

The Parliament of the Commonwealth of Australia

Efficiency Audit Review:

**The National Highway
'Lifeline of the Nation'**

**Report from the House of Representatives
Standing Committee on Transport,
Communications and Infrastructure**

November 1994

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HOUSE OF REPRESENTATIVES STANDING COMMITTEE
ON TRANSPORT, COMMUNICATIONS
AND INFRASTRUCTURE

(37TH PARLIAMENT)

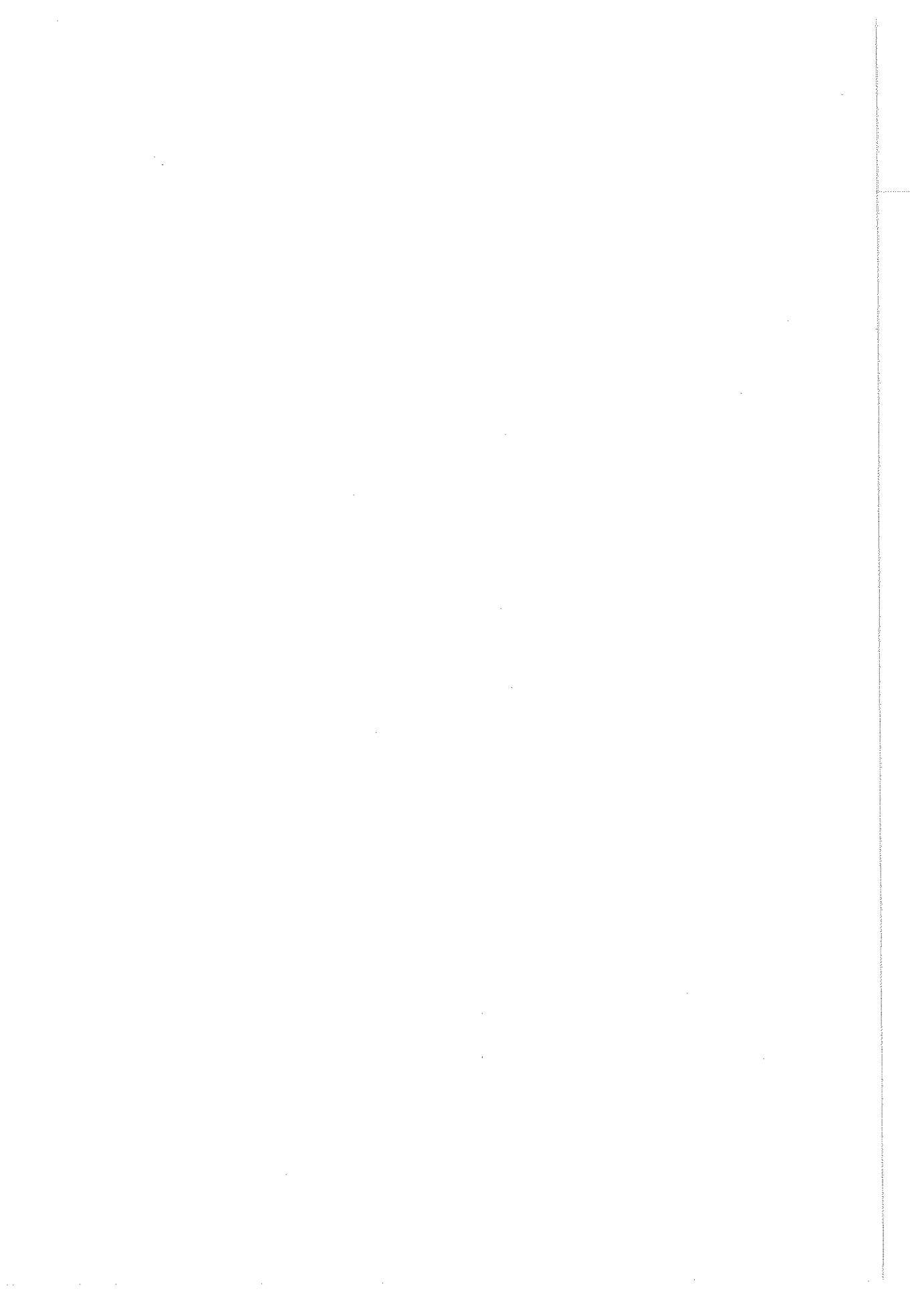
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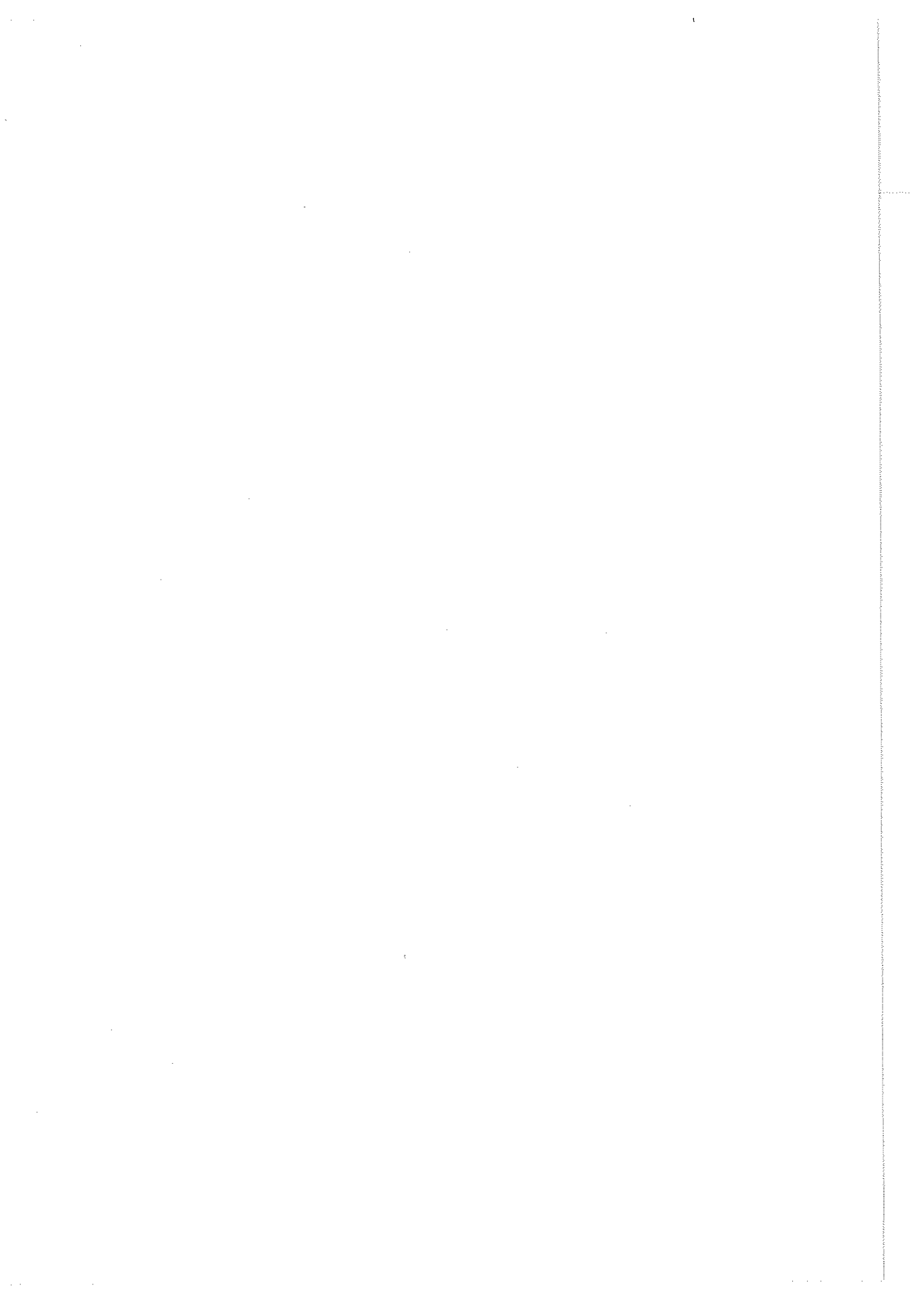
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OVERVIEW

1. This report looks at areas of contention between the Department of Transport and the Australian National Audit Office which arose following an efficiency audit of the management of the National Highway System.

2. The areas of contention are:

- . more rigorous matching of payments to reporting of progress
- . incentives to reduce costs
- . multi year works programs and national prioritisation of works
- . improved accountability of state authorities
- . improved project progress monitoring and quality systems.

3. The report examines only these issues.

4. It became evident during the committee's inquiry that the Department of Transport and the Australian National Audit Office have reached at least some form of agreement in most of these areas.

5. The commonwealth government intends to introduce the new national highway management program legislation in parliament early in 1995. New measures included in the legislation are:

- . improved information collection and performance monitoring systems
- . enhanced project monitoring
- . the introduction of performance indicator and performance agreements with state authorities.

6. The committee believes that recent improvements in the management system and the changes to be introduced in the new legislation will ensure that the national highway is managed.

CHAPTER 1

Introduction

Terms of reference and conduct of the inquiry

1.1 The Australian National Audit Office tabled Audit Report No.15 1993-94, The National Highway, 'Lifeline of the Nation' in parliament on 3 December 1993. The report was referred to the House of Representatives Standing Committee on Transport, Communications and Infrastructure by the House of Representatives on 13 December 1993.

1.2 Submissions were sought and received from the Department of Transport (DOT) and the Australian National Audit Office (ANAO). These submissions are at Appendix 1.

1.3 The committee took evidence at a public hearing in Canberra on 10 November at which the Department of Transport and the Australian National Audit Office appeared. Details of those who appeared are at Appendix 3.

Scope of Inquiry

1.4 The report is narrowly focused on the administration of the National Highway System (NHS). Specifically, it focuses on those administrative areas where ANAO and DOT disagree. There are five areas of contention identified in the DOT response to the ANAO report. These are:

- . more rigorous matching of payments to reporting of progress
- . incentives to reduce costs
- . multi year works programs and national prioritisation of works
- . improved accountability of state authorities
- . improved project progress monitoring and quality systems.

1.5 This report examines these topics only.

Recent history of the management of the National Highway System

1.6 Many improvements have been made to the NHS during the life of the *Australian Land Transport Development Act (ALTD)* program. These include:

- . the complete sealing of the NHS
- . the nearly complete duplication of the Sydney - Melbourne link
- . significant improvements in the Brisbane - Cairns and Hobart - Launceston links
- . the construction of the Sydney - Newcastle link
- . the reconstruction and widening of large sections of highway in Western Australia, South Australia and Queensland
- . the addition of the Adelaide - Sydney and Brisbane - Melbourne links to the national highway network.

1.7 It should also be pointed out that the 'construction and reconstruction of (Australian) rural highways and main roads is equal to or less than that reported for similar roads overseas.' (Kneebone;1993:11) This suggests that most national highway projects have been constructed efficiently.

1.8 The management program under which these improvements were made has changed. At the 1991 Heads of Government meeting in Brisbane the federal and state governments agreed to clearly define road funding and management responsibilities. As a result of this meeting the commonwealth government will only fund the National Highway System (NHS). Ownership of the NHS remains with the states. The commonwealth government will no longer fund any other type of road.

1.9 These new funding and management arrangements took effect from 1 January 1994. In the lead up to this date the Department of Transport was developing a new management program to cater for the

administrative arrangements required to properly manage the National Highway System. It was during this transitional period that the audit of the management of the National Highway System was undertaken by the Australian National Audit Office.

1.10 Provisions which cater for the new management system are included in proposed amendments to the existing *Australian Land Transport Development Act 1990 (ALTD)*. The government intends to introduce the legislation in the first half of 1995 so that the amendments would take effect from 1 July 1995.

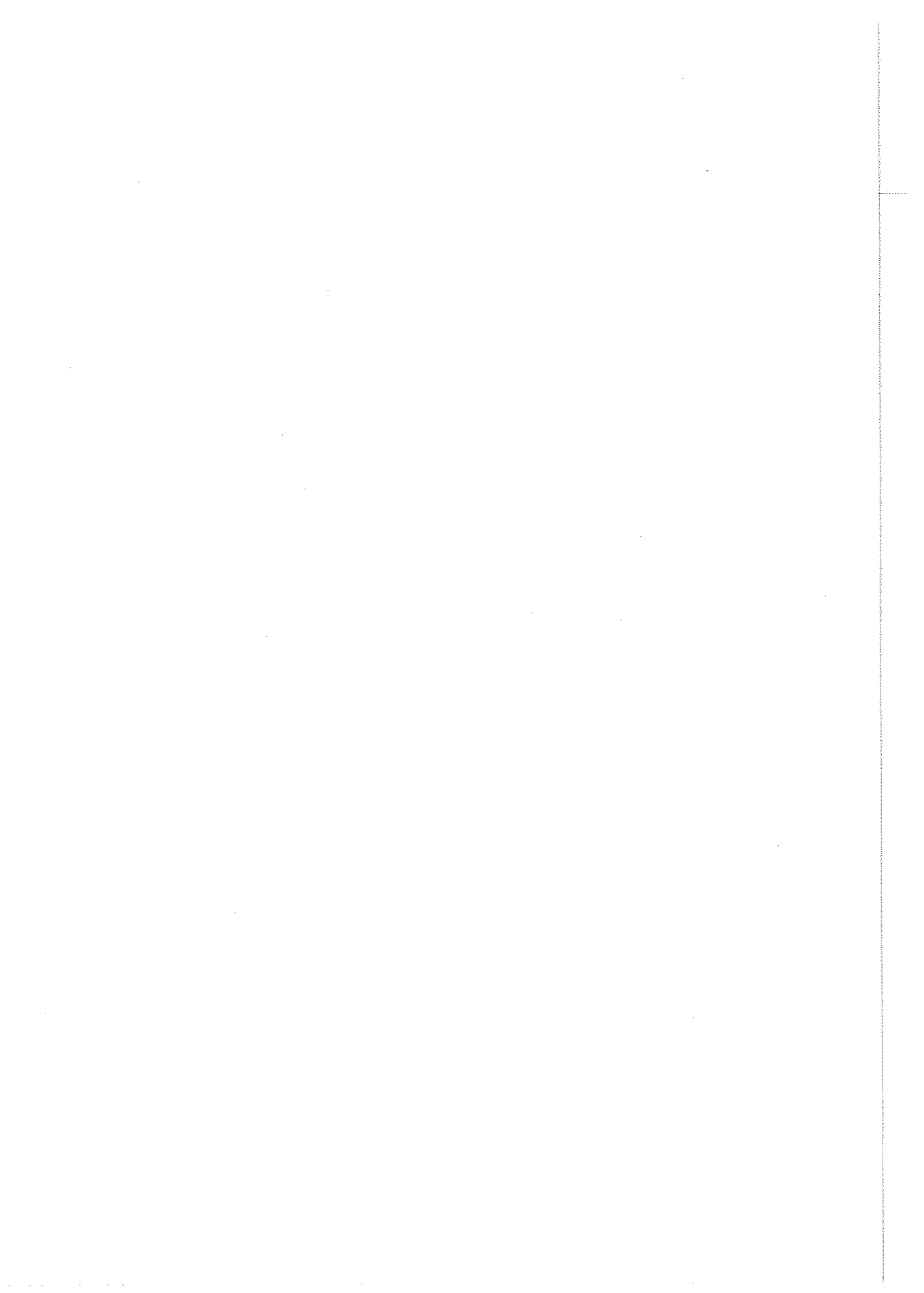
1.11 It is clear to the committee that many of the 33 recommendations in the audit report were considered by DOT in the development of the new management system to be outlined in the new legislation. Many of ANAO's recommendations have now been implemented, are being implemented or are being considered for implementation.

1.12 In this report the committee will focus on the suitability of the current management program for the NHS. The committee did not consider past administration of the National Highway System.

Structure of report

1.13 Chapter 2 of the report examines each of the administrative issues identified by the Department of Transport as being in contention with the Australian National Audit Office.

1.14 Chapter 3 outlines the committee's conclusions.



CHAPTER 2

Issues in contention

More rigorous matching of payments to reporting of progress

2.1 The Department of Transport (DOT) has restructured its system of payments to the states. The monthly payment system which was trialled has been discontinued. Under the new program each state reports actual and expected expenditure on approved projects each month. The state receives only those funds '...it will reasonably need to meet expected costs to the middle of the following month. This means that the state has an average of two weeks credit at any time.' (DOT submission:Attachment B). States gain an interest benefit from this two week credit period.

2.2 Australian National Audit Office have calculated the interest benefit to the states to be approximately \$1m per year (ANAO submission:1).The ANAO would prefer that interest benefits be eliminated. However, ANAO agrees with the changes which have been made to the payments system to reduce the interest benefit to the states (Transcript:13).

2.3 Both DOT and ANAO believe that there needs to be a balance between the interest benefits to the states and the need for efficient cash management by the commonwealth government. Under the current administrative program the committee feels that the system is satisfactory.

2.4 Of concern to the ANAO is the financial reporting by state governments of their commonwealth government road expenditure. Under the *Australian Land Transport Development Act (ALTD)* state Auditors-General are required to submit financial statements indicating what funds have been spent on roads and those that have been set aside but not expended during the year (ANAO submission:1).

2.5 The ANAO stated that this requirement is not being met. It states that some reports contain very little information and that there is little consistency between the information contained in the various state reports (ANAO;1993:41,42).

2.6 DOT maintains that it will implement the ANAO recommendation if the requirements of the state Auditors-General are amended in the new legislation which is soon to be considered by parliament (DOT submission; Attachment C:2).

2.7 DOT have advised the committee that changes to reporting requirements is unlikely. If in the future, the reporting requirements of state Auditors-General become a problem DOT will re examine the issue (Transcript:20).

Incentives to reduce costs

General administration costs

2.8 DOT advise that under the current program payments will only be made on the basis of detailed proposals on how much is expected to be spent in the following areas:

- . road data - collection, storage and transmission of information about NHS roads
- . project progress - monitoring and reporting on construction progress, cash flows and cost estimates
- . strategy development - assessment of future construction and maintenance needs
- . quality assurance - monitoring and reporting of quality assurance programs
- . network management - management of maintenance and construction programs
- . auditing of financial statements required by the commonwealth (DOT submission:2).

2.9 Under the new program administration costs incurred on a project must be included in the cost of that project and must not be paid from general administration funds.

2.10 ANAO assert that DOT has not gone far enough with the new program. ANAO suggest that all claims should be in a form which permits interstate comparison and performance measurement (ANAO submission:2.1).

2.11 DOT has advised the committee that the development of management programs through the NHS strategy study will ensure that data collected from the states is comparable (Transcript:34).

Asset preservation costs

2.12 Under DOT's current program all maintenance work other than routine work, such as grass cutting, line marking or drain clearing, will go to tender (DOT submission; Attachment B:1).

2.13 ANAO claim that DOT have adopted the wrong approach and should be adopting a 'life cycle' costing approach. This approach would put an emphasis on which maintenance tasks are undertaken rather than how they are undertaken. The objective being to ensure that the right maintenance tasks are undertaken to preserve the road asset (ANAO submission:2.2).

2.14 DOT claim that ANAO's concerns will be met in the National Highway Strategy Study which is currently being undertaken (see paragraphs 2.24-2.26).

Use of savings

2.15 Under the current arrangements a state may redirect to other projects any savings gained where a project is completed under budget. The current program allows states to spend savings on:

- contingency claims (previous overspends)
- costs of additional maintenance work
- acceleration of works listed in 1994-95 NH program
- other projects agreed by the minister (DOT submission: Attachment B:2).

2.16 DOT argue that allowing states to keep project savings is a powerful incentive for project costs to be kept to the absolute minimum.

2.17 The ANAO disagrees with this practice. ANAO states that if the benefit/cost based priority project selection system is to work effectively surplus funds should be returned to the national pool for re allocation to the next priority projects. These projects may not be in the state which makes the saving (ANAO submission:2.3).

2.18 At the public hearing on 10 November ANAO agreed that the benefits gained from the incentive offered to states by allowing them to redirect savings may outweigh the benefits of re directing savings to the next priority project (Transcript:42,43).

Project cost reduction incentives

2.19 The proposed NHS project selection system uses a priority ranking system based on benefit/cost ratio. The higher the benefit/cost ratio the higher the priority of a project. Projects will be ranked nationally, not according to state allocations as was previously the case. DOT suggest that the national ranking system provides the states with an incentive to reduce costs. The lower the cost the better the benefit/cost ratio of a project. Consequently the project receives a higher national priority ranking and is more likely to be undertaken. (DOT submission; Attachment B:2,3).

2.20 ANAO suggest that the priority ranking system does not guarantee that the best value project gains the highest priority (ANAO submission:2.4). If the means of calculating the benefit/cost ratio is not uniform across all states then making comparison between the projects will be meaningless, making the national priority ranking system futile.

2.21 DOT have advised the committee that information collected from the states during the national highway strategy study is comparable - allowing a valid comparison to be made (Transcript:34).

2.22 There is a wide discrepancy in project management costs between state authorities (ANAO;1993:43). ANAO suggested that the department should look at this as an area where efficiency gains can be made (Transcript:34).

2.23 DOT pointed out that the development and implementation of performance indicators and performance agreements with the states will allow the department to better monitor the performance of state authorities (Transcript:48,49).

Multi year works programs and national prioritisation of works

2.24 Consultants have been engaged to undertake a strategy study of the National Highway System. The study will provide an inventory of the NHS collated on a comparable basis and will be used to plan the development of the NHS over the next 20 years (DOT submission; Attachment B:3).

2.25 The study will enable the commonwealth to:

- . monitor road condition and plan national maintenance strategies
- . take decisions on multi year investment for the NHS which will involve a shift away from state based allocations.

2.26 ANAO welcomes action taken by DOT in this area. ANAO points out that the consultants reports have been delayed. DOT admit that the strategy study is behind schedule. The study should be completed in the near future (Transcript:48).

Improved accountability of state authorities through performance agreements

2.27 Performance agreements are being developed to improve the accountability of state authorities. The ALTD Act is being amended to provide for the requirement for state authority performance agreements. Performance agreements will cover two areas:

- . road system performance characteristics
- . the efficiency of project delivery and administrative tasks.

2.28 The performance indicators will allow timely, comprehensive and comparable reporting to all Australian governments on the performance of the National Highway System (DOT submission; Attachment B:4).

2.29 ANAO support this approach but is concerned by a lack of a firm timetable for the introduction of legislation introducing the new procedures.

2.30 DOT advise the committee that the government intends to introduce the legislation in the first half of 1995 and the program should be operational by 1 July 1995. In anticipation of the legislation performance agreements are being set in place in cooperation with the states (Transcript:47).

Improved project progress monitoring and quality systems

2.31 The Department of Transport has engaged a consultant to develop a computer program which will enable better project monitoring and progress reporting. The new system is called the Roads Project Management Information System (RPMIS). It is expected that RPMIS will automate many of the current routine processes. RPMIS will encompass quality systems to ensure consistency and efficiency in program administration (DOT submission:Attachment B:5).

2.32 ANAO welcomes the move to establish a road project monitoring data base. However, it points out that the system is not operating due to technical problems.

2.33 DOT advise the committee that RPMIS is still some two or three months from completion and should be operational by early 1995.

CHAPTER 3

Conclusions

3.1 It is clear that there has been considerable improvement in the standard of the National Highway System over recent years. The committee takes this improvement as a sign that the management of the National Highway System (NHS), while it may not have been perfect, has been proficient.

3.2 Despite the commonwealth government's success in developing the National Highway System there is still potential for improvement. The committee views the Australian National Audit Office audit of the management of the NHS as timely and necessary.

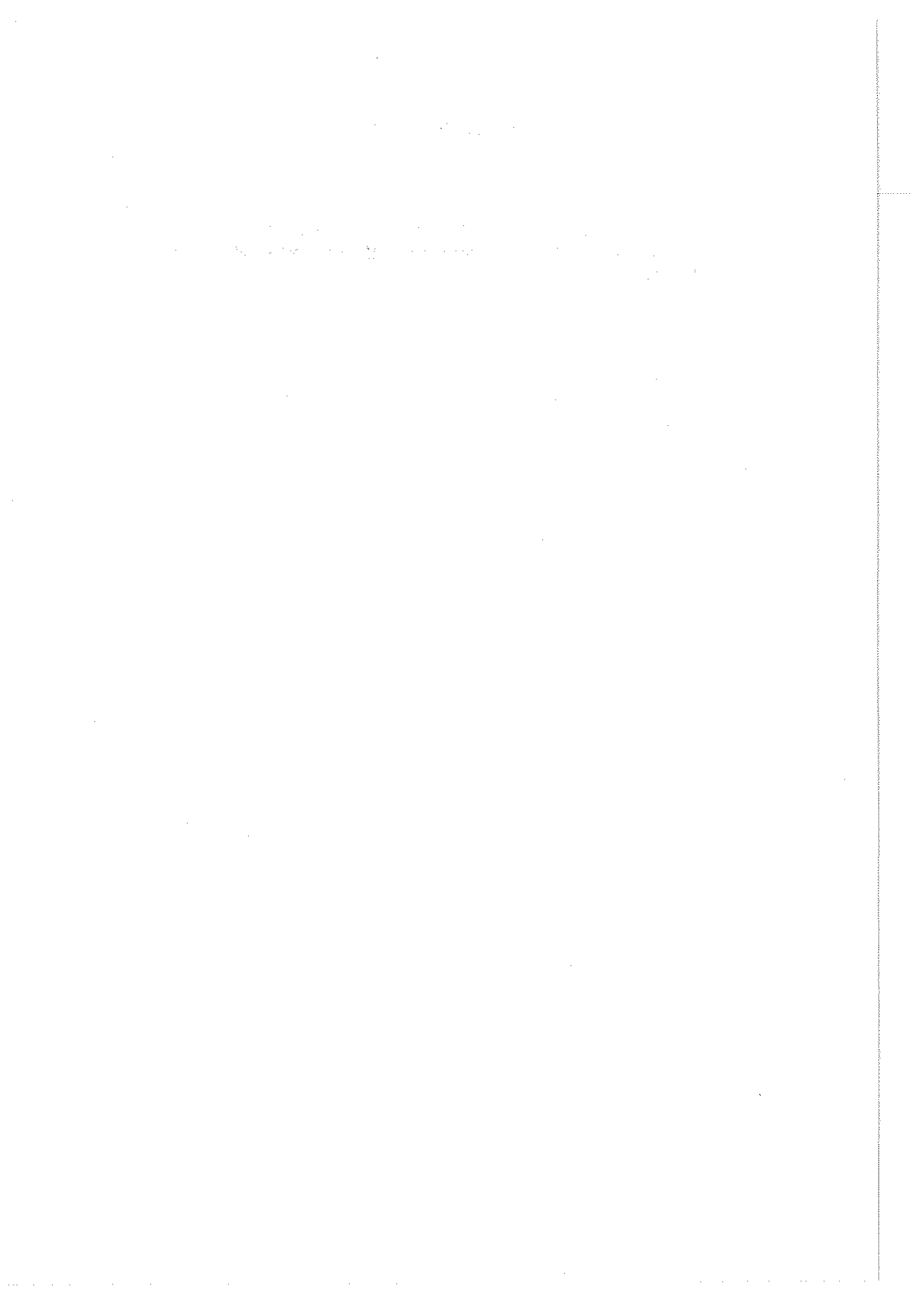
3.3 By incorporating ANAO recommendations in its new management program the Department of Transport has, in the committee's view, improved the effectiveness and efficiency of its management of the NHS. The adoption of most of the ANAO recommendations indicates that the DOT and ANAO agree generally on how the NHS is best managed.

3.4 As the new NHS management system is a move away from state based allocations of funding it is, essentially, a section 96 grant.

3.5 The Joint Committee on Public Accounts is currently conducting an inquiry into the operation of section 96 grants. The committee suggests that when the report of the inquiry is tabled the Department of Transport examine its recommendations and consider incorporating appropriate recommendations into the management program for the National Highway System.

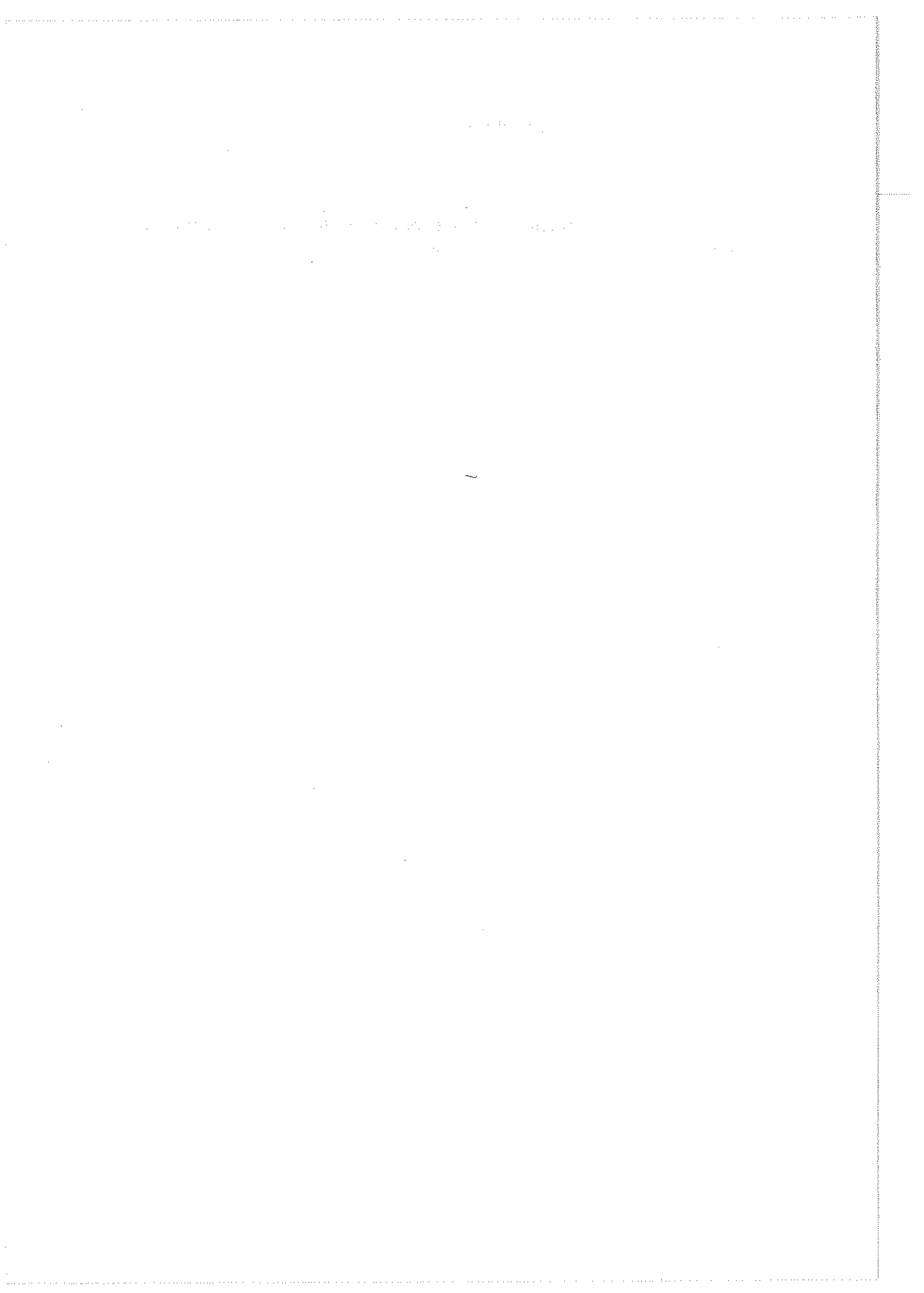
PETER MORRIS MHR
Chairman

16 November 1994



REFERENCE LIST

Kneebone, D, (1993), International Benchmarking Road Construction and Maintenance in Australia - A Discussion Paper, Business Council of Australia, Melbourne.





DEPARTMENT OF
Transport

Secretary
Graham Evans

File Ref: L93/1014

Mr Malcolm Aldons
Secretary
House of Representatives Standing Committee on
Transport, Communications and Infrastructure
Parliament House
CANBERRA ACT 2600

Dear Mr Aldons

Thank you for your letter of 24 May 1994 advising that the Australian National Audit Office (ANAO) Report No 15 '*The National Highway: Lifeline of a Nation*' had been referred to the House of Representatives Standing Committee on Transport, Communications and Infrastructure and seeking advice on the implementation of the audit report recommendations.

The Department's formal response to the Report is reproduced at Attachment A.

The Commonwealth does not own and directly control what happens on roads. It promotes its roads policy objectives through exerting a major influence on how the States undertake their road management functions. It does this by providing funding for certain categories of road construction and maintenance, subject to clearly defined conditions.

Following the Heads of Government agreement that the Commonwealth's roads program be confined to the National Highway System (NHS) from 1994, the Government reviewed the administrative arrangements for the program in 1993, while the ANAO review was underway. The Government decided to strengthen the process for setting forward strategies and for providing incentives for gaining best value outputs, while allowing the States and Territories, as managers of Australia's total road system, flexibility to undertake their task within reasonable parameters.

The ANAO's recommendations that are in line with this approach have been, or are being, implemented. Attachment B provides a detailed commentary on the action taken in these areas. The key points, however, involve:

APPENDIX 1

NO 1.

Secretary:

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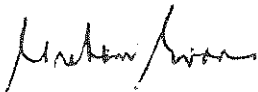
- multi-year works programming;
- prioritising of investments on a national basis;
- improved accountability of State authorities through performance agreements;
- improved quality systems;
- more rigorous matching of payments to cash flow needs;
- more detailed monthly progress reporting;
- greater controls on administration grants;
- widened competitive tendering requirements; and
- best value incentives, such as opportunities to redirect efficiency savings to other high priority projects.

The ANAO also recommended some, more intrusive, administrative controls focussed on management inputs as a means of being assured of better value outcomes from the program. The ANAO report provided no evidence that these outcomes could be achieved by their recommendations. The Department considers that the systemic approach, outlined above, is the best way to ensure effective resource management. This involves high level incentives for obtaining best value, and requirements for open competition, rather than arbitrary limits on the permissible expenditures on particular input costs.

The current implementation status of every ANAO recommendation is shown in Attachment C. Some of the recommendations reflect a misunderstanding about the Commonwealth's role and objectives in relation to roads expenditure. In these cases, it is our view that the ANAO's intent can be better addressed by the more strategic approach to program management outlined above.

In summary, almost all of the ANAO Report's recommendations have already been picked up by actions completed or in train to improve the strategic focus and management of the NHS program.

Yours sincerely



GRAHAM EVANS

8.7.94

DOTAC'S FORMAL RESPONSE TO THE ANAO'S AUDIT REPORT (a)

The Department of Transport and Communications wishes to explain the basis on which it has administered the Australian Land Transport Development (ALTD) Program, to put in perspective its responses to the specific findings and recommendations of the Report.

Getting best value for the taxpayer

The States (and Territories) own the roads which make up the National Highway System (NHS) and are responsible for their management. This has provided a clear incentive to the States to maximise the benefit from their annual allocations of Federal roads grants, which have always been time limited. This incentive has been reinforced as a matter of policy by successive Commonwealth Governments, most particularly by allocating road grants in broadly consistent and hence predictable shares, with the result that savings in any State can be retained for other projects in the same State.

The Commonwealth's approach to the management of the program has been based on outcomes, not inputs. The strategy has been to provide combinations of requirements (though grant conditions) and incentives for the States to be efficient in managing the road assets that the Commonwealth has funded, and to avoid wasteful Commonwealth duplication of what are properly State functions, or the imposition of unnecessary administrative costs.

The Department has been effective in managing the ALTD program in this way.

Over the life of the program, road users have seen major improvements in the quality, safety and performance of the roads funded under this program. This has been achieved through the (imminent) completion of duplication of the Hume Highway in Victoria, and of major new sections in NSW, including the Mittagong and Goulburn bypasses and the Cullarin Range deviation (which replaced a long, narrow and notoriously unsafe section of road); the completion of the sealing of the NHS, the significant improvement of sections of the Bruce and Midland Highways and the Newcastle Freeway; and the reconstruction and widening of long sections of the

(a) (Reproduced from p 67-70 of the ANAO Report No 15)

NHS in Western Australia, Queensland, South Australia and the Northern Territory.

This progress has been achieved cost effectively to the taxpayer. In many cases, major projects have come in well under Budget and ahead of time, particularly on the Hume Highway. There is evidence that NHS construction costs are in line with best international practice. The study sponsored by the Business Council of Australia, *International Benchmarking Road Construction and Maintenance in Australia* (June 1993) found that "the unit cost per lane-km for construction and reconstruction of rural highways and main roads in Australia is equal to or less than that reported for similar roads overseas" (page 11). All parts of the NHS are of this description.

Significant steps taken by the Commonwealth over the life of the ALTD Program to encourage the States to deliver to the taxpayer value for the substantial Commonwealth funding provided for the NHS include:

- . extending the requirement for State roads administrations to put NHS projects to tender rather than undertake many of these functions themselves;
- . promoting the introduction and use by State roads administrations of quality assurance systems, including the first large scale application to civil engineering contracts in Australia - acknowledged by one State to have been an important source of improved efficiency;
- . promoting the comparable assessment of pavement condition by requiring States and Territories to apply consistent pavement management systems;
- . limiting the extent to which cost overruns are reimbursed (project cost underestimating was a major problem addressed in a 1989 ANAO Report);
- . assessing project submissions from the States on a case by case basis against wide ranging public benefit criteria, including economic and social justification, physical details, cost and timeframe. (To ensure Commonwealth objectives are met in respect of specific projects, the Department's interactions with the States on these assessments often leads to rescheduling and redesign to improve efficiency and outputs); and
- . participating with States in planning for new works.

These measures are administratively inexpensive. They recognise the States' long term interests and responsibilities as owners and managers of the roads, and

build on the fact that the States already have a range of systems in place for assessing what ought to be done to maintain and improve their road systems. (The NHS is less than 2.5% by length of the total road system).

Increasing the Commonwealth's level of monitoring and control would have meant additional administrative costs. These could be substantial in the areas of asset management (such as in the determination of appropriate maintenance treatments) and detailed engineering and economic appraisals of individual projects. These are highly technical and resource intensive functions currently carried out by State roads administrations which the Commonwealth would not wish to duplicate. As already stated, with the States owning the asset, and receiving funds in fairly consistent shares, the States have every incentive to maximise benefits from the expenditure. No case has been made that the Commonwealth could undertake these functions more efficiently than they are now undertaken by the States.

The policy and legislative framework

To understand fully the scope of the Department's administration of the program, it is necessary to understand the policy and legislative framework within which the Department operates.

Decisions on the allocations of grants to States are matters for the Minister. The Minister decides early in each financial year how much of the funds appropriated to the program in each financial year are to be 'allocated' to each State and Territory. The decision is widely publicised, and generally attracts vigorous response from States which feel their allocation should have been higher. The detailed work program for each State is determined by the Minister within the limits of the State's allocation after consultation with each State.

As noted above, these allocations have been in fairly consistent shares, with project cost savings being available for use by the State generating the saving. This has been an incentive for good management practice by the States. However, this has not meant passive acceptance of State expenditure proposals by the Commonwealth. As well as the positive interventions indicated above, the Commonwealth has determined multi-year NHS strategies which have sought to attain physical goals of a national character (eg duplication of the Hume Highway, sealing all unsealed sections and widening narrow seal sections of the NHS in remote areas).

The Department acknowledges the need for the administration responsible for the long term management of the road asset to apply sound asset management principles and has actively

promoted this. Under the ALTD and predecessor roads programs, this has been unequivocally the responsibility of the States.

The Department agrees that in managing Specific Purpose Payments, Departments must have adequate mechanisms in place to enable effective program management to ensure national objectives are being achieved, and funds are being expended in a cost effective manner. The Department's administrative mechanisms have been directed to this end. The Department does not consider that the Report demonstrates that any alternative form of administration would have been more cost effective in delivering the NHS program, given the policy framework within which it has operated, than that applied by the Department.

Policy change

Finally, it should be noted that from 1994, the Commonwealth will have clear and ongoing responsibility to fund the NHS, arising from the decision by Heads of Government in 1991 to delineate clearly the road funding responsibilities of each level of Government. As a consequence of this, the Government has announced its intention to change significantly the policy framework applying to the funding of the NHS, under legislation to replace the ALTD Act. Proposed Legislative Principles for this purpose were issued by the Minister for Transport and Communications, Senator the Hon Bob Collins, on 29 July 1993.

The Minister's statement indicates many changes, including:

- . the Government's program objectives will be stated in the new Act;
- . NHS project priorities will be assessed against these objectives on a national basis;
- . investment principles in the form of detailed criteria for selecting projects and allocating funds will be published in the form of a NHS Strategic Plan;
- . there will be a rolling three year program of works;
- . the role and responsibilities of the State authorities responsible for the management of NHS roadworks in each State will be set out in performance agreements, which will cover such matters as road system performance standards, the effectiveness of project delivery and administration costs.

None of this alters the underlying legal fact that the NHS roads are owned and managed by the States and Territories in which they are located, and that the new program will therefore be a s.96 grants scheme.

The changed policy framework significantly alters the incentive structure of the current program, and will require therefore a new approach to be adopted to the administration of the program to ensure cost effective outcomes continue to be achieved.

In this context, more of the ANAO's Report's recommendations become relevant and, as indicated by the Department's responses to them, will be fully considered when the administration arrangements for the new program are finalised.

IMPLEMENTATION OF THE ANAO RECOMMENDATIONS ON THE
ADMINISTRATION OF THE NATIONAL HIGHWAY PROGRAM : COMMENTS
ON THE MAIN ISSUES

More rigorous matching of payments to reporting of progress

ANAO recommended that DOT only make payments on the basis of States' actual expenditures (Recommendations 6a, 6b, 14a and 14c).

All specific purpose payment schemes involving advance payments to the States will result in an interest benefit to the recipient States. NH program payment arrangements that have been in place since October 1992 aim to minimise this effect.

Each State reports in the second week of each month its actual expenditure on approved projects in the preceding month and its expected expenditure in the current and following months. Sufficient payment is then made that the State receives no more than it will reasonably need to meet expected costs to the middle of the following month, when the next payment is due. This means that the State has an average of two weeks credit at any time.

An equal monthly instalment process trialed from March 1992 led to an undue interest benefit for the recipient States, and was quickly discontinued.

Incentives to reduce costs

ANAO recommended tighter control over inputs more like an own purpose program for the administration of the National Highway Program. (Recommendations 14a, 14b, 14c, 14d, 23, 25, 27 28, 29).

The Department considers that the savings are best realised from high level incentives for obtaining best value, and requirements for open competition, rather than from further limiting the permissible expenditures on particular input costs.

Asset preservation costs

Tenders will be required to be called for all asset preservation works except routine works to keep the road in a safe and trafficable condition, such as road patrols, grass cutting, line marking, shoulder gradings, drain clearing, traffic signal maintenance and routine minor repairs included in the 1994-95 maintenance program.

The Minister may exempt projects from this requirement if the exemption criteria in the ALTD Act are satisfied.

Administration costs

From 1994/95 no administration payments will be made, except to meet the following overhead costs:

- Road data: Collection, storage and transmission of information about National Highway roads.
- Project progress: Monitoring and reporting of physical progress, cash flow and cost estimates of National Highway projects.
- Strategy development: Assessment of future maintenance and construction needs of National Highway roads.
- Quality assurance: Monitoring and reporting of quality assurance arrangements for National Highway contracting.
- Network management: Day to day management of maintenance and construction of National Highway roads.
- Auditing of financial statements for submission to the Commonwealth.

Administration costs incurred in respect of particular works involved in the carrying out of an approved project or the maintenance program must be attributed to the project or program, and cannot be funded from the general administration grant.

General administration payments will be made only on the basis of a detailed proposal indicating how much is proposed to be expended on each of the above areas.

Use of savings

Savings arising in a State on approved projects, and any surplus administration funds, will be available for allocation to that State. The funds may be used to meet contingency claims (ie previous overspends), or the costs of additional asset preservation works, further accelerating works listed in the 1994-95 NH Strategy or to initiate other priority projects as agreed by the Minister.

Incentives to reduce project costs

Projects will not be funded after 1994-95 unless identified in the multi-year NH Strategy to be issued in early 1995. This Strategy is expected to rank projects nationally

according to evaluation criteria that will include benefit cost ratio. The lower the overall cost (including, but not restricted to, project management and administration costs) for given benefits, the higher the benefit /cost ratio the higher the priority of the project. States will therefore have an incentive to reduce overall costs.

Multi year works programs and national prioritisation of works

ANAO recommended that a program of national priorities be developed for the National Highway (recommendations 2, 4, 9a and 9b).

Consultants, Ove Arup and Partners and Nelson English Loxton and Andrews have been commissioned to undertake a strategy study of the National Highway System. The reports are due in September 1994.

This independent study will provide for the first time a comprehensive inventory of the whole NHS collected on a comparable basis, and is intended to identify the improvements to the NHS which will be required over the next 20 years.

All States and Territories are co-operating in the study by participating in an advisory steering committee for the project and by providing data. One of the key outcomes expected from the study is the establishment of mechanisms for the ongoing provision and analysis of road condition data, which will allow the development of more soundly based, national maintenance strategies.

The study will complement States' advice on investment priorities and will provide a framework against which the Commonwealth can take decisions on multi-year investment priorities for the NHS. This will entail a significant shift away from State based allocations.

As an interim arrangement, the funding allocations for 1994/95 have been made on the basis of clearly identified principles (summarised in 'Incentives to reduce cost' (pages 1-2 above) and reproduced in full in Attachment D) and are aimed at 'clearing the decks' of partially completed projects so that the Minister will have maximum flexibility to implement a multi-year, national investment strategy.

**Improved accountability of State authorities through
Performance Agreements**

ANAO recommended that DOT develop performance agreements between the Commonwealth and the States (recommendations 1a, 1b, 1c, and 3,).

NH performance agreements are currently being developed to strengthen performance incentives by further enhancing accountability of State agencies for their delivery services. Amendments to the ALTD Act are being prepared to provide for performance agreements. The first agreements are being developed for introduction in 1994.

NH performance agreements will cover road system performance characteristics under the control of State agencies (eg. the effectiveness of their maintenance programs over which the Commonwealth does not exercise project specific controls), and the efficiency of project delivery and administrative tasks. The agreements will also allow administrative rules to be tailored to the needs of each State.

Key relevant indicators, and targets, to be included in performance agreements are now being developed between the Department and each State road and traffic authority.

The lack of the indicators which would allow robust comparison of the performance of road management agencies has been recognised as a major deficiency for some time.

The Department has worked with Austroads to develop suitable indicators for assessing and, where appropriate, benchmarking the performance of the road system overall and of State road managers.

This has not been easy due to the heterogeneous nature of roads, but the stage has now been reached where twenty three indicators have been developed for this purpose. They range from measuring social benefits of the road system to the technical efficiency of the road construction activity.

The Department has been closely involved in promoting the development of these indicators.

Implementation arrangements, including systematic reporting of performance in relation to these indicators, were endorsed at the June 1994 Austroads Council meeting.

This will allow timely, comprehensive and comparable reporting to all Australian Governments on the performance of the national road system and its management agencies, starting with 1994/95. This is in line with ANAO recommendations.

Improved project progress monitoring and quality systems

ANAO recommended that DOT overhaul its management and data base systems (recommendations 5a, 5b 10a and 10b).

A consultancy is currently underway to develop a computer system to enable better project monitoring and progress reporting, automate much of the current routine paper processing and recording thereby freeing resources for the strategic issues. The new system, called Roads Project Management Information Systems (RPMIS), is expected to be implemented from July 1994. The RPMIS is being developed in a way which will allow integration with State systems.

The RPMIS will supersede the existing electronic data base, Focus, with a more user friendly, flexible system that integrates project and financial reporting.

Quality systems are being embodied in the RPMIS systems to ensure consistency and efficiency in program administration.

A NAO Report - Actions taken as at 7/7/94

	Recommendation	Para	Action taken
1a	DOTAC develop performance indicators for monitoring its own performance, and the performance of the SRAs	2.14	Being implemented. Performance agreements being developed with all States using a number of performance indicators to measure both road and organisational performance.
1b	Common indicators for all States should be introduced for SRA performance reporting, and		Being implemented. Austroads has agreed on 23 common indicators of performance for annual publication. Performance agreements will have indicators focussed on the National Highway.
1c	DOTAC should recommend that the proposed new legislation contains clear requirements for performance indicators, performance measurement and performance reporting.		Being implemented. Proposed amendments to ALTD Act will require performance agreements between the Commonwealth and each State.
2	DOTAC investigate the use of benefit-cost ratio analysis for the evaluation and ranking of projects and establishing the National Highway program.	2.18	Implemented.
3	DOTAC establish performance agreements with the SRAs.	2.22	Being implemented. See recommendation 1.
4	DOTAC undertake the corridor reviews as soon as possible.	2.27	Implemented. NH Strategy Studies covering all corridors under way. Report due 30/9/94.
5a	DOTAC overhaul the database and management information system using the ANAO model as a basis and develop effective analyses and reporting routines	2.34	Implemented. New management information system being developed for introduction in July 1994.
5b	DOTAC examine the possibility of electronic transfer/interchange of data with the States.		Implemented. Interchange arrangements are under examination.
5c	DOTAC consult with the BTCE (which has collected roads data for its studies in the past), and maintain liaison with overseas counterparts to develop international benchmark comparisons.		Implemented. Included in Austroads work program for 1994-95.
6a	DOTAC continue to make payments only on the basis of the States' actual expenditure advised in monthly progress reports, and	2.46	Implemented.
6b	DOTAC monitor the annual carry-over of funds.		Implemented.

7	DOTAC should ensure the audited financial statements submitted by the SRAs comply with requirements of the ALTD Act.	2.52	Implemented.
8	In developing financial accountability requirements for the new Act, DOTAC should fully consult with and obtain the agreement of the State Auditors-General if it is intended that they continue to be involved in the provision of audit certificates.	2.55	Will be implemented if the provisions affecting State Auditors-General are to be amended.
9a	DOTAC ensure that States' Forward Strategy Reports and Five Year Plans identify road condition and key network performance indicators such as road condition and benefit cost ratios	3.10	Being implemented. States will be required to submit relevant condition and performance information in their next forward strategy report due 31/12/94.
9b	DOTAC develop national priorities to ensure the relative needs of all sections of the National Highway are assessed, and		Being implemented in development of the NH Strategy to apply from 1 July 1995.
9c	DOTAC publish the program annually, showing the priorities, benefit-cost ratios and any other key factors that affected the decision making process in determining the approved program.		Implemented for the 1994-95 program in that all relevant factors were advised to the States.
10a	DOTAC review and revitalise the internal quality management system for program and project approval	3.20	Being implemented. The new management information system will embody an updated quality system to ensure consistency/efficiency in program administration.
10b	DOTAC introduce procedures within the quality management system to improve project assessment by fully evaluating project benefit-cost ratio assumptions, cost estimates and site characteristics, and		DOT will review the extent to which each of these matters needs to be evaluated in the development of the NH Strategy to apply from 1 July 1995.
10c	DOTAC liaise with the State Road Authorities to ensure that the new assessment procedures lead to improved practice within SRAs.		Being implemented.
11a	DOTAC review the accuracy of SRAs' estimates with a view to publishing the results of the review, and	3.31	Under the proposed arrangement for ranking of projects there will be a strong incentive to keep estimated costs down to ensure that projects rank sufficiently highly on benefit-cost ratios to be funded. This should achieve the ANAO objective underpinning this recommendation.

11b	DOTAC liaise with the SRAs to ensure improved procedures are established that monitor the accuracy of estimates.		See recommendation 11(a).
12a	DOTAC liaise with the SRAs to standardise as far as possible the definition of all sub-items that make up a cost estimate, and	3.37	Being implemented. Notes on Administration of the ALTD Program being revised to include standardised definitions.
12b	DOTAC adopt the ANAO framework proposed as a basis for the development of consistent definitions for the States' project estimates.		Being implemented. See recommendation 12(a).
13	DOTAC introduce procedures to review the reasonableness of allowances for cost increases and monitor total project costs against the project budget.	4.17	Implemented. New reporting arrangements allow closer monitoring of project costs. Reasonableness of allowances to be addressed in consistency process at recommendation 12(a).
14a	DOTAC define the administration costs which can be claimed, and ensure this is applied uniformly by all States when developing their annual budgets	4.23	Implemented.
14b	DOTAC consider negotiating the absolute level of administration costs to be paid in an effort to find savings		Being implemented as part of the development of performance agreements.
14c	DOTAC develop procedures to ensure all administrative cost claims by States are for justified items before payment is made, and		Implemented.
14d	DOTAC ensure all administrative cost claims by States are submitted in a form which permits inter-state comparison and performance measurement.		Implemented.
15	DOTAC consider establishing the NSW level of project-specific administration costs as the Australian benchmark.	4.33	New program ranking mechanisms will provide incentives for States to minimise administrative overheads, thus achieving the ANAO objective underpinning this recommendation.
16a	DOTAC should introduce performance criteria for project specific administrative costs for each State Road Authority with the aim of progressively reducing project delivery costs, and	4.35	See recommendation 15.

16b	DOTAC should develop and implement procedures which would ensure that States fully identify and justify project specific overheads.		See recommendation 15.
17	DOTAC review and recommend funding research into other forms of project delivery which have the potential for gains.	4.44	Commonwealth actively participating with State Authorities through Austroads and ARRB to develop and deliver a targeted and effective National Strategic Road Research Program. This recommendation will be taken up in this context.
18	DOTAC improve the current system of progress reporting by:	4.49	
18a	ensuring that engineers are involved to provide technical assurance on actual progress		Implemented. Technical advice will be sought when required.
18b	the inclusion of milestone indicators, and		Being implemented. More comprehensive reporting required from 1 July 1994.
18c	enhancing the capability of the database.		See recommendation 5a.
19a	DOTAC collect the relevant information on project progress and provide the necessary reports to the Minister, and	4.53	Implemented.
19b	DOTAC recommend replacing the deadline to report (on ALTD Operations) 'as soon as practicable' with a firm deadline of 31 December in the new legislation.		A firm deadline of 31 December is not considered to be practical, given the time it takes for the States to finalise expenditure after the completion of physical works (eg because of contractor billing delays). The importance of timely reporting to the Parliament is recognised and current arrangements are being streamlined to improve the timeliness of this report.
20a	DOTAC resume the quality assurance inspection and audit program,	4.61	As part of the review of the Notes on Administration, States to be encouraged to obtain accreditation for their quality systems.
20b	the quality assurance inspection and audit program be funded from the National Highway program, and		Under consideration.
20c	DOTAC report on the benefits accruing from quality management systems.		Being implemented, with a view to a report being published with 1993-94 ALTD Review of Operations.
21a	DOTAC pursue the development of uniform PMS systems by the States,	5.13	Being implemented. States are required to provide comprehensive data for the NH Strategy Study. The NH Strategy Study will also provide the basis for ongoing comparison.
21b	DOTAC ensure that all information is provided by the States, in particular estimates of the remaining life of the pavement.		Being implemented, through NH Strategy Study.
22a	DOTAC reassess the reporting links of the National Highway, and	5.17	Being implemented, through NH Strategy Study.

22b	DOTAC after full consultation with the States, establish and publish the methodology to be used.		Being implemented, through NH strategy study.
23	DOTAC develop a maintenance strategy based on asset management principles and full consideration of all stages of the maintenance cycle.	5.25	Being implemented through NH Strategy Study and through processes to be appraised in 1994. DOT is actively participating in Austroads work on harmonised asset management practices.
24	DOTAC should ensure all relevant steps in the maintenance funding process are documented to provide:	5.27	Implemented.
24a	defensible evidence supporting the decisions taken, and		Implemented.
24b	an adequate audit trail and proper lines of accountability.		Implemented.
25	DOTAC use the life cycle costing technique to ensure maintenance options are fully evaluated.	5.32	Being considered in context of NH Strategy Study.
26	DOTAC identify community service obligations in a published annual program.	5.35	Being considered in the context of the NH Strategy Study, which will indicate relevant key social benefits.
27	DOTAC review the application of maintenance standards to take account of traffic volume and economic benefits.	5.38	Being implemented through NH Strategy Study.
28	DOTAC adopt an asset management approach to network construction planning which:	6.11	
28a	includes both 'top-down' optimisation techniques and 'bottom-up' needs analyses		Being implemented through NH Strategy Study.
28b	clearly defines Government policy objectives and assessment criteria, and		Being implemented through NH Strategy Study.
28c	has as its primary output an overall list of recommended projects in priority order based on agreed criteria.		Being implemented through NH Strategy Study.
29	DOTAC adopt the maintenance management model for the management of maintenance of the National Highway.	6.18	Maintenance management models will be considered in the context of the NH Strategy Study.

PRINCIPLES FOR THE 1994-95 NATIONAL HIGHWAYS (NH) STRATEGY

Projects now Underway, or Substantially Committed

1. The Strategy provides as much funding as possible to allow earliest practicable completion of projects in the following three categories:

- construction works which are physically underway;
- a project on which construction works are not physically underway but where other linked stages are underway; and
- works are not underway but have previously been announced to be funded in 1994-95.

New Enhancement Projects

2. The Strategy funds new enhancement works which have the following characteristics:

- relatively small and therefore able to be initiated and completed in 1994-95 (these are mainly passing lanes, and intersection improvements); and
- necessary preliminary planning, environment assessment or land acquisition for projects which are the most likely to be funded in the next three years.

Asset preservation

3. Only routine asset management works to keep the road in a safe and trafficable condition, such as road patrols, grass cutting, line marking, shoulder gradings, drain clearing, traffic signal maintenance and routine minor repairs, may be included in the 1994-95 maintenance program. Tenders will not be required to be called for these works, assuming none exceeds \$2m in cost.

4. Other works which have previously been included in bulk works and maintenance programs, such as pavement resealing and rehabilitation, intersection improvements and road widening works will need to be submitted for approval as construction projects, though it will be permitted to aggregate a number of such works in a single project proposal. Tenders will need to be called for these projects unless exempted by the Minister in each case.

Administration Payments

5. General administration payments will be available to meet the following costs incurred directly in connection with the construction or maintenance of National Highway roads but not incurred in respect of any particular approved works:

- Road data: Collection, storage and transmission of information about National Highway roads.
- Project progress: Monitoring and reporting of physical progress, cash flow and cost estimates of National Highway projects.
- Strategy development: Assessment of future maintenance and construction needs of National Highway roads.
- Quality assurance: Establishment, monitoring and reporting of quality assurance arrangements for National Highway contracting.
- Network management: Day to day management of maintenance and construction of National Highway roads.
- Auditing of financial statements for submission to the Commonwealth.

6. Administration costs incurred in respect of particular works involved in the carrying out of an approved project or the maintenance program must be attributed to the project or program, and cannot be funded from the general administration grant.

7. General administration payments will be made only on the basis of a detailed proposal indicating how much is proposed to be expended on each of the above areas. A breakdown of anticipated costs against each of the above categories should be submitted when the general administration program is submitted for approval. At this time, consideration would be given to any proposal for meeting any other categories of administration costs within the indicated notional administration allocation.

Use of Savings

8. Savings arising in a State or Territory on approved projects, and any surplus administration funds, will be available for allocation to that State or Territory to meet contingency claims, for additional asset preservation works, or to further accelerate works listed in this Strategy. Other priority projects may also be funded, to be submitted for approval following consultation with the Commonwealth Department.

Emergency Repairs

9. Application may be made for funds to meet costs of unforeseeable safety and trafficability repairs (eg bridge failures, and flood damage to pavements) anywhere on the NH. There is a small reserve of unallocated funds for this purpose.

Performance Agreements

10. Performance targets for the maintenance program and for the uses of administration funds will be, with other elements of the program, the subject of performance agreements which the Department of Transport is developing with State and Territory agencies.

Invitation for Particulars

11. Funds cannot be provided for any listed project which is not approved by the Minister. States and Territories are invited to submit particulars of any listed project which is not already approved, and any project which the State or Territory considers should be funded within the asset preservation allocation (see paragraph, 4 above) in accordance with the Notes of Administration.

12. Funds cannot be provided for the maintenance program until it is approved by the Minister. States and Territories are invited to submit particulars of a program for the maintenance of the NH (as described in paragraph 3, above), also to be funded within the asset preservation allocation, in accordance with the Notes of Administration.

13. Funds cannot be provided for the general administration program until it is approved by the Minister. States and Territories are invited to submit the information sought in paragraph 7, above) for the Minister's consideration.

Further Information

14. The Department of Transport will advise details of the project approval arrangements and any consequential changes to the Notes of Administration arising from this Strategy.



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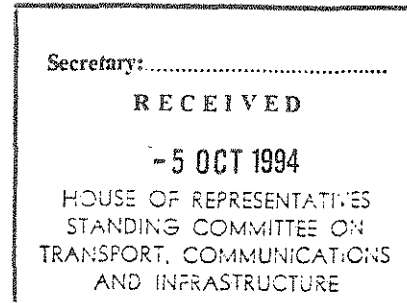
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APPENDIX 2

NO 2

29 September 1994

Mr M. Aldons
Secretary
House of Representatives
Standing Committee on Transport,
Communications and Infrastructure
Parliament House
Canberra ACT 2600



Dear Mr Aldons

AUDIT REPORT NO.15 1993-94 'THE NATIONAL HIGHWAY'

Thank you for your letter of 25 August 1994 seeking comments on the Department of Transport's submission on the implementation of the recommendations in Audit Report No.15 1993-94 'The National Highway'.

The ANAO appreciates this opportunity to comment on the Department's response to the Committee in respect of the audit of the National Highway program. The audit was timely in the light of the proposed changes to the program and associated legislation which were generally supported by ANAO. The recommendations in the report were designed to ensure that effective management arrangements were in place for the new program.

At this stage we have not conducted a follow-up audit to assess the effectiveness of the implementation of our recommendations. However, we will consider such an audit in our strategic audit planning. Such an audit will depend on suitable resources being available at the time.

The ANAO is pleased to see the Secretary of the Department in his letter to you of 8 July 1994 has advised that 'almost all of the ANAO Report's recommendations have already been picked up by actions completed or in train to improve the strategic focus and management of the National Highway System program'.

However, we are concerned that the Department appears to have rejected a number of recommendations that they consider more intrusive i.e. those proposing tighter administrative controls.

We appreciate the Department's view that it is important that an appropriate administrative and management framework is in place to ensure value for money. Nevertheless, we believe it is also important to have in place a monitoring mechanism to ensure that the framework is working as it should. An appropriate framework is necessary but is not sufficient by itself. We acknowledge that additional monitoring carries a cost. However, as the Committee found during its own inquiry, there is a paucity of information available to policy makers on which to base road planning decisions. We share the Committee's view of the need for greater involvement by the Department to ensure information is available to Parliament that taxpayers are getting value for each road dollar spent.

The Department has confirmed that the new program will be a Special Purpose Payment. You will no doubt be aware that the JCPA is conducting a comprehensive review of grant payments to the States. Furthermore, Audit Report No.6 1993-94 'An audit commentary on aspects of Commonwealth-State agreements' included, amongst other things, comment on reporting and other accountability arrangements including the need for mechanisms to be in place to provide timely assurance that best value for money is being obtained.

In this context we noted a report in the Daily Commercial News of 16 December 1993 (copy attached) which stated that the former Minister Mr Brown had written to the then Transport Minister Mr Collins in response to the Department's response to the audit report. The article quotes Mr Brown as saying there was a strong disposition within the Department to move from a project approval approach to a program management approach without any closer supervisory role. Mr Brown is quoted as saying he resisted this as he believed the Commonwealth had a responsibility to supervise more closely the efficient and effective use of the national taxpayer's dollar.

We are also concerned that the Department considers some of our recommendations reflect a misunderstanding of the Commonwealth's role and objectives in respect of roads expenditure. The ANAO goes to considerable lengths including clearing draft reports with the department(s) involved, to ensure that our reports reflect accurately policy and program objectives.

In this respect the ANAO was pleased to see the Committee's report 'Driving the roads dollar further' referred to the need to 'make further comments on objectives', noting that the absence of clearly articulated program objectives is a serious omission. We understand from recent discussions with the Department that there has been a delay with the development of the amended ALTD legislation which was to have set out the program objectives. This is a disappointment particularly as there appears to be no timetable set for the introduction of the amendments. Nevertheless, the Department has told us that they are working to a set of objectives that would be included in the legislation.

More detailed comments on the Department's submission are attached.

Should you wish to discuss any of these matters, please telephone Mr Peter White on 2037685 or Mr Michael Lewis on 2037683.

Yours sincerely

A handwritten signature in cursive script, appearing to read "Warren J. Cochrane".

Warren J. Cochrane
Acting National Business Director
Performance Audit

PUBLIC HEARING WITNESSES

1. The following witnesses appeared at a public hearing in Canberra on 10 November 1994.

Mr Michael Kenneth Lewis
Executive Director
Australian National Audit Office

Mr Anthony James Slatyer
Assistant Secretary
Roads Branch
Land Transport Policy Division
Department of Transport

Mr David Norman Smith
Audit Manager
Australian National Audit Office

Mr Christopher Thorpe
First Assistant Secretary
Land Transport Policy Division
Department of Transport

Mr Peter Frank White
Acting Group Director
Australian National Audit Office

