difficulties encountered within the Department of Territories itself.⁵

Relevance of the Forward Obligations System to Overall Budget Strategy

3.20 Most departmental comments focussed on the importance of the forward obligations system to their own financial operations. The Department of Health, however, also discussed the issue of the macro-economic relevance of the forward obligations system. Health noted that:

- about 85 per cent of its expenditures were exempt from the obligations system (including Medical Benefits, Pharmaceutical Benefits, Medicare Grants and salaries);

1. Because of the requirement to find offsetting savings, over-commitments do not necessarily lead to over-spending - see Chapter 4.

2. Auditor-General, September 1984 Report.
3. 241st Report of Joint Committee of Public Accounts, September 1985.
4. Auditor-General, March 1986 Report.
5. Auditor-General, September 1985 Report.

- the forward obligations limits did not reflect the true extent of budget 'lock-ins', because most programs tended to continue; and
- the only function the forward obligations system appeared to have was to prevent departments from committing themselves too heavily in certain 'discretionary' items.

3.21 On the basis of these observations, Health raised the crucial issues of what the objectives of the forward obligations system were, and how well the system was able to meet these. Health also said that, if the initial purpose of the system to indicate and limit the extent of budget 'lock-ins' still held, then consideration would have to be given to an extension of its coverage to most expenditure items. Health noted that the only exemptions should be those items for which there was no danger of 'lock-in'.

Comments on Other Issues Raised by Audit

3.22 Most departments indicated that they had no problems with the existing forward obligations system. They said that they generally complied with the Finance guidelines and had no difficulty in interpreting these. Some, however, said that it would be useful if Finance conducted seminars on all aspects of estimating and funds control.

3.23 A number of departments supported the concept of forward obligations and noted that the system had proved quite valuable as a management tool.⁶ Others were critical of the existing arrangements.⁷ Immigration and Ethnic Affairs, for example, said that monitoring by Finance was minimal and there was little impetus to improve the system. As noted in Chapter 2, similar comments were made by the Department of Local Government and Administrative Services to the Auditor-General. Several departments also noted that records of obligations incurred and approved limits were not always properly maintained by Finance in its Finance Ledger System (FLS). Industry, Technology and Commerce claimed that the issues raised in the Auditor General's reports were important, not only with respect to the management of the forward obligations system itself, but also to Public Service management principles and practices.

3.24 Many departments indicated that they maintained their own separate recording system for forward obligations. The reason most often put forward was the inability of the FLS to provide accurate and effective control of forward obligations.⁸ The Department of Aviation, for example, stated that many of the current difficulties arose because the FLS had not achieved its initially perceived potential.

3.25 Others were of the view that a centralised system, such as an enhanced version of the FLS, would be more effective because it would obviate the need for each department to develop its own subsidiary system.⁹ Community Services, for example, argued that such a centralised system would ensure consistency in data definition and entry and would facilitate the preparation of advice to Government on likely future outlays.

3.26 Most departments were of the view that responsibility for maintaining accurate information on forward obligations and ensuring compliance with Finance Regulations should continue to reside with departmental secretaries. Some, such as Defence and Education, added that it was proper for Finance to continue to exercise an oversight of obligations incurred, within the context of the overall financial control of funds appropriated by Parliament.¹⁰

3.27 It was clear from the submissions that users of the FLS had varying requirements. This was reflected in the suggestions put forward by departments as to changes that should be made.¹¹ A few suggestions were common to many submissions. These included enhancements which would:

- lead to a clearer definition of the objectives of the forward obligations system;
- allow differentiation between limits and obligations incurred for the current year and for future years; and
- allow the recording of limits and obligations incurred below certain sub-account levels.

3.28 Departments noted that suggestions to enhance the FLS system have been put to Finance for some years, but that higher priority work has prevented Finance from accepting such suggestions. As noted earlier, several departments resolved the limitations of the FLS by developing in-house systems.

3.29 On the issue of the timing of the current and forward obligations processes, several departments noted the difficulties associated with the concurrent deadlines for submitting these estimates to the Department of Finance. Some recognised that the obligations and expenditure bids were inextricably linked and sought a short separation of these deadlines.¹² Others suggested a more pronounced separation in the two processes. For example, Health proposed a separate formal requirement to prepare forward obligations following settlement of the budget (no earlier than November, with one review within each financial year).

6. For example Communications, Education and Foreign Affairs.
7. For example Health, Immigration and Ethnic Affairs, Industry, Technology and Commerce.
8. For example Communications, Health, Aviation, Immigration and Ethnic Affairs.

9. For example Trade, Community Services, Industry, Technology and Commerce.
10. The Defence submission made it clear that it did not consider the actual prevention of breaches to be a practical proposition.
11. For example Defence, Communications, Education, Foreign Affairs, Trade, Health and Aviation.
12. For example Defence.

CHAPTER 4

FURTHER INVESTIGATIONS

4.1 The Committee examined the Auditor-General's findings and assessed departments' responses against the broad objectives set for the forward obligations system in 1976. It concluded that many of the problems identified by Audit arose from differing perceptions of the major purpose of the forward obligations system. Because of this, the Committee considered that it was necessary to clarify the objectives of the system and to review the system to ensure that it more clearly responded to present day needs.

4.2 The forward obligations system in its present form has been in existence for ten years, during which important developments in budget monitoring and control techniques took place.

4.3 The Committee was of the view that, only by examining the importance of monitoring to the overall budget process, could the issue of responsibilities for the inadequacies discovered by Audit be resolved. This was also important to assessing whether there was a need for additional reporting to Government. In essence, the more important the forward obligations system to overall budget policy, the greater the need to monitor departmental performance centrally, and to inform Government of significant service-wide over-commitments. In the Committee's view the need to ensure that adequate recording of obligations took place at the departmental level was also important, because central monitoring clearly was not possible if such records did not exist.

4.4 Before developing its conclusions and recommendations, the Committee initiated further investigations in three main areas:

- a clarification of the relative importance of the forward obligation system to departmental managers and to the overall budget process;
- a better understanding of the relationship between forward obligations and other budget planning systems, such as forward estimates; and
- an assessment of how important the breaches (ie commitments in excess of approved limits) identified by Audit were likely to have been within the overall budgetary context.

4.5 In carrying out these investigations, the Committee drew on discussions held with Finance officers and on an additional submission from Treasury. The outcomes of these investigations are summarised below.

Purpose of Forward Obligations

4.6 The essential purpose of the forward obligations system is to allow departments to enter into future commitments in certain expenditure areas. Because the obligations system only concerns already approved purchases of capital items, property or contractual arrangements, the authorisation by the Minister for Finance, or his delegate, of the obligation limits for any one year in the purchasing or contractual cycle would, in most cases, be a formality. This would also be the case in many instances when changes to approved limits are sought, because requests for altering limits are often made in response to changes in government policy.⁴

4.7 The forward obligations system has, in its present form, a coverage different to what was envisaged in 1976. Although the categories of exemptions have remained essentially the same, their significance in total budget outlays has increased considerably. In particular, the proportion of budget outlays covered by standing and special appropriations has risen markedly. As a result, the forward obligations system now covers less than 20 per cent of budget outlays.

4.8 During discussions, it was explained that the reason for the exclusion of most special appropriations was that the corresponding legislations allowed very little flexibility in expenditure control, effectively obligating the relevant expenditure regardless of any departmental action. For example, the legislation relating to unemployment benefits tightly specified weekly rates and the conditions under which the benefits applied. In the case of legislative undertakings, future obligations were generally specified in the relevant Act of Parliament and no further authorisation was necessary.

Relationship with Forward Estimates

4.9 Forward estimates are the main mechanisms through which the extent of budget 'lock-in' is assessed and controlled. The forward estimates cover all budget outlays and incorporate the limits approved under the forward obligations system.²

Significance of Over-Commitments

4.10 As noted in Chapter 2, the Auditor-General found numerous instances in which approved forward obligation limits have been exceeded, in breach of Finance Regulation 44A. The Auditor-General's comments and departments' responses in

1. Information obtained during discussions with Finance.
2. See Department of Finance, Report on Forward Estimates of Budget Outlays and Staffing, 1985-86, 1986-87 and 1987-88, November 1985 and Budget Statements, 1985-86, AGPS, 1985 (p.311).

submissions suggest that failure to maintain adequate departmental records and controls was the main reason why the approved limits have been exceeded.

4.11 The Department of Finance indicated to the Committee that it is general policy within that Department to require offsetting savings in cases of requests for additional funds or increases to forward obligations limits. Finance officers noted that it was usually easier for large departments to find offsetting savings than for smaller units.

4.12 The Department submitted to the Committee several recent budget circulars which re-stated the general principle of offsetting savings. It also provided copies of a number of recent approvals of increases to forward obligations limits, where offsetting savings have been implemented in either the current or in a future financial year.

4.13 In relation to the major overcommitments described in the Auditor-General's report, offsetting savings have been obtained wherever this was appropriate and possible. In the case of the ACT Commissioner for Housing Loans Scheme, the eventual funding deficit for this scheme in 1984-85 was reduced significantly from \$7.9 million to \$1.25 million, with offsetting savings being achieved from elsewhere in the portfolio in the same year. The supplementary Finance submission reproduced in Appendix C provides details of how the offsetting mechanism has worked in the Housing Loans case and in the other cases identified by the Auditor-General during the audit at the Department of Finance itself.

4.14 In the Committee's view, the discipline of having to forego expenditure, in cases where commitments in excess of approved limits had been entered into, should represent an incentive to departmental secretaries to improve control of their forward obligations systems.

4.15 The departments identified by Audit indicated that they took steps to ensure that officers designated for control of forward obligations were aware of their responsibilities and that they acted accordingly (Chapter 3). In addition, several departments advised that they were developing 'in-house' computerised systems to monitor commitments against approved forward obligations limits.

4.16 An analysis prepared by the Department of Finance provides details of departments' in-house computerised systems and their relative importance in terms of their use of the forward obligations system. In particular, the analysis indicates that 13 departments, accounting for some 50 per cent of obligations outstanding at 30 June 1986, had developed or were in the process of developing their own obligations recording

systems. Thus, by the time in-house systems in all 13 departments are completed, around half of forward obligations would be controlled within departments by considerably improved methods. (Appendix C)

Importance to Overall Budget Strategy

4.17 Treasury stated that it did not 'directly utilise the information provided by the Forward obligations system during Budget processes'.¹³ This statement reinforces the general impression gained by the Committee regarding the relative unimportance of forward obligations to overall budget strategy. The issue of whether the Government should be advised of departmental performance against both the original and varied approved obligation limits depends, in the Committee's view, on how important commitments in excess of approved limits are likely to be to the control of overall budget expenditures.

4.18 It was noted in Chapter 2 that the commitments in excess of limits, as reported by Audit in its September 1985 report, amounted to around \$12 million in 1984-85 and \$28 million in 1983-84. During discussions, Finance officers advised that they expected the over-commitments to be somewhat lower in a typical year.

4.19 As noted in the previous section, over-commitments do not necessarily lead to an increase in overall budget outlays, because in many instances departments are able to either partially or fully offset the increases sought in forward obligation limits.

4.20 On the basis of these findings, the Committee formed the judgment that the actual budgetary impact of commitments in excess of approved limits were unlikely to be much higher than \$10 million a year. The Committee also noted that this was small compared with budget outlays which, for 1985-86, were around \$69 billion, and with the budget deficit which, for the same year, was around \$5 billion.

Review by Finance

4.21 In response to the Auditor-General's findings, the Department of Finance initiated an internal review of the forward obligations system. A draft of an options paper prepared for the departmental steering committee has been made available to the Committee on a confidential basis. The paper canvassed six options:

- extend Finance's role to detailed monitoring of departments' performance against approved limits
- enhance Finance's centralised systems support, with focus on data accuracy and uniformity

3. Treasury's supplementary submission.

- delegate powers under Regulation 44A to departmental secretaries, except where obligations have major significance for future budget allocations
- provide more detailed guidelines and assistance to departments in enhancing their own management information systems
- provide departments with global obligation limits, allowing re-allocation of obligations across programs or items
- abolish the forward obligations control system completely, recognising the doubtful usefulness of the system to control budget 'lock-ins'.

4.22 The steering committee's paper discussed the advantages and disadvantages of each option and expressed a preference for the third option.

4.23 The Committee understands that the process to be followed will involve recommendations to be put to the Minister for Finance, following receipt of comments from user departments. Subsequently Cabinet approval will be sought. The Committee was informed that implementation of any new system was unlikely to take place before 1987 or 1988.

CHAPTER 5

CONCLUSIONS AND RECOMMENDATIONS

Conclusions

5.1 The Committee found that the objectives set for forward obligations in 1976, when the system was first introduced, were no longer appropriate.

5.2 Forward obligations are a relatively minor subset of forward estimates. They account for less than 20 per cent of budget outlays.

5.3 The budgetary impact of over-commitments by departments, as reported by the Auditor-General, are likely to be minor. This is partly because the over-commitments are small compared with overall budget outlays and the deficit and partly because, in many cases, departments have been able to find offsetting savings from other appropriations.

5.4 Within the overall budgetary context, it would be possible to integrate forward obligations with the forward estimates processes to a greater extent than at present. However, unlike forward estimates, forward obligations allow for authorisation of future expenditure commitments by departments and this feature makes the obligations system an important management tool at the departmental level.

5.5 The Committee concludes that

- forward obligations are no longer important to overall budget strategy, but are still important at the departmental level.

5.6 The significant developments that occurred in budgetary processes over the past ten years, and the policy of devolution of responsibilities to departmental secretaries, suggest that realigning the forward obligations system with present needs and policies could lead to significant efficiency gains.

5.7 The Committee concludes that

- it is time to review the purpose and the operations of the system within a broader context than that adopted by the Auditor-General in his September 1985 report.

5.8 The Committee notes that the Department of Finance has already initiated an internal review of the forward obligations system and has prepared a draft options paper.

Recommendations

5.9 The Committee recommends that

- the current review, by Finance, of the forward obligations system be expedited.

5.10 Further, it recommends that the new procedures arising from this review:

- specify that the main purpose of the system is to authorise departments to enter into forward commitments in certain expenditure categories;
- limit the extent of monitoring by Finance to those obligations which could have a significant impact on overall budget outlays.

5.11 The Committee recommends that

- in developing the details of the new regulatory arrangements, the policy of greater devolution of responsibility to departmental secretaries be given as much weight as possible. In this context, the Committee considers that monitoring arrangements by Finance which rely on global obligation limits for departments would be preferable to arrangements which monitored obligations at the program level.

5.12 The Committee notes that, under current practice, mechanisms already exist through which Finance can inform Government of significant over-commitments. If the proposed changes to the system are introduced, then the reporting mechanisms - as they now stand - should be sufficient to ensure that significant breaches to approved limits are brought to the Government's notice.

5.13 The Committee is of the view that the forward obligations system is sufficiently important at the departmental level to be retained.

5.14 In this context, the Committee recommends that

- departments rectify the inadequacies identified by Audit in terms of record keeping, monitoring, and control of commitments and expenditures within approved limits.

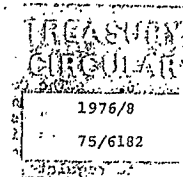
5.15 The Committee sees merit in requiring departments to report in their annual reports breaches to approved obligation limits. This would provide added incentives to improve performance. Nevertheless, the Committee is aware that such a requirement could equally be applied to a whole range of other financial breaches. It considers that the issue of reporting

financial breaches, and the broader question of sanctions, would be more appropriately addressed outside this inquiry. The Committee will examine this issue in detail when it considers a new set of guidelines for preparation of departmental annual reports. These guidelines have been recently referred by the Prime Minister to the Committee for consideration.

APPENDIX A

THE REGULATORY FRAMEWORK

CIRCULAR MEMORANDUM
TO DEPARTMENTS



FORWARD COMMITMENT OF GOVERNMENT EXPENDITURES

The purpose of this Circular is to outline new procedures which the Government has decided should be established for the regulation of expenditure commitments in association with the annual budgetary process and throughout the course of on-going administration.

2. You will, I am sure, appreciate the importance the Government attaches to achievement of its objective of reining in the rate of growth in government spending and reducing the relative size of the government sector. The Prime Minister has emphasised that this is central to the Government's whole economic and social strategy.

3. In practice, what can be done at any time about the rate of growth of government expenditures, at least in the shorter term, depends very much on the extent and nature of commitments already made. In many areas of expenditure, budget allocations for a new financial year, and sometimes for years beyond it, can be largely pre-determined by commitments made before that year begins.

4. For control of expenditure, the commitment stage is a decisive one.

5. In this context commitments are to be taken to include not only legislative undertakings but also actions falling within the area of Executive power such as the signing of contracts for buildings or supplies or the entering into of other agreements or undertakings which, while they may not create legally enforceable claims, will obligate the Government to the payment of moneys.

6. The Government has decided that, for budget planning purposes, and to assist it in its task of expenditure control, it should have available to it, when it is considering its budget options, comprehensive information on both existing and proposed commitments and should be enabled to regulate, in a systematic way and consistently with its overall budget strategy, the extent to which commitments that would require future budget allocations might be made.

7. The set of procedures now to be instituted is designed to meet these requirements without imposing unwarranted constraints on departments and authorities in the performance of their respective functions.

8. The central feature of the new procedures is the application across the broad range of budget expenditures of a forward programming system, similar in broad concept to systematic arrangements which have been built up over the years in respect of the Civil Works Program and certain other categories of expenditure, under which existing and proposed commitments will be identified and considered at the same time as cash allocations for the emergent financial year are being determined by the Government.

9. This forward programming system is to be applied in the budget-making process for 1976-77 and subsequent years. For 1976-77 this will mean that departments and relevant authorities must provide, by 19 May 1976, basic information listed below in respect of every expenditure bid (except certain specified categories which I shall mention later):-

- (a) the total value of commitments which it is estimated will remain undischarged at the end of 1975-76;
- (b) the total value of new commitments (or variations to currently approved commitments proposed) to be made during 1976-77;
- (c) the total of the proposed commitment program - i.e., (a) and (b);
- (d) the expenditure bids for 1976-77 - i.e., the appropriations required; and
- (e) the estimated total value of commitments which will not be discharged at the end of 1976-77 and for which appropriations will be sought in subsequent years, indicating the expected financial year of maturity.

Similar information will be required in connection with the submission of draft estimates for subsequent financial years.

10. For orderly presentation to Cabinet of relevant commitment figures in association with bids for cash (appropriations), as part of the regular budgetary processes each year, there will need to be discussions on these figures between the Treasury and each department and relevant authority before Cabinet's examination of the Budget proposals.

11. It should be noted that, to meet Cabinet's requirements for comprehensive information, this forward commitment programming system will apply not only to commitments of expenditures financed by means of annual appropriations but also to commitments for expenditure from special appropriations, other than in cases where the amounts and timing of the expenditure are firmly pre-determined by the provisions of the relevant legislation.

12. The Government has also decided that this comprehensive forward commitment programming system should extend to those commitments of statutory authorities that might lead to a request for the provision of funds from the Budget. The Treasurer will be consulting with the responsible Minister on the particular manner of its application, in the light of provisions of the specific legislation under which the authority operates, in respect of each relevant authority.

13. There is provision for the exemption of certain appropriations from this general system. At the outset, the following, in addition to the class of special appropriations referred to in paragraph 11 above, will be exempted:-

- (a) Salaries and allowances;
- (b) Overtime;
- (c) Travelling and subsistence; and
- (d) Postage, telegrams and telephone expenses.

Other categories may be exempted upon further examination or after consideration of a specific request by a department. In all cases fully justified estimates of cash (appropriation) requirements are to be submitted to the Treasury, as at present.

14. Commitment approval will not be necessary for on-going commitments at existing rates and levels of activity in respect of the expenditure categories listed in paragraph 13. However, it is important to note that proper financial management of all these expenditures requires

that, if funds additional to an existing budget allocation are needed in the current year (or, if not for the current year, for future years), to meet rate and tariff increases or levels of activity higher than envisaged when Cabinet approved the budget allocation, approval to anticipate the provision of such funds be sought.

15. The introduction of the new forward commitment programming system will not remove or diminish established procedures which require Cabinet or Treasurer's approval for particular commitments including the procedures relating to the Defence Program, the Civil Works Program, etc. Nor will the system replace or in any way detract from the requirement for forward estimates. On the contrary it is expected that, by clearly identifying the extent of forward commitments made against the appropriations of future years, an improved basis will emerge for the compilation of forward estimates of on-going expenditure programs.

16. As part of the budget-making process, Cabinet will consider both the cash and commitment proposals submitted by departments and relevant authorities. Budget allocations for the current year will appear in the Appropriation Bills or other documents tabled in Parliament on Budget night. As soon as the Budget is introduced, departments and relevant authorities will be advised of the limits approved by Cabinet within which they should contain relevant commitments which they might have outstanding at the end of the financial year for funding in future financial years. They will then be authorised, subject to any qualifications that may be laid down by Cabinet or by the Treasurer, to enter into commitments within these Cabinet approved limits without the need for further specific approvals (except where such approvals are required in particular cases by established procedures of the kinds referred to in paragraph 15 above).

17. Prior approval by Cabinet or by the Treasurer will be required before any commitment is made which would result in an approved limit, either for the current year (appropriations) or for carryover of commitments at the end of that year, being exceeded. In this regard I should emphasise that before requests for approval of increased limits are brought forward all possibilities for substitution of one project or activity for another within the limits set should have been examined.

18. To facilitate commitment action by departments and relevant authorities Cabinet has also authorised "blanket" approvals for the entering of commitments to be funded from the Supply Acts and the Budget Appropriations as outlined below:-

(a) Cabinet has authorised that, as soon as the Supply Bills are introduced into Parliament, departments and relevant authorities may make commitments to be funded wholly from proposed 1976-77 Supply appropriations. It is expected that similar "blanket" approvals in relation to Supply appropriations in future years will be given. If it is necessary to commit against Supply appropriations prior to the introduction of Supply Bills for 1976-77, and approval of Cabinet or the Treasurer of the commitment has not already been given, the Treasurer's approval should be sought by application to the Secretary to the Treasury; and

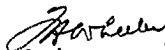
(b) Cabinet has also authorised that departments and relevant authorities may make, without the need for further approval, commitments to be funded wholly from proposed 1976-77 Appropriation Act appropriations as soon as the Appropriation Bills are introduced into Parliament. Where departments or relevant authorities need to make commitments against funds to be provided in the 1976-77 Appropriation Bills before the relevant Bills are introduced into Parliament, and approval of Cabinet or the Treasurer for those commitments has not already been given, the Treasurer's approval should be sought by application to the Secretary to the Treasury.

These "blanket" authorisations are also subject to any qualifications that may be laid down by Cabinet or by the Treasurer and will not obviate the need to obtain specific approval where this is required in particular cases under established procedures as mentioned in paragraph 15 above.

19. During the period up to the introduction of the 1976-77 Budget the arrangements for approval of commitments will, in the case of your Department and any authorities for which your Minister is responsible, be as set out in the Treasurer's letter of 4 Mar 1976 to your Minister, as amended by any subsequent decisions by Cabinet or the Treasurer, including the prospective "blanket" approval, referred to in paragraph 18(a) above. This "blanket" approval will be available in respect of commitments to be funded from the proposed appropriations in the next Supply Bills as from the time those Bills are introduced.

20. The implementation of the new procedures will not mean that there will be any material change in the manner in which appropriations are supplemented, as necessary, from the Advances to the Treasurer. Applications for forward commitment approvals should specify whether and, if so, to what extent Treasurer's Advance funds will be required (in so far as this is known) and separate application then made for Warrant Authority as necessary.

21. I look forward to the co-operation of departments and authorities in bringing in these new procedures in a way which will be of mutual advantage. Any questions in relation to the operation of the new system should be directed to Mr J.L. Griffin, telephone 632513.



F.H. Wheeler
Secretary to the Treasury
14 Apr 1976

A2 Finance Regulation 44A (1980)

PART IIA—OBLIGATIONS INVOLVING EXPENDITURE OF PUBLIC MONEYS

- 44A. (1.) Subject to sub-regulation (2), an officer shall not incur, on behalf of, or for the purposes of, the Commonwealth, an obligation involving expenditure of public moneys, being an obligation in respect of—
- (a) the execution of works or the supply of services for or by the Commonwealth; or
 - (b) the purchase of chattels or other property for or by the Commonwealth,
- unless—
- (c) where a payment in connection with the obligation would be required to be made during the financial year that is current when the obligation is incurred—
 - (i) moneys have been appropriated under a head of expenditure in an Appropriation Act for that financial year that are sufficient to meet the payment and all other payments that have been met, or may reasonably be expected to be met during that financial year, from that head of expenditure;
 - (ii) provision for such an appropriation has been included in a proposed law submitted to the Parliament; or
 - (iii) the Minister has given his approval to the obligation being incurred; and
 - (d) where a payment in connection with the obligation would be required to be made after the end of the financial year that is current when the obligation is incurred—
 - (i) approval has been given by the Minister for the payment to be met from moneys to be appropriated for the service of, or for specified expenditure in respect of, such financial year as the Minister specifies; or
 - (ii) the obligation is specified in, or is included in a class of obligations that is specified in, a declaration made by the Minister under sub-regulation (3.).
- (2.) Sub-regulation (1.) does not apply in relation to an obligation of a kind referred to in that sub-regulation if the obligation is incurred in pursuance of the provisions of an enactment authorizing the incurring of the obligation.
- (3.) The Minister may, by instrument in writing, declare, in relation to an obligation of a kind referred to in sub-regulation (1) that is specified in, or is included in a class of obligations specified in, the instrument, that any payment in connection with the obligation, being a payment that is to be made after the end of the financial year that is current when the obligation is incurred, may be made without the approval of the Minister referred to in sub-paragraph (1) (d) (i) in relation to the payment being obtained.

CHAPTER 7

FORWARD OBLIGATIONS IN RESPECT OF GOVERNMENT EXPENDITURES

7.1 The Commonwealth system of financial management requires, as does the United Kingdom system, the Parliament to appropriate any public moneys needed for the purposes of the Commonwealth (Constitution, section 83). There is, however, no requirement similar to that in the United States of America whereby legislative authority must also be obtained before the Executive Government may enter into an obligation. Nevertheless, there is a requirement under Finance Regulation 44A made pursuant to the provisions of the Audit Act, reinforced by Government decision in respect of obligations not covered by that Regulation that an officer shall not incur an obligation on behalf of the Commonwealth unless provision for an appropriation has been made or proposed, or unless the Minister for Finance has given approval.

7.2 In many areas of government activity, budget allocations for a new financial year, and sometimes for years beyond it, can have been largely predetermined by obligations entered into before that year began. In this context obligations will include not only undertakings arising through specific legislation but also actions falling within the area of executive power, such as the signing of contracts for buildings or supplies or the entering into of other agreements for undertakings which, while they may not create legally enforceable claims, will obligate the Government to the payment of moneys.

7.3 For budget planning purposes, and to assist in maintaining expenditure control, procedures have been instituted to provide the Government with comprehensive information on existing and proposed obligations. The central feature of the procedures is the application across the broad range of budget expenditures of a forward planning system, similar in concept to arrangements in respect of the Civil Works Program, under which existing and proposed obligations are identified, considered and approved by the Government at the same time as cash (i.e. Budget) allocations for the emergent financial year are being determined.

7.4 To meet the requirement for comprehensive information, the forward programming system applies not only to obligations to be financed from annual appropriations of departments but also to those to be financed from special appropriations - other than in cases where the amounts and timing of the expenditure are firmly predetermined by the provisions of the relevant legislation.

7.5 The procedures also extend to obligations of statutory authorities operating within the Commonwealth Public Account and, where the obligation might lead to a request for the provision of funds from the Budget, to those operating outside the Public Account.

7.6 As soon as the Budget is introduced, departments and authorities are advised of the limits approved by the Government within which they should contain obligations which they consider will be outstanding at the end of the financial year for funding in future financial years. Subject to any special qualifications laid down by Cabinet or the Minister for Finance, and to the observance of established procedures relating to, for example, the Civil Works Program, Defence Program etc, departments may then enter into obligations up to the limits approved by the Government without further specific approvals.

7.7 Prior approval of the Minister for Finance is required before an obligation is entered into which would result in approved obligation limits being exceeded in respect of matters covered by Finance Regulation 44A, ie:

- the execution of works or the supply of services for or by the Commonwealth; or
- the purchase of chattels or other property for or by the Commonwealth.

7.8 In respect of obligations outside the scope of Finance Regulation 44A, eg. grants, loans and guarantees, prior approval of Cabinet or the Minister for Finance is required.

7.9 General exemptions from the system have been granted to obligations in respect of salaries and allowances, overtime, travelling and subsistence, postage, telegrams and telephone expenses. Exemptions have also been granted in respect of particular appropriations where it was considered appropriate because of the nature of the expenditure, other existing controls etc. Applications by departments for exemptions are considered on their merits.

APPENDIX B

LIST OF DEPARTMENTAL SUBMISSIONS

LIST OF DEPARTMENTAL SUBMISSIONS

DEPARTMENT	SUBMISSION	
	REQUESTED	RECEIVED
1. Aboriginal Affairs	X	X
2. Arts, Heritage and Environment	X	X
3. Attorney General	X	X
4. Aust Development Assistance Bureau	X	X
5. Aviation	X	X
6. Communications	X	X
7. Community Services	X	X
8. Defence	X	X
9. Education	X	X
10. Employment and Industrial Relations	X	X
11. Finance	X	X
12. Foreign affairs	X	X
13. Health	X	X
14. Housing and Construction	X	X
15. Immigration and Ethnic Affairs	X	X
16. Industry Technology and Commerce	X	X
17. Local Government and Admin Services	X	X
18. Primary Industry	X	X
19. Prime Minister and Cabinet	X	X
20. Public Service Board	X	X
21. Resources and Energy	X	X
22. Science	X	X
23. Social Security	X	X
24. Special Minister of State*	X	-
25. Sport Recreation and Tourism	X	X
26. Territories	X	X
27. Trade	X	X
28. Transport	X	X
29. Treasury	X	X
30. Veterans Affairs	X	X

* The Department of Special Minister of State advised that it only had a minimum involvement with forward obligations and, because of this, it did not forward a submission to the Committee.

APPENDIX C

ADDITIONAL MATERIAL SUBMITTED BY THE

DEPARTMENT OF FINANCE

C1 Offsetting Savings

As noted in discussions with the Committee Secretariat, the requirement for offsetting savings is a general budgetary guideline that is applied in respect of requests for additional funding but only applies in relation to ~~current~~ year allocations and associated obligation limits. Approvals for increases in ~~forward~~ obligation limits are normally qualified with a requirement that they be a first charge against funds provided under the relative appropriation in the relevant financial year thus ensuring that departments/agencies address priorities in submitting forward obligation proposals.

In its examination of Finance records Audit noted "... the Department was committed to approve large increases to obligation limits/appropriations as a result of deficiencies in the operation of the forward obligation control system. These were:

- the 1984-85 appropriation for the ACT Commissioner for Housing Loans Scheme had to be increased by \$7.9 million because commitments had been entered into in 1983-84 without forward obligation approval;
- although the approved forward obligation limit as at 30 June 1984 for the Community Employment Program administered by the Department of Employment and Industrial Relations was \$266 million, the actual amount of obligations carried forward from 30 June was \$283.2 million; and
- in 1983-84 the Department of Aviation received Department of Finance approval for the commitment involved in a 4 year airport cleaning contract, totalling \$11.25 million, after the contract had been approved and notified in the Australian Government Gazette. It is understood that similar contracts had existed in the past but had not been included in the Department's forward obligations estimates ..."

In respect of the ACT Commissioner for Housing Loan Schemes:

- This breach was identified in the first instance by Finance, in early July 1984, through its normal oversight and monitoring role in relation to forward obligations.
- The original estimated funding deficit was identified as \$7.9 million. The Government agreed to provide additional funds in 1984-85 and, following a recommendation by Finance, made the additional funds subject to the achievement of full offsetting savings from elsewhere within the portfolio.
- The Auditor-General was requested by the Minister for Finance to carry out a special audit of the operation of the ACT Commissioner for Housing Loans Scheme.

In the event, the funding deficit for the Scheme in 1984-85 was only \$1.25 million (compared with the original estimate of \$7.9 million) for which offsetting savings of \$1.067 million were achieved from elsewhere within the portfolio.

In relation to the breach identified in the operation of the Community Employment Program, this was also identified in the first instance by Finance (on 8 June 1984) through existing procedures for the monitoring of obligations entered into against approved limits. It was considered inappropriate in this instance to impose a requirement for offsetting savings because:

- (a) the breach occurred in a forward obligation limit (1984-85) rather than the obligation limit for the current (1983-84) financial year; and
- (b) the breach effectively had no impact on budgetary flexibility in future years (ie 1984-85) as the Government had, in advance of the breach, agreed to a funding level in 1984-85 (\$410 million) of significantly greater magnitude than the obligations which had been entered into in 1983-84 in respect of 1984-85 (\$283 million). In other words, the breach (\$17.2 million) was absorbed within (or became a first charge against) the ongoing funding level for the program.

The 'breach' in respect of Department of Aviation cleaning contracts was also identified by Finance in the first instance. The issue was in the nature of a 'technical breach' in that the contract, having been entered into prior to obligation approval being given, resulted from an oversight on the part of both Finance and Aviation in not including estimates for this item in the proposed limits approved by the Government in August 1984. Once identified, approval of the Minister for Finance to the obligation was obtained.

It was not considered appropriate in this instance to impose any sanction in the nature of offsetting savings as:

- (a) the obligation concerned related to ongoing cleaning contracts that had been in existence for sometime and extended over a number of years into the future; and
- (b) the nature of the breach was such that had the amounts been included within the Department's original obligation estimates they would have been fully supported and recommended for approval by Finance.

C2 Devolution of Responsibilities to Departments

The principle of devolution of responsibility to departmental Secretaries was embodied in the Parliament's amendments to the Audit Act in 1979 (Section 2AB) (see Attachment A) and in recent public service and budget reforms initiated by the Government. These principles were summarised in the Government policy paper entitled 'Budget Reform' in April 1984. Briefly, the document outlined a number of initiatives which the Government was either currently implementing or intended implementing with a view to improving the efficiency and effectiveness of financial management in the Australian Public Service. Generally, the reforms outlined reflect on the view that the provision of appropriate incentives to departmental managers, including greater flexibility in the management of the resources for which they have responsibility, will encourage improved performance. The quid pro quo for this increased flexibility is more stringent (cash) limits on aggregate expenditure and the provision of information to the Government and Parliament which gives a better indication of what is achieved with funds appropriated. The latter is the focus of Program Budgeting.

(4) Where an amount payable out of or into a Fund in relation to which this section applies has been lawfully set off against an amount payable into or out of the same or another Fund in relation to which this section applies and, by reason of the set-off, no amounts are payable out of or into those Funds, the amounts that, but for the set-off, would have been paid out of or into those Funds shall, for the purposes of this Act, be deemed to have been so paid at the time when the set-off took place.

Application of Act
Inserted by
No. 49, 1961,
L 4
Sub-section (1)
amended by
No. 216, 1971,
L 3; No. 8, 1978,
L 4

2A. (1) This Act extends to every Territory, but does not apply to or in relation to revenues, moneys or stores of the Northern Territory or an external Territory or the operations of the administration of, or persons in the service of, the Northern Territory or an external Territory in relation to the receipt, expenditure or control of any such revenues, moneys or stores.

Substituted by
No. 8, 1978, L 4

(2) Subject to any modifications and exceptions specified in regulations made in pursuance of section 63 or 63A, this Act applies outside Australia and the Territories to and in relation to every person who is or has been an officer, whether or not he is an Australian citizen, and the functions, powers, duties and responsibilities conferred or imposed by this Act on the Minister, the Auditor-General and other specified persons and authorities in relation to persons who are or have been officers, and in relation to public moneys and other matters, are exercisable or shall be performed accordingly.

(3) The provisions of this Act do not apply to or in relation to affairs and transactions (including the receipt or expenditure of money) in relation to the Parliamentary Refreshment Rooms except affairs or transactions involving the expenditure of moneys for the purpose of which the Consolidated Revenue Fund has been appropriated.

Responsibilities of Permanent Heads
Inserted by
No. 8, 1978, L 3

2AB. (1) The Permanent Head of a Department is responsible for making appropriate arrangements for implementing the provisions of this Act, the regulations and any directions given under this Act or under the regulations in relation to the Department.

(2) In sub-section (1)—

“Department” means—

- (a) a Department of State;
- (b) a Department of the Parliament; or
- (c) a branch or part of the Australian Public Service in relation to which a person has, under an Act, the powers of, or exercisable by, the Permanent Head of a Department of the Australian Public Service;

“2AB”

“Permanent Head” means—

- (a) in relation to a Department of State or a Department of the Parliament—the person who, under the *Public Service Act 1922*, holds, or is performing the duties of, the office of Permanent Head of that Department; or
- (b) in relation to a branch or part of the Australian Public Service referred to in paragraph (c) of the definition of “Department” in this sub-section—the person who has the powers of, or exercisable by, the Permanent Head of a Department of the Australian Public Service so far as those powers relate to that branch or part of that Service.

C3 Departments_Obligation_Recording_Systems

Departments' submissions to the JCPA and the views of a cross section of departments proffered in the context of a survey conducted by Finance during the course of its Review of the Obligations System indicate a significant number of departments that have developed or are in the process of developing their own computerised systems for the monitoring of progress against approved forward obligation limits.

Attachment B presents details as to where Commonwealth departments are in respect of this type of systems development. Importantly, the table indicates that 14 departments accounting for some 50% of obligations outstanding at 30 June 1986, had developed or were in the process of developing their own obligations recording systems to meet individual program requirements.

ATTACHMENT B

DEPARTMENT	Percentage of total Obligations Outstanding at 30.6.86	Departments that have Developed their own Systems	Departments that intend to develop their own Systems	JCPA Submission Reference
Parliamentary Depts	-			
Aboriginal Affairs	0.5			
Arts Heritage and Environment	0.3		X	Para 7
Attorney-General's	0.1		X	Para 6
Aviation	1.7		X	Para 6
Communications	1.6		X	Para 4
Community Services	1.5			
Defence	41.4			
Education	6.0	X		Para 3
Employment and Industrial Relations	2.0	X		Para 2
Finance	-			
Foreign Affairs	19.7		X	Para 2
Health	3.4		X	Para 9
Housing and Construction	5.0	X		Para 4.4.1
Immigration and Ethnic Affairs	0.3		X	Para 3.18
Industry, Technology and Commerce	0.9	X		Para 2
Local Government and Administrative Services	5.5			
Primary Industry	0.4			
Prime Minister & Cabinet	-			
Resources and Energy	0.8			
Science	1.0			
Social Security	0.3		X	Para iii (6)
Special Minister of State	0.1			
Sport Recreation and Tourism	0.1			
Territories	5.6		X	Para 5
Trade	1.0			
Transport	-			
Treasury	0.6			
Veterans Affairs	0.1			
	----	----	----	
Total	100	13.9%	33.0	
	----	----	----	

46.2

C4 An Alternative Forward Obligation System

[Note: in this section the Department of Finance refers to the Draft Options Paper prepared by its Obligations Steering Committee]

Remodelling of the obligations system along the lines of option 3 of the Steering Committee's draft options paper would result in the same proportion of outlays being subject to some form of forward obligation approval process as is currently the case (ie around 20 per cent of Budget outlays).

The procedures envisaged in option 3 differ from current practice with respect to where forward obligation control would be exercised viz:

- centrally (Cabinet, Minister for Finance or Department of Finance);
- departmentally; or
- through other budgetary processes.

As indicated in the draft options paper provided to the Committee Secretariat, consistent with the redefined objectives of the obligations system it is intended that, under option 3, a centralised system of approvals would be maintained but refined to apply only to those programs/items where obligations entered into have major significance for future budgetary allocations/future budgetary flexibility. The central system would exclude those obligations that are likely to have minimal impact on future budget allocations (responsibility for approving these limits would be devolved to departmental Secretaries) and would also exclude those programs/items whose obligations are separately and explicitly regulated by other formal budgetary control procedures (eg Civil Works, Repairs and Maintenance).

Compared with the existing obligations system which covers around 20 per cent of budget outlays, it is envisaged that under Option 3, 17 per cent of budget outlays would continue to be subject to obligation control centrally or through other budgetary processes. Obligation control in respect of the remaining 3 per cent of outlays would be devolved to departmental Secretaries. However, it is estimated that the 17 per cent of budget outlays referred to above would comprise only 30 per cent of the appropriation items presently subject to obligation procedures. Whereas the 3 per cent of budget outlays, obligation control for which would be devolved to departmental Secretaries, would include around 70 per cent of appropriation items subject to existing obligation procedures.

In other words, the option has its basis in the view that Finance and Cabinet should not be focussing unnecessarily on a wide range of relatively minor items which will have little or no impact upon future appropriations.