

The Parliament of the Commonwealth of Australia

Joint Committee of Public Accounts
and Audit

P. Allen

DEPARTMENT OF THE SENATE
PAPER No. 13226
DATE 30 JUN 1998
PRESENTED
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REPORT 362

**General and Specific
Purpose Payments
to the States**

June 1998



The Parliament of the
Commonwealth of Australia

Joint Committee of
Public Accounts and Audit

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CHAIRMAN'S FOREWORD

The Australian States and Territories are dependent on funding from the Commonwealth for a significant proportion of their expenditure.

The financial assistance provided by the Commonwealth to State and local governments is a substantial component of both the outlays of the Commonwealth and the revenues of the other levels of government. It accounted for approximately 20 per cent of the total outlays of the Commonwealth general government sector in 1996-97. It also represented approximately 37 per cent of the total revenues of the State general government sector and 19 per cent of that of the local general government sector.

All Commonwealth payments to the States and Territories are made as Specific Purpose Payments (SPPs) or General Purpose Payments (GPPs). The grants are contingent upon the fulfilment of a wide range of terms and conditions.

The conditions which the Commonwealth usually attaches to the *use* of SPP funds are generally set out in Commonwealth legislation, in agreements concluded between the parties or in other program documentation. While conditions are not imposed on the States' use of GPPs, some conditions are attached to the *receipt* of those funds. These conditions are set out in States Grants (General Purposes) legislation.

The JCPAA was asked to report on conditions which may appropriately be attached to SPPs and GPPs.

From its examination of SPP program administrative arrangements, the Committee reached a number of conclusions regarding SPP payments and conditions which may appropriately be attached to them. In particular, the Committee believes that Commonwealth departments should draw upon the ideal features which it has set out in this report in preparing specific conditions to be attached to individual SPPs under their administration.

The Committee examined the four conditions which currently apply to GPPs and concluded that there is little to be gained from attempting to prescribe a definitive list of specific conditions which might appropriately be applied to hypothetical future conditional GPP funding arrangements. Those conditions would need to be determined for each case.

Constitutionally, the Commonwealth may grant financial assistance to the States and Territories on such terms and conditions as the Parliament sees fit. The Committee believes that the system is best served when the Commonwealth and States act cooperatively.

The report also addresses conditions relating to the role of State Auditors-General. The Committee found that problems have been encountered by State Auditors-General when financial audit and acquittal responsibilities are imposed on them under SPP agreements between the Commonwealth and the States.

The Committee believes that, in the interests of enhancing the public accountability of Commonwealth and State government agencies for SPP programs without compromising the statutory independence of State Auditors-General, it is important that responsibilities for the financial certification of SPP payments are not imposed on State Auditors-General. It is also important that opportunities for the conduct of coordinated or joint audits of SPP programs by the Commonwealth and State Auditors-General continue to be actively pursued.

The JCPAA was also asked to inquire into 'recent developments concerning the Victorian Auditor-General'. Although the Committee found this part of the terms of reference to be imprecise, the Committee has taken it to allude to the review of the Victorian *Audit Act 1994*. In the Committee's view, this is a matter which falls within the constitutional jurisdiction of the State of Victoria; the JCPAA's mandate is limited to the Commonwealth sphere. The report therefore does not address this issue.

In conclusion, I wish to thank Russell Laphorne from the Australian National Audit Office for his contribution to this report.



Bob Charles MP
Chairman

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MEMBERSHIP OF THE COMMITTEE

Mr R E Charles, MP (Chairman)

Mr A P Griffin, MP (Vice-Chairman)

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Mr L Anthony MP

Senator the Hon R Crowley

Hon D Beddall MP

Senator the Hon B Gibson AM

Mr R Broadbent MP

Senator J Hogg

Hon J Crosio MP

Senator A Murray

Mr J Fitzgibbon MP

Senator J Watson

Mr P Georgiou MP

Hon J Sharp MP

Mrs S Stone MP

Secretary:

Dr Margot Kerley

MEMBERSHIP OF THE SECTIONAL COMMITTEE

Mr Bob Charles, MP (Chairman)

Mr Alan Griffin, MP (Vice-Chairman)

Senator Andrew Murray

Hon David Beddall MP

Mr Petro Georgiou MP

Hon Janice Crosio MP

Sectional Committee Secretary:

Ms Gillian Gould

Inquiry Staff:

**Mr Russell Laphorne
Ms Laura Gillies**

DUTIES OF THE COMMITTEE

The Joint Committee of Public Accounts and Audit is a statutory committee of the Australian Parliament, established by the *Public Accounts and Audit Committee Act 1951*.

Section 8(1) of the Act describes the Committee's duties as being to:

- (a) examine the accounts of the receipts and expenditure of the Commonwealth, including the financial statements given to the Auditor-General under subsections 49(1) and 55(2) of the *Financial Management and Accountability Act 1997*;
- (b) examine the financial affairs of authorities of the Commonwealth to which this Act applies and of intergovernmental bodies to which this Act applies;
- (c) examine all reports of the Auditor-General (including reports of the results of performance audits) that are tabled in each House of the Parliament;
- (d) report to both Houses of the Parliament, with any comment it thinks fit, on any items or matters in those accounts, statements and reports, or any circumstances connected with them, that the Committee thinks should be drawn to the attention of the Parliament;
- (e) report to both Houses of the Parliament any alteration that the Committee thinks desirable in:
 - (i) the form of the public accounts or in the method of keeping them; or
 - (ii) the mode of receipt, control, issue or payment of public moneys;
- (f) inquire into any question connected with the public accounts which is referred to the Committee by either House of the Parliament, and to report to that House on that question;
- (g) consider:
 - (i) the operations of the Audit Office;
 - (ii) the resources of the Audit Office, including funding, staff and information technology;
 - (iii) reports of the Independent Auditor on operations of the Audit Office;

- (h) report to both Houses of the Parliament on any matter arising out of the Committee's consideration of the matters listed in paragraph (g), or on any other matter relating to the Auditor-General's functions and powers, that the Committee considers should be drawn to the attention of the Parliament;
- (i) report to both Houses of the Parliament on the performance of the Audit Office at any time;
- (j) consider draft estimates for the Audit Office submitted under section 53 of the *Auditor-General Act 1997*;
- (k) consider the level of fees determined by the Auditor-General under subsection 14(1) of the *Auditor-General Act 1997*;
- (l) make recommendations to both Houses of Parliament, and to the Minister who administers the *Auditor-General Act 1997*, on draft estimates referred to in paragraph (j);
- (m) determine the audit priorities of the Parliament and to advise the Auditor-General of those priorities;
- (n) determine the audit priorities of the Parliament for audits of the Audit Office and to advise the Independent Auditor of those priorities; and
- (o) undertake any other duties given to the Committee by this Act, by any other law or by Joint Standing Orders approved by both Houses of the Parliament.

TERMS OF REFERENCE

On 26 November 1997 the Senate agreed to the States Grants (General Purposes) Amendment Bill (No.2) 1997, with the following amendment:

'and that the following matter be referred to the Joint Committee of Public Accounts and Audit for inquiry and report by 30 June 1998:

Conditions which may appropriately be attached to:

- (a) general purpose payments to States; and
- (b) specific purpose payments to States;

including conditions relating to the role of State Auditors-General, with particular references to recent developments concerning the Victorian Auditor-General'.

GLOSSARY

ACCC	Australian Competition and Consumer Commission
ANAO	Australian National Audit Office
BCP	Better Cities Program
COAG	Council of Australian Governments
CGC	Commonwealth Grants Commission
CSHA	Commonwealth-State Housing Agreement
DEETYA	Department of Employment, Education, Training and Youth Affairs
DoFA	Department of Finance and Administration
FAG	Financial Assistance Grant
FMA	Financial Management and Accounting (Act)
GDP	Gross Domestic Product
GPP	General Purpose Payment
HFE	Horizontal fiscal equalisation
JCPA	Joint Committee of Public Accounts
JCPAA	Joint Committee of Public Accounts and Audit
NCC	National Competition Council
NCP	National Competition Payment
QPAC	Queensland Public Accounts Committee
RRP	Revenue Replacement Payment
SPP	Specific Purpose Payment
SRA	Special Revenue Assistance

INTRODUCTION

Overview

1.1 This chapter describes Commonwealth financial assistance to the States and Territories.¹ It particularly addresses:

- the overall level of Commonwealth financial assistance and its significance for the States;
- the origins and emergence of fiscal imbalance of Australian federalism;
- the constitutional basis for Commonwealth financial assistance and the basic characteristics of general purpose and specific purpose payments;
- the institutional arrangements for determining general purpose and specific purpose payments; and
- the conditions attaching to these payments.

1.2 The chapter also outlines the background to the terms of reference for the inquiry and the Committee's conduct of the inquiry.

Commonwealth financial assistance to the States

1.3 The Australian States are dependent on funding from the Commonwealth for a significant proportion of their expenditure. Commonwealth payments to the States supplement the States' own-source revenues² and support the

1 The States and Territories are referred to as 'the States' in this report unless otherwise indicated.

2 The States raise revenue through, for example, licence fees, property taxes, payroll taxes, stamp duties and taxes on financial transactions.

delivery of specific services to the community. The Commonwealth also distributes substantial financial assistance *through* the States to educational institutions.³

1.4 Commonwealth payments to and through the State and local government sector are estimated to be \$35.2 billion in 1997-98,⁴ including \$27.7 billion for State governments, \$1.5 billion for local government authorities and \$6 billion for educational institutions.⁵

1.5 The financial assistance provided by the Commonwealth to State and local governments is a significant component of both the outlays of the Commonwealth and the revenues of the other levels of government. It accounted for approximately 20 per cent of the total outlays of the Commonwealth general government sector in 1996-97. It also represented approximately 37 per cent of the total revenues of the State general government sector and 19 per cent of that of the local general government sector.⁶

Emergence of fiscal imbalance

1.6 The relative fiscal imbalance between the Commonwealth and other levels of government that characterises Australian federalism has its origins in the agreement of the framers of the Constitution that exclusive Commonwealth control over customs duties⁷ and excise duties⁸ was essential for the economic union of the federating

3 For an overview of federal fiscal arrangements in Australia, see Budget Paper No.3, *Federal Financial Relations 1997-98*, 1997, especially pp.13-15.

4 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.15.

5 Figures presented throughout this report are rounded. Therefore minor discrepancies may occur between totals and sums of components. The payment estimates have been derived from data in Budget Paper No.3, *Federal Financial Relations 1997-98*, Chart 5, p.15, Table 6, p.22 and Table A2, pp.81-91.

6 These amounts exclude Commonwealth financial assistance to educational institutions distributed through the States. See Budget Paper No.3, *Federal Financial Relations 1997-98*, p.14.

7 A customs duty is a tax imposed on goods when they come into the jurisdiction that imposes tax. A Commonwealth customs duty is therefore a tax on goods that enter Australia.

8 An excise duty is a tax imposed on goods manufactured within a jurisdiction. The term 'excise' is not easily defined. Issues that have

colonies.⁹ The exclusive power of the Commonwealth to impose customs and excise duties is enshrined in section 90 of the Constitution.¹⁰

1.7 A by-product of section 90 was to create a revenue imbalance, or *vertical fiscal imbalance*, between the Commonwealth and the States by preventing the States from imposing certain taxes on goods. The constitutional studies academic Cheryl Saunders has commented that the imbalance has become greater as the definition of *excise duties* has been expanded:

*At the very least, an excise is a tax imposed on goods at the time of their manufacture or production. The definition of excise has gradually been extended by the High Court, however, to the point where a majority of the Court currently accepts that an excise is any tax imposed on goods up to (but probably not including) the point of consumption.*¹¹

1.8 Another factor contributing to the vertical fiscal imbalance between the Commonwealth and the States is the monopoly of the Commonwealth on imposing income tax. While there is no Constitutional bar to the States imposing income tax, the Commonwealth assumed exclusive responsibility for income tax in 1942 as a wartime measure, under a legislative scheme that at the time could be supported by the defence power.¹² Sanctioned by the High Court, the Commonwealth has continued its monopoly over income taxation since then, mainly on grounds other than the defence power.¹³

arisen in relation to the definition of excise duty are discussed in more detail later in this chapter.

9 Arguably, the potential economic benefit to be gained from a single Australian tariff (or customs duty) for overseas trade, together with free trade within Australia, was one of the main motives for Federation. Cheryl Saunders (1997), Annotated Text, *The Australian Constitution*, Constitutional Centenary Foundation, p.90.

10 Section 90 also exclusively empowers the Commonwealth to grant bounties on the production or export of goods.

11 Cheryl Saunders (1997), p.97.

12 Prior to 1942 the States levied income tax at varying levels.

13 Brian Galligan (1995), *A Federal Republic: Australia's Constitutional System of Government*, Cambridge University Press, p.226; Cheryl Saunders (1997), p.90.

1.9 The Commonwealth's ability to levy customs and excise duties and to impose income tax means that the Commonwealth has more money than is needed to meet its direct policy responsibilities and the States have more policy responsibilities and expenditure needs than they can fund from their own revenue sources. The States therefore rely heavily on Commonwealth grants.¹⁴

Types of Commonwealth payments to the States

1.10 All Commonwealth payments to the States are made under section 96 of the Constitution, which provides the constitutional base for distribution of revenue from the Commonwealth to the States. Section 96 gives the Commonwealth Parliament a power to:

grant financial assistance to any State on such terms and conditions as the Parliament thinks fit.

1.11 It follows that the Parliament can discuss and decide the conditions to be attached to financial assistance to the States. There is effectively no limit to the 'terms and conditions' which the Parliament may attach to section 96 grants, beyond clear requirements of the Constitution itself.

1.12 Section 96 is used both for general revenue distribution and for grants for specific purposes.¹⁵ These types of payments are designated as General Purpose Payments (GPPs) and Specific Purpose Payments (SPPs) respectively. The grants are contingent upon the fulfilment of a wide range of terms and conditions.

14 Brian Galligan (1995), p.228.

15 Cheryl Saunders (1997), pp.101-103.

Specific purpose payments

1.13 Specific purpose payments are payments for specific policy purposes which are related to particular Commonwealth or State activities. The SPP payment category encompasses all Commonwealth payments other than GPPs.¹⁶

1.14 The term *specific purpose payment* applies to payments for a wide range of specific purposes, for example, education, health, housing or environmental projects.¹⁷

1.15 The term also has covered a payment from the States to the Commonwealth, programs with similar arrangements to general purpose payments to the States, a loan to the States and a number of payments which relate to the transfer of revenue collected under various regulatory arrangements and generally not subject to conditions.¹⁸

1.16 SPPs to the States were estimated to total \$18.1 billion in 1997-98.

General purpose payments

1.17 General purpose payments are payments for general revenue assistance to the States. They are not directly related to particular Commonwealth or State activities. The Commonwealth provides GPPs as general budget support for the States. The States are not required to use the funds on specific areas of government activity but can use them in accordance with their own priorities. The Commonwealth, however, may stipulate that the States meet certain conditions for receipt of the funds.¹⁹

16 Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, February 1997, p.6.

17 ANAO, *Audit Report No.21 1994-95, Specific Purpose Payments to and through the States and Territories*, p.4.

18 ANAO, *Audit Report No.21 1994-95*, p.4.

19 Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, p.6.

1.18 GPPs are currently paid to the States as:²⁰

- Financial Assistance Grants (FAGs);
- Special Revenue Assistance Grants (SRA), and
- National Competition Payments (NCPs).

Institutional arrangements

1.19 Both general purpose funding and specific purpose funding are determined within the framework which has evolved between the Commonwealth and the States for the management of intergovernmental financial relations.

1.20 The more important institutional arrangements for dealing with general purpose payments are:

- the Premiers' Conference (which pre-dates Federation in 1901);
- the Australian Loan Council (established informally in 1923 and formally in 1927); and
- the Commonwealth Grants Commission (established in 1933).

1.21 The annual Premiers' Conference determines the amount and distribution of general revenue assistance. These payments are subject to negotiation between the Commonwealth and the States. The distribution of GPP funding between the States generally reflects the per capita relativities recommended by the Commonwealth Grants Commission. Relativities are set with a view to compensating the States for relative revenue and expenditure disabilities in their current budgets, in accordance with the *principle of horizontal fiscal equalisation*.²¹

20 These GPP funding categories are discussed in Chapter 3 of this report.

21 The object of fiscal equalisation is to give each State the capacity to provide an average level of services provided it makes a standard effort to raise State taxes and charges and operates at an average level of efficiency. The Commonwealth Grants Commission determines a distribution that enables each State, using comparable revenue effort, to deliver services to residents at a standard not

1.22 The Council of Australian Governments (COAG), established in 1992, is another important element of the institutional framework for intergovernmental relations. COAG is a forum for initiating, developing and implementing policy reforms which are of national significance and which require cooperative action by the States. While the primary purpose of the Premiers' Conference is to settle the level and distribution of general revenue assistance between the States for the forthcoming financial year, COAG facilitates consideration of other issues.²²

1.23 The amount and distribution of specific purpose payments is usually determined in the context of the Commonwealth's Budget deliberations. Discussions concerning SPP programs are undertaken either on a bilateral basis between the Commonwealth and the States, or through more formal channels such as Commonwealth-State Ministerial Councils or Conferences. These Councils or Conferences deal with non-financial matters, as well as the funding of SPP programs.²³

Conditions attaching to SPPs

1.24 Most SPPs are 'tied' grants that are subject to conditions which reflect Commonwealth policy objectives or national policy objectives agreed between the Commonwealth and the States.²⁴ The provision of grants to the States in the form of SPPs is a means for the Commonwealth to pursue its policy objectives in areas where the States are the primary service providers.²⁵

appreciably different from other States. Galligan (1995), p.234. Issues relating to fiscal equalisation principles and methodology are discussed further in Chapter 3 of this report.

22 Meredith Edwards and Alan Henderson, 'Council of Australian Governments: A Vehicle for Reform' in Peter Carroll and Martin Painter (eds), *Microeconomic Reform and Federalism*, Federalism Research Centre, The Australian National University, 1995, pp.22-23.

23 Budget Paper No.4, *Commonwealth Financial Relations with Other Levels of Government 1990-91*, p.9.

24 Budget Paper No.3, *Federal Financial Relations 1998-99*, p.35.

25 Budget Paper No.3, *Federal Financial Relations 1998-99*, pp.14-15.

1.25 Conditions may include:

- general policy requirements on the States (for example, that the States provide free public hospital treatment to Medicare patients as a condition of receiving hospital funding grants);
- a requirement that a payment be expended for a specified purpose (for example, housing assistance for homeless people);
- meeting broad Commonwealth-State agreements covering principles and program delivery mechanisms (for example, the Commonwealth-State Housing Agreement); and
- conditions of joint expenditure programs including project approval, matching grants (for example, dollar-for-dollar contributions) and performance information.²⁶

1.26 Conditions attached to SPPs can limit the ability of State governments to set their own spending priorities. The ability of the States to switch 'tied' grants to purposes other than those stipulated by the Commonwealth is limited because a substantial proportion of SPP funding is for programs in which the Commonwealth either exerts direct control or imposes substantial conditions.²⁷

1.27 Conditions imposed on individual SPPs vary in both degree and form, ranging from the requirement that expenditure be made on specific activities to general policy requirements.²⁸ The extent of the detail of the conditions attached to grants also varies. Ideally, SPP programs have formal agreements which specify the payment conditions, including the States' acceptance of Commonwealth monitoring of the use made of grants and of the effectiveness of assisted projects in achieving program objectives.

26 Budget Paper No.3, *Federal Financial Relations 1998-99*, p.37.

27 Brian Galligan (1995), p.231.

28 ANAO, *Audit Report No.21, 1994-95*, p.4.

Conditions attaching to GPPs

1.28 Although GPPs are 'untied' grants and may be used by the States to meet their own spending priorities, conditions may be attached to the receipt of these funds. Some of the conditions are similar in form to those attached to SPPs. Others, imposed to meet particular Commonwealth purposes, are set out in States Grants (General Purposes) legislation.

1.29 The *States Grants (General Purposes) Act 1994* provides for grants to the States, the Northern Territory and the Australian Capital Territory, and for related purposes. The Act describes the conditions with which the States must comply in order to receive general purpose payments. They are:

- compliance with national competition policy and related reforms in accordance with an agreement executed by the Council of Australian Governments in April 1995;
- payment of the State's share of the costs of any unfunded superannuation liabilities of higher education institutions being discharged in the State;
- compliance with the higher education funding condition; and
- payment by the State of a specified amount of fiscal contribution.²⁹

1.30 Each year amendments to the States Grants (General Purposes) Act are introduced into the Parliament by the Treasurer through a States Grants (General Purposes) Amendment Bill that appropriates funding from consolidated revenue for GPPs.

Context of the inquiry

1.31 The terms of reference for this inquiry arose in the context of debate in the Senate on the States Grants (General Purposes) Amendments Bills during 1997.

29 The payment conditions set out in States Grants (General Purposes) legislation are explained in depth in Chapter 3 of this report.

1.32 The States Grants (General Purposes) Amendment Bill 1997 had two purposes:

- firstly, to put in place arrangements for the provision of general revenue assistance to the States for 1997-98, consistent with decisions reached at the 1997 Premiers' Conference and related agreements with the States; and
- secondly, to provide authority for the Commonwealth to pay the States the revenue it collects under safety net arrangements being implemented to protect State revenues following a High Court decision on State business franchise fees.³⁰

Revenue replacement payments for the States

1.33 As mentioned above, the definition of excise duty is complicated and has been a subject of disagreement between High Court justices. While it had been accepted by the majority of the High Court that an excise is 'any tax imposed on goods up to the point of consumption', there had been:

*one rather precarious exception, for certain types of licence fees for the sale of goods, which [enabled] the States to impose some taxes on sales of liquor, tobacco and petrol.*³¹

1.34 These taxes (or business franchise fees) generated State revenues of around \$5 billion annually.

1.35 The High Court ruling on 5 August 1997 on tobacco franchise fees in New South Wales (*Ha and Lim v. New South Wales* and *Walter Hammond & Associates Pty Ltd v. New South Wales*) cast into doubt the constitutional validity of all State business franchise fees, and the Commonwealth assumed responsibility for their collection.

1.36 Pursuant to the *States Grants (General Purposes) Amendment Act (No 2) 1997*, all revenue collected by the Commonwealth under the safety net arrangements is returned to the States (less administrative costs) as *revenue*

30 Senate *Hansard*, 1 September 1997.

31 Cheryl Saunders (1997), p.97.

replacement payments (RRPs). The States have acknowledged that these arrangements represent State taxes imposed and collected by the Commonwealth at the request and on behalf of the States. The distribution of RRP's between the States was agreed by the States.

Terms of reference for the inquiry

1.37 At the second reading stage, the States Grants (General Purposes) Amendment Bill (No.2) 1997 was agreed to by the Senate, with the following amendment:

At the end of the motion add:

and that the following matter be referred to the Joint Committee of Public Accounts and Audit for inquiry and report by 30 June 1998:

Conditions which may appropriately be attached to:

- (i) *general purpose payments to States; and*
- (ii) *specific purpose payments to States;*

*including conditions relating to the role of State Auditors-General, with particular reference to recent developments concerning the Victorian Auditor-General.*³²

Conduct of the inquiry

1.38 The terms of reference of the inquiry address matters which have been of long-standing interest to the JCPAA and the subject of inquiry over a number of years.³³

1.39 The JCPA conducted a major review of the Australian Audit Office which culminated in Report 296, *The Auditor-General: Ally of the People and Parliament, Reform of the Australian Audit Office*. The Committee took substantial

32 Senate *Hansard*, 26 November 1997, p.9261.

33 Previous inquiries were conducted by the Joint Committee of Public Accounts (JCPA) which, through a legislative change, became the Joint Committee of Public Accounts and Audit (JCPAA) on 1 January 1998.

and comprehensive evidence on the issue of attaching conditions relating to the role of State Auditors-General and made a number of recommendations.

1.40 The Committee again considered this issue in 1994-95 in Report 342, *The Administration of Specific Purpose Payments: A Focus on Outcomes*. In the course of its inquiry into the administration of SPPs:

*The Committee went to considerable lengths to gain information and comments on the administration of SPPs which included: conducting a joint survey with the Australian National Audit Office of SPP administration by the Commonwealth; sending questionnaires to each State and Territory government and inviting their representatives, and others, to appear before the Committee at hearings held in most capital cities.*³⁴

1.41 Report 342 addressed, among other things, the effectiveness of SPP requirements for accountability to Parliament and the need to better define the roles and mandate of Commonwealth and State Auditors-General to audit SPPs. These issues have direct relevance to the current terms of reference.

1.42 The JCPA made 23 recommendations relating to Commonwealth administration of SPPs. The Government responded to the recommendations of the JCPA through a Finance Minute in January 1997.³⁵ The Finance Minute was prepared on the basis of detailed responses from 13 Commonwealth departments. The JCPA was generally

34 JCPA, *Report 342, The Administration of Specific Purpose Payments: A Focus on Outcomes*, November 1995, p.xi.

35 The Government responds to JCPAA reports in two ways:

(i) responses to recommendations concerning administration are provided to the JCPAA in a Finance Minute which is coordinated by the Department of Finance and Administration, and after JCPAA consideration is tabled by the JCPAA in the Parliament; and

(ii) Government responses to policy matters are tabled by the responsible Minister directly in the Parliament.

satisfied with the positive responses of the departments to its recommendations and tabled the Finance Minute in Parliament on 3 June 1997.³⁶

1.43 In the Finance Minute, departments signalled their intention to incorporate recommendations of Report 342 into new or renewed SPP agreements. Some departments indicated that an extended time-frame would be required for the implementation of recommendations as SPP agreements expired over time.

1.44 The Committee recognised in its report that:

*the incorporation of many of its recommendations into SPPs will not be easy, particularly for the large, ongoing SPPs in the health, education and community services areas. Changes of the magnitude recommended in this report need to be implemented at a measured pace and in full consultation with the parties to SPP agreements and those affected by them.*³⁷

1.45 In addition to the JCPA's inquiries into the matters raised in the terms of reference, the Australian National Audit Office (ANAO) has previously conducted a number of pertinent reviews³⁸ and is currently conducting a survey of Commonwealth-State agreements for specific purpose payments.³⁹

1.46 The ANAO survey will provide a longitudinal analysis of progress since the last survey in 1994-95 which was conducted jointly with the JCPA and became the basis of Report 342. It is expected that the ANAO will present its findings to the Parliament in October 1998. The ANAO report

36 House of Representatives *Hansard*, 3 June 1997, p.4690. The JCPAA has the power to re-open an inquiry should it consider the responses unsatisfactory.

37 JCPA, *Report 342*, p.xii.

38 These reviews are listed in Chapter 2 of this report.

39 The ANAO issued the survey on 31 October 1997. Departments were required to return completed surveys on all SPPs administered by them by 1 December 1997.

will then be reviewed by the JCPAA in accordance with the Committee's statutory duty to examine all reports of the Auditor-General.⁴⁰

1.47 Other Parliamentary committees have recently inquired into matters relevant to the terms of reference for the current JCPAA inquiry. In particular, the House of Representatives Standing Committee on Financial Institutions and Public Administration in June 1997 tabled its report entitled *Cultivating Competition: Inquiry into Aspects of the National Competition Policy Reform Package*. The Committee examined the national competition policy reform framework and addressed a number of general issues relating to the reform package. As noted above, some GPP funding elements are provided to the States on condition that they implement national competition policy and related reforms.

1.48 The JCPAA concluded that the previous JCPA and other committee reports, together with the Finance Minute, ANAO reports and other available documentation provide up to date information on conditions which may appropriately be attached to section 96 payments. The Committee therefore has drawn extensively upon these reports in addressing the terms of reference.

1.49 The Committee found the wording of the final part of the terms of reference, that is, 'recent developments concerning the Victorian Auditor-General', to be imprecise. However, the Committee has taken this part of the terms of reference to allude to the review of the *Victorian Audit Act 1994*.

1.50 The Premier of Victoria, as Minister responsible for the *Audit Act 1994*, established an independent committee in December 1996 to undertake a review of the *Audit Act* and report on its findings to the Victorian Government. According to the discussion paper of the review committee, the review was undertaken as part of the Victorian Government's commitment to National Competition Policy.⁴¹ The JCPAA noted that three States, Victoria, New South Wales and Tasmania, listed their audit acts for review under these arrangements. The Australian Capital Territory specifically

40 Pursuant to Section 8(1)(c) of the *Public Accounts and Audit Committee Act 1951*.

41 *Audit Act 1994 Review* (Victoria), Discussion Paper, February 1997.

excluded its audit act from review.⁴² The Commonwealth recently re-wrote its audit act outside of this review framework.

1.51 As mentioned earlier in this chapter, a condition for the receipt of GPPs is the States' compliance with the Agreement to Implement the National Competition Policy and Related Reforms. The Agreement was made by the Council of Australian Governments on 11 April 1995.

1.52 The *Competition Policy Reform Act 1995*, which sets out the main elements of the policy, is complemented by three inter-governmental agreements, including the *Competition Principles Agreement*. This agreement provides a blueprint for future action by all governments.⁴³ It includes an agreement to review regulation restricting competition against a public benefit test. The Agreement committed the Commonwealth, States and Territories to develop a timetable, by June 1996, for the review, and where appropriate, reform of all existing legislation that restricts competition by the year 2000. In Victoria this involves review of 441 pieces of legislation.⁴⁴

1.53 The Victorian Audit Act review culminated in changes to the Act which introduced a competitive framework for public sector audits.⁴⁵ The review and the events leading to changes to the legislation have been a matter of some controversy in Victoria, and some members of the JCPAA share some of these concerns.

1.54 The Committee has not examined the 'recent events concerning the Victorian Auditor-General' because, in the Committee's view, it is a matter which falls within the constitutional jurisdiction of the State of Victoria. The

42 National Competition Council, *Legislation Review Compendium*, April 1997, p.35, p.253, p.288.

43 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition: Inquiry into Aspects of the National Competition Policy Reform Package*, June 1997, p.4.

44 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition: Inquiry into Aspects of the National Competition Policy Reform Package*, p.14.

45 The *Victorian Audit (Amendment) Act 1997* received assent on 16 December 1997.

JCPAA's mandate is limited to the Commonwealth sphere.⁴⁶ For this reason the Committee, in inquiring into the administration of SPPs in 1994-95, did not comment on the administrative practices of the non-Commonwealth parties to SPP agreements.⁴⁷

1.55 While the Committee considers the section of the terms of reference regarding 'recent developments concerning the Victorian Auditor-General' to be imprecise, it is clearly outside the jurisdiction of the Committee and where State executive privilege could be asserted.

1.56 The Committee noted the view of the Premier of Victoria in his response to an invitation from the Senate Select Committee on the Victorian Casino to provide a written submission:

... the State of Victoria is protected by its executive privilege against actions of the Commonwealth which threaten its autonomy or curtail its capacity to function effectively

... the State of Victoria will assert its executive privilege if the Committee attempts to obtain evidence from current or former Ministers or Public Servants, either voluntarily or by compulsion of law.⁴⁸

1.57 Unlike the Senate Select Committee on the Victorian Casino which was unable to continue its inquiry in the absence of information from the Victorian Government, the JCPAA has been able to draw upon sufficient material to address the terms of reference with the exception of the final clause.

1.58 This report provides a very detailed consideration of conditions which may appropriately be attached to specific purpose payments to the States and deals comprehensively with conditions currently attached to general purpose payments. It highlights the nature of problems which have been encountered by State Auditors-General when Commonwealth departments have sought to impose conditions relating to the role of State Auditors-General. The report also

46 The duties of the JCPAA, pursuant to the *Public Accounts and Audit Committee Act 1951*, are set out on page xi of this report.

47 JCPA, *Report 342*, pp.8-9.

48 Cited in the report of the Senate Select Committee on the Victorian Casino Inquiry, *Compelling Evidence*, December 1996, p.39.

suggests possible ways of improving accountability for SPP funding through, for example, the conduct of coordinated or joint performance audits.

Structure of the report

1.59 Following this introductory chapter, Chapter 2 examines SPP program administrative arrangements. The Committee reached a number of conclusions regarding SPP payments and conditions which may appropriately be attached to them.

1.60 The Committee examines conditions which are currently attached to general purpose payments and sets out its conclusions in Chapter 3.

1.61 Chapter 4 discusses some of the implications for State Auditors-General when Commonwealth departments attach particular conditions to SPPs. The scope for coordinated or joint audits of SPP programs by the Commonwealth and State Auditors-General is also addressed in this chapter.

2

SPECIFIC PURPOSE PAYMENTS

Introduction

2.1 This chapter describes important features of specific purpose payments, amplifies the Committee's approach to the examination of specific purpose payments during the current inquiry and discusses conditions which may appropriately be attached to specific purpose payments.

2.2 The chapter specifically addresses conditions concerning:

- the authority for specific purpose payments;
- the roles and responsibilities of parties to specific purpose payment arrangements;
- recognition of the Commonwealth's contribution to specific purpose payments;
- program objectives and requirements regarding financial contributions;
- funds disbursement;
- performance information;
- financial accountability requirements;
- incentives and sanctions;
- evaluations; and
- reporting to Parliament.

Specific purpose payments

Number of SPP programs

2.3 As noted in Chapter 1, Specific Purpose Payments (SPPs) are payments for specific policy purposes which are related to particular government activities. The Commonwealth usually attaches conditions to the use of these funds and generally requires other conditions to be met by the

States or other parties to particular SPP arrangements. The SPP payment category encompasses all Commonwealth payments other than GPPs.¹

2.4 The Commonwealth has a large number of SPP arrangements in place with State governments, local government authorities and educational institutions. On available information, the Committee estimates that there are currently around 97 SPP programs.²

2.5 The overall number of SPPs appears to have remained relatively constant since the 1995 JCPA inquiry. The joint ANAO-JCPA survey of SPPs identified 92 SPPs in existence in 1994.³

2.6 There has continued to be some turnover in individual SPPs in recent years. This reflects the cessation of old SPPs that have reached the end of their agreed funding period and the establishment of new SPPs to promote current government policy interests and objectives and to respond to new funding needs.⁴

1 Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, p.6.

2 SPP programs are listed in two official sources: the Department of Finance catalogue of SPPs, last issued in February 1997, and the annual Budget Paper No.3.

The 1996-97 Finance catalogue provided a summary list of 90 SPPs paid to or through the States. See Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, pp.1-4. This was not an exhaustive list of SPPs as it did not include SPPs paid directly to local government authorities.

The 1997-98 Budget Paper No.3 contained tables showing SPPs paid to the States and SPP paid direct to local government authorities. Current and capital SPP payments were presented separately. There appeared to be seven discrete SPPs involving payments direct to local governments in 1997-98. However, the number of SPPs either paid to or through the States or paid direct to local government cannot be determined conclusively from these lists. See Budget Paper No.3, *Federal Financial Relations 1997-98*, especially Table A4, p.95.

3 ANAO, *Audit Report No.21 1994-95, Special Purpose Payments to and through the States and Territories*, p.4.

4 Details of changes to particular SPPs since 1993-94 have been briefly noted in Finance SPP catalogues. See Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1995-96*, February 1996, pp.12-14 and Department of Finance,

Outlays on SPP programs

2.7 SPPs involve very large Commonwealth outlays. SPP payments to and through the States were estimated to amount to \$18.1 billion in 1997-98. This was equivalent to around 52 per cent of total gross Commonwealth payments to the States.⁵

2.8 The SPP share of total Commonwealth payments to the States has increased over the last twenty years, by around seven percentage points. The relatively more generous funding escalation arrangements applied to SPPs compared to GPPs has been identified as the principal reason for this. A slight decline in the SPP share was expected in 1997-98, due to the effect of several special one-off factors.⁶

Purposes of SPPs

2.9 The majority of SPPs exist to support the provision of various kinds of specific services to the Australian community. SPP arrangements enable the Commonwealth to pursue its policy objectives as well as discharge its responsibilities in specific functional areas of government activity. SPPs provide a framework for the Commonwealth and other parties to work together in the program management, funding and delivery of important services.⁷

Catalogue of Specific Purpose Payments to the States and Territories 1996-97, pp.12-14.

5 In addition, the Commonwealth expected to make SPP payments amounting to \$0.2 billion directly to local government authorities in 1997-98. This is discussed further below. See Budget Paper No.3, *Federal Financial Relations 1997-98*, pp.38-39, Table A4, p.95.

6 Budget Paper No.3, *Federal Financial Relations 1997-98*, Chart 7, p.39.

7 Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, p.6; Budget Paper No.3, *Federal Financial Relations 1997-98*, p.14.

2.10 The SPP payment category also covers a diverse range of payments made to the States for other purposes. These include a small number of SPPs established either to share revenues with the States under particular regulatory arrangements or to provide compensation to the States for Commonwealth actions affecting State government finances.⁸

Functional areas assisted by SPP programs

2.11 SPPs provide financial assistance across a wide spectrum of government activities.⁹ The largest number of SPPs are in the health area. Social security and welfare; education; agriculture, forestry and fishing; and housing and community amenities are other areas assisted through many SPPs.¹⁰

2.12 The largest SPP funding allocations are in the education and health areas. Local government; social security and welfare; and housing and community amenities also receive major financial assistance through SPPs.¹¹

8 ANAO, *Audit Report No.21 1994-95*, p.4; Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, p.6.

9 Individual SPP programs are classified using the standard functional classification for all government outlays presented in annual budget papers. See Budget Paper No.3, *Federal Financial Relations 1997-98*, p.49.

10 Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, pp.1-4.

11 Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, pp.9-11; Budget Paper No.3, *Federal Financial Relations 1997-98*, Chart 8, p.40.

Table 1

**Specific Purpose Payments to and through the States,
1996-97**

Functional area (see Note 1)	Number	Amount (\$'000)
Education	8	7 070 001
Health	23	5 304 124
Not allocated to function - general public services and other purposes (see Note 2)	10	2 243 395
Social security and welfare	11	1 151 469
Housing and community amenities	7	1 044 290
Transport and communication	4	851 820
Public order and safety	5	653 174
Agriculture, forestry and fishing	8	247 902
Other economic affairs	2	30 774
Mining, manufacturing and construction	5	17 299
Recreation and culture	5	14 812
Tourism and area promotion	1	3 000
Fuel and energy	1	1 085
Total SPPs	90	18 633 145

Source: Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, pp.1-4, pp.9-11.

Note 1: The Catalogue did not classify SPP payments through the States by functional area. Those payments have been classified in this table, drawing on their classification in Budget Paper No.3, *Federal Financial Relations 1997-98*, Table A1, pp.50-79.

Note 2: Local government financial assistance in this category amounted to \$1 216 416 000.

Means of distributing SPP funds

2.13 SPPs are distributed in three ways: *to* the States, *through* the States to other agencies including local government, and *direct to* local government authorities.¹²

2.14 *SPPs to the States* are payments made direct to the States to fund specific government activities. The overwhelming majority of SPPs are in this category and account for the bulk of SPP funds.¹³ SPP payments to the States were estimated to total \$10.9 billion in 1997-98.¹⁴

2.15 *SPPs through the States* are payments to the States that are passed on to other agencies. Universities, non-government schools and local government authorities are currently assisted under these SPP arrangements, which have minimal impact on State governments. There are only a small number of SPPs paid through the States, but each one involves relatively large amounts of Commonwealth financial assistance. SPP payments through the States were expected to amount to \$7.2 billion in 1997-98.¹⁵

2.16 *SPPs direct to local governments* are payments made directly to local government authorities to fund specific government activities. These SPPs are separate from SPPs through the States that provide general revenue assistance to local government.¹⁶ SPPs direct to local governments are the smallest of the three SPP funding categories, with payments expected to be worth \$0.2 billion in 1997-98.¹⁷

12 Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, p.7; Budget Paper No.3, *Federal Financial Relations 1997-98*, p.37.

13 The Department of Finance's 1996-97 SPP catalogue listed 85 SPPs to the States, compared with 5 SPPs through the States. See Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, pp.1-4.

14 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.39.

15 Budget Paper No.3, *Federal Financial Relations 1997-98*, pp.38-39.

16 Budget Paper No.3, *Federal Financial Relations 1997-98*, pp.34-35.

17 Budget Paper No.3, *Federal Financial Relations 1997-98*, Table A4, p.95.

Conditions attached to SPPs

2.17 Conditions attached to SPP funding are a key feature of most SPPs. Conditions in individual SPPs can vary considerably, in terms of the range of matters covered and the extent of flexibility and discretion afforded to the parties. SPP conditions may range from basic financial certification requirements that funds be expended on specified activities to more comprehensive frameworks for SPP program administration.¹⁸

2.18 SPPs may require the parties to comply with a range of program conditions including requirements relating to program objectives and strategies, consultative arrangements, program delivery mechanisms, program funding, community access to services and performance and financial accountability arrangements.¹⁹

Committee approach

2.19 The Committee reviewed coverage of SPP conditions in previous JCPA reports, audit reports on SPP administration and the responses of Commonwealth departments to those reports. The Committee considered references to SPP arrangements in recent reports of other parliamentary committees, government agencies and official inquiries. The Committee also examined coverage of SPP issues in a number of specialist public administration journals as well as academic publications.

Previous reviews

2.20 Four reports and documents were of particular relevance to the Committee's current consideration of SPP conditions:

18 ANAO, *Audit Report No.21 1994-95*, p.5; Budget Paper No.3, *Federal Financial Relations 1997-98*, p.37.

19 Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, p.6; Budget Paper No.3, *Federal Financial Relations 1997-98*, pp.37-38.

- Audit Report No.6 1993-94 (September 1993) provided ANAO commentary on important features and practices in the administration of Commonwealth-State agreements.²⁰
- Audit Report No.21 1994-95 (February 1995) documented the results of a survey of SPPs conducted jointly by the ANAO and the JCPA.²¹
- JCPA Report 342 (November 1995) set out the Committee's findings and recommendations regarding the administration of SPPs.²²
- Finance Minute on Report 342 (January 1997) contained the responses of 13 Commonwealth departments to the JCPA report on SPP administration.²³

2.21 JCPA Report 342 was the culmination of a very comprehensive Committee inquiry into Commonwealth administration of SPPs. The JCPA took written and oral evidence from Commonwealth departments, State governments, Auditors-General, community organisations and individuals with an interest in SPP programs.²⁴ It also made extensive use of the results of the joint ANAO-JCPA survey of SPPs mentioned above.

2.22 The JCPA concluded that the Commonwealth should strengthen its focus on strategic planning and performance assessment for SPPs. This required the articulation of SPP objectives in terms of measurable outcomes in the community and the assessment of performance towards meeting those objectives. The JCPA also

20 ANAO, *Audit Report No.6 1993-94, An Audit Commentary on Aspects of Commonwealth-State Agreements*, September 1993.

21 ANAO, *Audit Report No.21 1994-95, Special Purpose Payments to and through the States and Territories*, February 1995.

22 JCPA, *Report 342, The Administration of Specific Purpose Payments: A Focus on Outcomes*, November 1995.

23 Department of Finance, *Finance Minute on JCPA Report 342, The Administration of Specific Purpose Payments: A Focus on Outcomes*, January 1997. The Finance Minute was presented to the Parliament in June 1997. See House of Representatives *Hansard*, 3 June 1997.

24 The inquiry received 53 submissions and held 10 public hearings in Canberra and the State capitals. See JCPA, *Report 342*, p.9.

proposed that the Commonwealth progressively disengage from SPP micro-management, leaving this task to State governments and other parties to SPP agreements.²⁵

2.23 The JCPA argued that many SPPs needed to be considerably reformed if they were to be efficient, effective and provide high quality service to the community. Throughout Report 342, the JCPA identified a number of features of SPPs that, when taken together, would characterise an 'ideal' SPP agreement:

- clear roles and responsibilities for each party to the agreement;
- objectives expressed in terms of measurable outcomes;
- primary accountability to the Commonwealth being for outcomes achieved rather than inputs and processes;
- performance indicators linked to each objective;
- data collection requirements linked to each performance indicator;
- details of performance incentives and graduated sanctions; and
- Commonwealth acquittals based on audited financial statements.²⁶

2.24 The JCPA made a number of recommendations for the incorporation of these principles in SPP agreements. It recognised that this would not be easy, particularly for the large, ongoing SPPs in the health, education and community services areas. Change needed to be implemented at a measured pace and in full consultation with the parties to SPP agreements and those affected by them.²⁷ Commonwealth departments administering SPPs indicated that they were generally supportive of the principles.²⁸

25 JCPA, *Report 342*, p.xi.

26 For convenience, the desirable SPP features have been re-arranged here to correspond to their order of presentation in the main body of Report 342, rather than as they are listed in the summary appearing in the concluding chapter of the Report; see JCPA, *Report 342*, pp.99-100.

27 JCPA, *Report 342*, p.xii, p.100.

28 House of Representatives *Hansard*, 3 June 1997.

Current inquiry

2.25 From examination of the range of available reference sources addressing SPP issues, including Report 342, the Committee concluded that there was sufficient information on SPP arrangements on hand for the Committee to identify conditions which may appropriately be attached to SPPs.

2.26 The Committee is aware that the ANAO is currently conducting a further audit of SPP performance information. Updated survey data on SPPs is being collected as part of the audit and will be included in the audit report, expected to be finalised by October 1998. The Committee will consider the forthcoming report as part of its statutory examination of all audit reports and determine whether the issues and findings raised in the report warrant further examination in a public hearing.

2.27 The Committee believes that the ideal SPP features identified in Report 342 are still generally relevant to contemporary SPP program design and management. Accordingly, in this chapter, the Committee restates and expands its previous list of desirable SPP features and also amplifies its views on a number of features in light of more recent information or commentary on particular issues.

2.28 The Committee considers that the desirable SPP features generally can be applied across the range of SPPs. At the same time, it recognises the diverse nature of the programs and activities that receive Commonwealth financial assistance under SPP agreements. Specific conditions incorporated in individual SPP agreements need to be tailored to meet the nature of each program and the requirements of the parties to the agreement. It is therefore important that Commonwealth departments continue to assess the relevance and appropriateness of the desirable features identified by the Committee to particular SPPs under their administration.

Authority for specific purpose payments

2.29 Various forms of authority have been used as a basis for SPP administration. These include Commonwealth and State legislation, agreements and memoranda of understanding, as well as Cabinet decisions and exchanges of correspondence. Particular SPP agreements may involve combinations of these forms of authority. Payments to the States pursuant to SPP agreements are made under specific SPP legislation where applicable, or general Appropriation Acts.²⁹

2.30 The joint ANAO-JCPA survey of SPPs found that most SPPs in existence in 1994 were administered under the authority of agreements or legislation. Other SPPs relied solely on exchanges of correspondence, Cabinet decisions or some other means for their authority. The ANAO expressed concern that the latter forms of authority would not provide an adequate basis for good program management.³⁰

Current situation

2.31 Examination by the Committee of the current Finance catalogue of SPPs indicates that some SPPs are not based on formal agreements or specific legislation.³¹

2.32 The Committee believes that, as a general principle, SPPs should be the subject of at least formal written agreements. An agreement usually will provide a more effective form of authority than an exchange of correspondence, in setting out SPP arrangements in a systematic and comprehensive manner. In addition, by signing SPP agreements the Commonwealth and the States demonstrate clearly their mutual acceptance of the specified conditions applying to Commonwealth financial assistance.

29 ANAO, *Audit Report No.6 1993-94*, p.5; ANAO, *Audit Report No.21 1994-95*, p.23, Figure 9, p.25.

30 ANAO, *Audit Report No.21 1994-95*, p.xi, p.23, Figure 9, p.25.

31 Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*.

2.33 The Committee considers that it is desirable for any SPP programs involving substantial Commonwealth financial assistance or having national significance to have a legislated basis. Parliamentary scrutiny of the design and administration of such SPP programs is crucial.

Specification of the roles and responsibilities of the parties

2.34 Many SPPs exist to provide services to the Australian community, through cooperation between the Commonwealth and other parties including State and local governments, educational institutions and community agencies.³² Administration of these SPPs requires a range of program management activities to be performed by one or other party, or shared between the parties.³³

2.35 These activities include the establishment of broad policy and objectives; strategic program planning; service delivery planning; actual program delivery; performance monitoring and financial reporting.³⁴ Effective arrangements for communication and consultation between the parties are also essential for efficient and effective service delivery.³⁵

2.36 JCPA Report 342 observed that many SPP agreements did not contain a short, clear in-principle statement of the roles and responsibilities of each party. It recommended that Commonwealth departments ensure that SPP agreements include such a statement.³⁶ Departments generally advised through the Finance Minute process that they supported the recommendation. Some departments mentioned that SPPs under their administration already included these details.³⁷

32 JCPA, *Report 342*, p.14.

33 ANAO, *Audit Report No.6 1993-94*, p.5; JCPA, *Report 342*, p.15.

34 ANAO, *Audit Report No.6 1993-94*, p.5; JCPA, *Report 342*, pp.14-15.

35 ANAO, *Audit Report No.6 1993-94*, p.12; JCPA, *Report 342*, p.19.

36 JCPA, *Report 342*, p.18.

37 Department of Finance, *Finance Minute*, paras.19-34.

2.37 Report 342 also referred to ANAO-JCPA survey findings that many SPP agreements did not identify the communication and consultation arrangements to operate between the parties. The Report recommended that Commonwealth departments ensure that SPP agreements clearly indicate these arrangements.³⁸ Departments supported the recommendation.³⁹

2.38 Report 342 went on to detail an ideal division of specific program management activities between the Commonwealth and other parties to SPP agreements. It noted that this was a generic framework and the extent of its applicability to individual SPPs would depend on the nature of the SPP programs.⁴⁰

Policy development and strategic planning

2.39 Report 342 proposed that the Commonwealth be primarily responsible for developing the broad policy and objectives for SPPs, as well as for setting national service standards.⁴¹ The Commonwealth should also have primary responsibility for strategic planning associated with the attainment of SPP objectives, particularly where SPPs are ongoing and complex.⁴² The Report emphasised the importance of Commonwealth consultation with the other parties to agreements, as well as other relevant stakeholders, regarding program objectives and strategic planning.⁴³

38 JCPA, *Report 342*, p.19.

39 Department of Finance, *Finance Minute*, paras.35-45.

40 JCPA, *Report 342*, p.19.

41 JCPA, *Report 342*, p.19.

42 Strategic planning refers to the financial management, resource allocation, information distribution and coordination necessary to achieve SPP objectives at the national level. It includes such tasks as the development of national strategic plans; the specification and maintenance of national data collection systems; and the commissioning and funding of research for policy development. The development of appropriate service delivery structures to ensure basic national consistency may also be part of strategic planning for some SPPs. See JCPA, *Report 342*, p.21.

43 JCPA, *Report 342*, pp.20-21.

Service delivery planning

2.40 Report 342 observed that the extent of any Commonwealth involvement in the planning of the delivery of SPP-funded services was a contentious issue.⁴⁴ In principle, the Commonwealth had recently agreed that the States should have primary responsibility for this aspect of program management. The ANAO-JCPA survey found that Commonwealth departments still had input to service delivery planning under many SPP agreements. However, the States were being vested with sole responsibility for service delivery planning under some new agreements. These arrangements allowed the States more flexibility in the delivery of SPP-funded services.⁴⁵

2.41 The Report supported greater autonomy for the States in service delivery planning, provided that there were arrangements in place for State accountability to the Commonwealth for service delivery performance as well as a framework of sanctions in the event of State non-compliance with the terms of SPP agreements. Accordingly the Report recommended that Commonwealth departments ensure that SPP agreements do not prescribe the method of service delivery, where arrangements are in place for accountability to the Commonwealth for service delivery performance and outcomes.⁴⁶ Departments generally supported the recommendation.⁴⁷

44 Service delivery planning involves the design, resource and financial management and coordination necessary for efficient service delivery. This includes ensuring that parties delivering services comply with service standards and that they remain financially accountable, and identifying where new or different service delivery strategies are needed and developing them. See JCPA, *Report 342*, p.23.

45 JCPA, *Report 342*, Table 2.2, p.22, pp.23-25.

46 ANAO, *Audit Report No.21 1994-95*, p.30; JCPA, *Report 342*, pp.24-25.

47 Department of Finance, *Finance Minute*, paras.46-58.

Other important program management responsibilities

2.42 Report 342 referred to the responsibilities of the Commonwealth and other parties in relation to three other important performance management activities: service delivery, the monitoring and assessment of performance, and the preparation of financial data and other accountability documents.

2.43 The Report noted that the Commonwealth was not involved in the actual delivery of SPP-funded services. The Commonwealth delivered its own programs through Commonwealth Own Purpose Outlays, not through SPPs.⁴⁸

2.44 The Report stated that the Commonwealth should have primary responsibility for assessing the performance of SPPs towards meeting national objectives. The Commonwealth and the other parties to SPP agreements should agree on data collection requirements and it should then be the responsibility of the other parties to provide the data to the Commonwealth.⁴⁹

2.45 The Report also proposed that the Commonwealth accept the audited annual financial statements of grant recipients, with appropriate annotations, as adequate for ensuring financial accountability for SPPs.⁵⁰

Recognition of the Commonwealth's contribution

2.46 The roles of the Commonwealth and other parties involved in SPP programs providing services to the Australian community need to be adequately recognised.⁵¹

2.47 Report 342 emphasised the importance of appropriate recognition of the Commonwealth's contribution to SPPs. It noted ANAO-JCPA survey findings that most SPPs did not specify arrangements for recognition of the contribution of the parties to SPPs. The Report recommended

48 JCPA, *Report 342*, pp.25-26.

49 JCPA, *Report 342*, p.27.

50 JCPA, *Report 342*, p.27.

51 ANAO, *Audit Report No.6 1993-94*, p.14; JCPA, *Report 342*, p.26.

that Commonwealth departments ensure that SPP agreements require that the Commonwealth's contribution is recognised in application documentation, approval announcements, media releases, official openings, signs, plaques and other program publicity.⁵²

2.48 Departments generally supported the recommendation. However, some departments including the Department of Employment, Education, Training and Youth Affairs (DEETYA) mentioned particular circumstances where recognition of the Commonwealth's contribution might be inappropriate or impracticable.⁵³ DEETYA stated that it supported the need for appropriate recognition of Commonwealth funding and would seek to incorporate this recommendation where applicable in SPP arrangements. It also said that recognition arrangements such as those outlined in the recommendation were not appropriate in SPP programs such as general recurrent grants for schools, where Commonwealth funds were not tied to a specific activity or location.⁵⁴

Committee comment

2.49 The Committee believes that recognition arrangements are appropriate to the full range of SPP-funded services. The actual form of recognition may need to vary according to the nature of the SPP program and the Commonwealth's contribution. In the case of SPP programs involving ongoing general Commonwealth financial assistance, the Commonwealth's role at the very least can be appropriately acknowledged in official program statements and reports issued by other parties to the SPP agreements.

52 ANAO, *Audit Report No.21 1994-95*, p.30; JCPA, *Report 342*, p.26.

53 Department of Finance, *Finance Minute*, paras.59-69.

54 Department of Finance, *Finance Minute*, para.60.

Program objectives and requirements regarding financial contributions

2.50 The Commonwealth and other parties enter into SPP agreements to achieve benefits for the Australian community at minimal cost.

2.51 Report 342 drew attention to the importance of setting clear national objectives for SPPs and phasing out of SPP agreements any inappropriate requirements regarding the financial contributions of the parties. It addressed these issues using an accepted framework for analysing program performance in terms of program objectives, inputs, outputs and outcomes.⁵⁵

Increasing the focus on objectives

2.52 The Report proposed that SPPs should be structured and administered in such a way as to focus on their objectives. SPPs needed objectives expressed in terms of clear, achievable and measurable outcomes.⁵⁶

2.53 The Report noted that increasing effort was being made to describe SPP objectives in terms of measurable outcomes, particularly in relation to health, housing and higher education programs.⁵⁷ The JCPA recognised that it was not so easy to define measurable outcomes for some SPP programs and that their development would take time and require wide consultation between the parties.⁵⁸

55 These terms can be defined as follows:

Objectives:	The desired benefits to the community from the program.
Inputs:	The resources used for the program.
Processes:	The activities that produce or support the outputs.
Outputs:	The products or services which are produced in order to achieve the objective.
Outcomes:	The effect of the program on the community.

See JCPA, *Report 342*, p.36, Table 3.1, p.37 and Table 3.2, p.38.

56 JCPA, *Report 342*, p.39, p.41.

57 JCPA, *Report 342*, p.41.

58 JCPA, *Report 342*, pp.41-42.

2.54 The Report recommended that Commonwealth departments ensure that SPP agreements contain a statement of why the parties are entering the agreement and concise statements of what the SPP is trying to achieve, expressed in terms of measurable outcomes. It also recommended that Commonwealth departments draw up a publicly available timetable for the incorporation of these statements of national objectives in existing agreements that lacked them.⁵⁹

2.55 Departments generally supported adoption of the recommendation when existing agreements were re-negotiated or new agreements were made.⁶⁰ DEETYA indicated some reservations about the recommendation. It said that it would adopt the recommendation where applicable for SPPs under its administration. It also mentioned that it was continuing efforts, particularly in relation to schools programs, to improve the focus on outcomes in SPP arrangements. However, it considered that it would be simplistic to assume that all objectives could be expressed in readily quantifiable terms and supported by numerical targets. It noted that the process of developing robust outcomes measures was complex and iterative and that it would not be feasible to have such measures in place across all objectives for the next round of agreements with the States or for the Commonwealth to give firm commitments to a timetable for their development.⁶¹

2.56 The Committee recognises the difficulties associated with the expression of objectives in terms of measurable outcomes, but believes that changes can be realised through sustained cooperative effort of the parties to SPP agreements.

2.57 In this regard the Committee notes that a new Commonwealth-State Housing Agreement (CSHA) which was being negotiated at the time of the JCPA inquiry, came into effect in 1996. The CSHA introduced a number of reforms in the provision of housing assistance under SPP arrangements, including the specification of national housing objectives and the reporting of program performance and outcomes in terms of agreed performance measures.⁶²

59 JCPA, *Report 342*, p.42.

60 Department of Finance, *Finance Minute*, paras.71-89.

61 Department of Finance, *Finance Minute*, paras.71 and 73.

62 Department of Social Security, *Housing Assistance Act 1989 Annual Report 1995-96*, p.14; Department of Social Security, *Annual Report*

Phasing out requirements regarding financial contributions

2.58 Report 342 proposed that requirements regarding the financial contributions of the parties (input controls) be phased out of SPP agreements, as arrangements for setting SPP objectives and for measuring progress towards achieving these objectives were incorporated in agreements. Input controls would be inappropriate as Commonwealth attention shifted to accountability for what was achieved (outcomes) rather than how it was achieved (processes and outputs).⁶³

2.59 The Report noted a continuing Commonwealth preoccupation with the activity associated with SPPs rather than the results of the activity. The Commonwealth controlled SPP activities - the processes and inputs - through attaching conditions to the use of SPP inputs.⁶⁴ These input controls usually took the form of maintenance of effort clauses, matched funding requirements or administrative caps in SPP agreements.⁶⁵

2.60 Report 342 identified two main reasons for the use of input controls. In the absence of outcome measurement, they might be the only way to keep other parties accountable for their use of Commonwealth funds. Input controls also aimed to prevent the States from withdrawing their existing funding for particular activities in response to the infusion of Commonwealth financial assistance under SPP arrangements.

1996-97, p.192; Senate Community Affairs Reference Committee, *Report on Housing Assistance*, December 1997, pp.17-18.

63 JCPA, *Report 342*, p.43, p.48.

64 JCPA, *Report 342*, p.43.

65 These input controls can be described as follows:

Maintenance of effort clauses require States to maintain their existing level of expenditure on program activities as a condition for receiving Commonwealth funds for the SPP program.

Matched funding arrangements require States to provide a certain level of funds to match Commonwealth funds for the SPP program. Complex formulae may be used to determine the State contribution.

Administrative caps limit the percentage of Commonwealth funds that can be applied for SPP administrative purposes.

See ANAO, *Audit Report No.6 1993-94*, p.9; JCPA, *Report 342*, p.45.

The Report noted that the latter concern was part of the wider practice known as 'cost shifting', where States try to use Commonwealth-funded programs instead of State-funded programs to deliver services.⁶⁶

2.61 The Report pointed out that, even though input controls did restrict cost shifting under existing SPP agreements, they had several disadvantages. SPP programs providing services to the community could suffer the double blow of losing Commonwealth funds simply because they had already lost State funding. Input controls also limited the incentive for the States to improve the efficiency of program activities and did not allow the States the flexibility to move funds between program elements within SPPs to ensure that overall objectives were achieved.⁶⁷

2.62 The Report recognised that the Commonwealth would continue to rely on input controls in SPP agreements while the potential for cost shifting existed. Accordingly the Report recommended that Commonwealth departments should ensure that input controls are phased out of existing SPP agreements at the same time as performance agreements are phased in, and that new SPPs which incorporate performance agreements not include input controls.⁶⁸

2.63 Departments had a wide range of responses to these recommendations. A number of departments indicated their intention to pursue the recommendations, or at least their support for the thrust of the recommendations, while noting the practicalities of their current reliance on input controls. Some departments suggested that SPP input controls might continue to be appropriate in some cases. Other departments expressly or implicitly disagreed with the recommendations on the basis that input controls were integral features of SPPs currently under their administration.⁶⁹

2.64 The Committee takes note of the responses of the Departments and accepts that there may be some circumstances where it is not feasible or desirable to phase out input controls and incorporate outcome-focused performance agreements in SPPs.

66 JCPA, Report 342, p.43.

67 JCPA, Report 342, p.47.

68 JCPA, Report 342, p.48.

69 Department of Finance, Finance Minute, paras.90-116.

Specification of requirements regarding financial contributions

2.65 Where the Commonwealth continues to rely on SPP input controls, the Committee believes that appropriate attention needs to be given to improving the specification of the respective financial contributions of the parties in SPP agreements. In the case of SPPs with matched funding requirements, the funding formula to be applied, the funds which are to be matched and the types of expenditure that qualify for inclusion as matching funds need to be clearly identified and defined.⁷⁰

2.66 The Committee notes the finding of the ANAO-JCPA survey that key features of matched funding requirements were not included in many SPP agreements in existence in 1994.⁷¹ The Committee awaits the results of the ANAO's further survey of SPPs, to see whether there has been any recent improvement in this area. "

2.67 The Committee considers that SPP agreements should contain detailed specifications of any matched funding requirements and other forms of input controls.

Funds disbursement

2.68 The Commonwealth disburses SPP funds to other parties under various financial arrangements. Payments are made in advance, progressively when milestones are reached, as reimbursements, in response to expenditure by the other parties, or through some combination of these. The timing of the transfer of SPP funds can significantly affect the day to day account balances of the Commonwealth and the other parties to SPP agreements. From the Commonwealth perspective, the pattern of SPP funds disbursement can put pressure on its cash holdings and contribute to the need for short-term borrowing to cover any cash shortfalls.⁷²

70 ANAO, Audit Report No.6 1993-94, p.9.

71 ANAO, Audit Report No.21 1994-95, pp.36-37.

72 ANAO, Audit Report No.21 1994-95, p.33; JCPA, Report 342, p.84.

2.69 Report 342 highlighted the finding of the joint ANAO-JCPA survey of SPPs that considerable SPP funds were paid in advance. The ANAO estimated that in 1994, in-advance payments of at least \$4.2 billion and up to \$9 billion were made under SPP arrangements.⁷³

2.70 The Report noted reviews had recently been undertaken by the ANAO and the JCPA into the Commonwealth's cash management practices with a view to minimising its recourse to short-term borrowing.⁷⁴ The Report also referred to the recent establishment of a task force to examine cash management aspects of payments to Commonwealth statutory authorities and specific purpose payments to the States.⁷⁵

2.71 The Report recommended that Commonwealth departments administering SPPs liaise with the Department of Finance to determine whether payments are being made on an optimal schedule and dates to minimise the Commonwealth's recourse to short-term borrowing.⁷⁶ It also recommended that departments investigate whether there are any unnecessary delays in the transfer of SPP funds through the States to other parties.⁷⁷

2.72 Departments generally supported the recommendations. Some departments qualified their responses, noting that the particular funding requirements of individual SPPs needed to be taken into account and that the agreement of other SPP parties would be required to revise existing payment schedules.⁷⁸

73 ANAO, *Audit Report No.21 1994-95*, p.33; JCPA, *Report 342*, pp.85-86.

74 JCPA, *Report 342*, p.84. For further reference to the reviews, see ANAO, *Audit Report No.22, 1993-94, Cash Management in Commonwealth Government Departments*; JCPA, *Report 342, Cash Matters: Cash Management in the Commonwealth*, October 1995.

75 JCPA, *Report 342*, p.85. For further reference to the establishment of the Easson task force on payments to the statutory authorities and the States, see Department of Finance, *Annual Report 1995-96*, p.52.

76 JCPA, *Report 342*, p.85.

77 JCPA, *Report 342*, p.87.

78 Department of Finance, *Finance Minute*, paras.234-259.

2.73 The Department of Finance set out its views regarding the scheduling of SPP payments in its responses to the JCPA inquiry and the earlier audit report on the joint ANAO-JCPA survey of SPPs. It advised the ANAO that SPP payments should be based on SPP program cash flow needs and, unless impractical, should be made following one of the Commonwealth tax revenue peaks in any month.⁷⁹ In commenting on the JCPA recommendation, Finance noted that the task force report had been submitted to the Government for consideration and the outcome of that consideration might have some bearing on the issue. It also said that it would be necessary to ensure that payment arrangements were consistent with SPP reforms being pursued through the Council of Australian Governments.⁸⁰

2.74 The Department of Finance noted that Commonwealth payments for some of the larger SPPs were timed to meet specific obligations of the States, such as to pay salaries. It said that it might not be practical to align SPP payments with Commonwealth revenue peaks, notwithstanding the cash management benefits to the Commonwealth of meeting this objective.⁸¹

Further developments

2.75 The task force on payments to statutory authorities and the States consulted with Commonwealth authorities and State government bodies between August and December 1995 and provided its report to the Minister for Finance in January 1996. The task force found that there was a cost to the Commonwealth in allowing payments to be made to authorities and the States in advance of their expenditure needs. Accordingly the task force recommended that the Government should exercise a reasonable level of control over cash draw-downs to ensure that authorities and the States (in relation to SPPs) did not accumulate surplus cash. It also

79 ANAO, *Audit Report No.21 1994-95*, p.34; JCPA, *Report 342*, p.84.

80 Department of Finance, *Finance Minute*, para.234.

81 Department of Finance, *Finance Minute*, para.235.

found that there was a serious lack of transparency in relation to SPPs, which made it difficult to track Commonwealth payments once they had been made to the States.⁸²

2.76 New payment arrangements for major Commonwealth statutory authorities were implemented during 1996-97 to avoid their accumulation of excess cash balances. The Department of Finance indicated that similar cash management principles would be applied in future negotiations for SPPs to the States.⁸³

Committee comment

2.77 The Committee notes that the potential for the Commonwealth to achieve dollar savings through improved cash management practices has now been recognised for a number of years. The application of these practices to SPP funds disbursement is in train.

2.78 The Committee considers that it is imperative that Commonwealth departments administering SPPs, in conjunction with the Department of Finance and Administration, actively pursue the introduction of revised payment schedules to ensure funds are released no earlier than necessary to meet identified immediate funding needs of other parties in relation to SPP programs.

Performance information

2.79 SPP performance information measures the extent to which the objectives of SPP programs have been achieved and the funds and other resources allocated to SPP programs have been used in an efficient manner to meet those objectives.⁸⁴

82 Department of Finance, *Annual Report 1995-96*, p.52.

83 Department of Finance, *Annual Report 1996-97*, p.23. See also Department of Finance, *Estimates Memorandum 1997/18-Review of Cash Management of Specific Purpose Payments (SPPs) to the States and Territories*, April 1997.

84 JCPA, *Report 342*, pp.49-50.

2.80 Report 342 focused on the need to specify suitable performance indicators for SPP programs and to have common management information systems to enable the collection of comparable SPP data in a consistent format.

Performance indicators

2.81 Report 342 observed that performance information for SPP programs tended to measure program inputs, processes and outputs, rather than program outcomes. Such data was often not adequate to monitor program performance or support strategic planning for SPPs.⁸⁵

2.82 The Report noted that the measurement of SPP performance can be a complex task, particularly when SPPs have multiple objectives which are hard to quantify. Outcomes may take time to become evident and also are potentially influenced by other factors outside of SPP programs.⁸⁶

2.83 The Report recognised departmental efforts being made to develop and refine suitable performance indicators for SPP programs. It also particularly highlighted the work of the steering committee for the review of Commonwealth-State service provision. This review aimed to develop agreed national performance indicators for a number of major service provision programs funded under SPP arrangements.⁸⁷

2.84 The Report recommended that Commonwealth departments ensure that SPP agreements specify measurable performance indicators for each SPP program objective.⁸⁸ Departments generally supported the recommendation.⁸⁹

85 JCPA, *Report 342*, p.51.

86 JCPA, *Report 342*, p.36, p.38.

87 JCPA, *Report 342*, p.55.

88 JCPA, *Report 342*, p.56.

89 Department of Finance, *Finance Minute*, paras.117-130.

Management information systems

2.85 Report 342 considered that it was responsibility of the Commonwealth to ensure that the parties to SPP agreements provided compatible and comparable performance data to the greatest possible extent. It noted that, ideally, their use of common data collection systems would allow the easy transfer of data and minimise system costs.⁹⁰

2.86 The Report recommended that SPP agreements should outline the basic data collection requirements for each performance indicator. It also recommended that Commonwealth departments should ensure that SPP management information systems have design features that collect and collate compatible and comparable data, for use by the Commonwealth and the other parties to agreements.⁹¹ Departments generally accepted these recommendations.⁹²

Further developments

2.87 The Productivity Commission's 1996 stocktake of progress in microeconomic reform identified effective performance monitoring as a key action required for public sector reform. The Commission noted the need for improved data collection in several areas assisted under SPP programs, including public hospitals, schools, aged care services, child care services and local government services. It recommended that the review of Commonwealth-State service provision should continue to develop comprehensive performance indicators and that governments should improve the coverage and quality of outcomes data across service areas.⁹³

90 JCPA, *Report 342*, p.59.

91 JCPA, *Report 342*, p.60.

92 Department of Finance, *Finance Minute*, paras.131-157.

93 Productivity Commission, *Stocktake of Progress in Microeconomic Reform*, June 1996, p.6, p.15, pp.21-22, p.164, pp.166-170. The stocktake report was prepared as a joint exercise of three agencies, the Industry Commission, the Bureau of Industry Economics and the Economic Planning Advisory Commission, that had begun amalgamating on an administrative basis to prepare for the formation of the Productivity Commission. The new Commission formally came into being in April 1998.

2.88 The steering committee for the review of Commonwealth-State service provision produced three reports on government services since the JCPA inquiry. Through cooperation with many other parties, the steering committee has developed and applied a general framework for measuring performance, extended the collection of performance data to a wider range of government services and made improvements to the quality of data presented in successive reports. The 1998 report included performance information on the broad areas of education, health, housing and community services including aged care, disability services and children's services. The steering committee drew particular attention in its latest report to important information gaps that remain about the quality of health care and school learning outcomes.⁹⁴

2.89 The Committee considers that the steering committee's compilation and publication of cross-jurisdictional performance data on government services, including those assisted under SPP arrangements, continues to be valuable in promoting transparency in performance and accountability for the efficiency and effectiveness of services to the Australian community.

Financial accountability requirements

2.90 Parties receiving SPP funds generally are required to demonstrate that Commonwealth financial assistance has been expended on the intended purpose in accordance with the terms of SPP agreements.

2.91 Report 342 emphasised that the JCPA had not received any evidence of financial impropriety in the administration of SPPs or any evidence of systemic failures in the processes for accounting for SPP expenditure.⁹⁵

94 Steering Committee for the Review of Commonwealth-State Service Provision, *Report on Government Services*, Volumes 1 and 2, 1998, pp.iii-iv, xxii-xxiv, p.1, p.4.

95 JCPA, *Report 342*, p.74.

2.92 The Report noted that the joint ANAO-JCPA survey of SPPs identified various problems regarding the provision of statements and certifications of SPP expenditure.⁹⁶ Some SPPs did not require parties receiving SPP funds to provide statements or certifications of expenditure. Many SPPs did not stipulate the time limit for the provision of required certifications and there were widespread delays in their submission to the Commonwealth.⁹⁷ The Report also pointed out that various SPPs administered by a particular Commonwealth department had different submission deadlines.⁹⁸

2.93 The Report proposed that SPP financial accountability mechanisms be streamlined.⁹⁹ It recommended that Commonwealth departments administering SPPs undertake negotiations with other parties to adopt a single form of financial statement that, when audited, would satisfy the annual financial reporting requirements of parties receiving SPP funds as well as Commonwealth financial accountability requirements for the acquittal of SPP grants.¹⁰⁰ Departments generally supported the recommendations.¹⁰¹

Recent developments

2.94 The Committee notes that the streamlining of financial accountability requirements applies equally to Commonwealth Own Purpose Outlays and SPPs.

96 The survey of SPPs defined these terms as follows.

A statement of expenditure refers to a statement to the Commonwealth describing how funds have been spent on the SPP over a period.

A certification of expenditure refers to a requirement to provide evidence to the Commonwealth in an agreed form to certify that the funds it contributed were expended in a manner consistent with the agreement.

See ANAO, *Audit Report No.21 1994-95*, p.9.

97 ANAO, *Audit Report No.21 1994-95*, pp.9-12.

98 JCPA, *Report 342*, pp.75-77.

99 *Report 342*, p.79.

100 JCPA, *Report 342*, p.82.

101 Department of Finance, *Finance Minute*, paras.209-233.

2.95 The JCPA and the Queensland Public Accounts Committee (QPAC) conducted a joint inquiry into financial accountability requirements in relation to Aboriginal Councils and Torres Strait Island Councils during 1997. The inquiry noted differences between the financial accountability requirements and processes of the various Commonwealth and Queensland government agencies which issue grants to the Councils.¹⁰²

2.96 The JCPA and QPAC considered that for efficiency considerations there was merit in the agencies standardising grant application and acquittal forms and processes. The Committees recommended that the Commonwealth and Queensland government agencies which provide funds to the Councils work together to standardise their grant application and acquittal processes.¹⁰³ The Finance Minute response to JCPA Report 355 tabled in November 1997 has not yet been received.

Incentives and sanctions

2.97 Financial incentives can be specified in SPP agreements to encourage parties to achieve or surpass program performance targets, minimise program delivery costs or introduce additional desirable controls over program activities, such as quality assurance measures. Sanctions in SPP agreements can be used to impose financial penalties on parties where they fail to comply with important SPP program requirements, such as the provision of accountability information to the Commonwealth.¹⁰⁴

102 JCPA, *Report 355, Aboriginal Councils and Torres Strait Island Councils: Review of Financial Accountability Requirements*, November 1997, pp.1-3, pp.6-9, pp.14-15.

103 JCPA, *Report 355*, pp.15-16, pp.20-21, p.33.

104 ANAO, *Audit Report No.6 1993-94*, pp.9-10, p.16; JCPA, *Report 342*, pp.60-61.

2.98 Report 342 observed that the Commonwealth appeared to be reluctant to apply SPP sanctions because the available sanctions were often inappropriate to the circumstances or their application would threaten service delivery to the public. It also noted ANAO-JCPA survey results indicating that some SPP programs lacked sanction provisions.¹⁰⁵

2.99 The Report recommended that SPP agreements specify incentives for good program management and performance, detail graduated sanctions for non-compliance and outline consultative processes to identify the reasons for failure to achieve performance targets before any sanctions are considered.¹⁰⁶ Departments generally supported the recommendation.¹⁰⁷

Evaluations

2.100 Periodic program evaluations are an important means of reviewing the extent to which SPP programs have been effective in meeting their objectives and efficient in their use of funds and other resources. Evaluations also can help the Commonwealth and other parties to SPP agreements assess the continuing relevance of SPP programs and consider improved ways of delivering services to the community.¹⁰⁸

2.101 Report 342 noted the joint ANAO-JCPA survey finding that a requirement for program evaluation was not stipulated in many SPP agreements. The survey also reported that reviews of various kinds had been undertaken in relation to a large number of SPP programs.¹⁰⁹

105 ANAO, *Audit Report No.21 1994-95*, Figure 10, p.27, p.28; JCPA, *Report 342*, pp.62-63.

106 JCPA, *Report 342*, p.64.

107 Department of Finance, *Finance Minute*, paras.158-176.

108 JCPA, *Report 342*, p.64.

109 ANAO, *Audit Report No.21 1994-95*, p.24; JCPA, *Report 342*, p.65.

2.102 The Report recommended that SPP agreements specify Commonwealth evaluation of SPP programs at least every three to five years.¹¹⁰ Departments generally supported the recommendation.¹¹¹

Reporting to Parliament

2.103 The accountability of Commonwealth departments and other parties to SPP agreements for the use of SPP funds and the performance of SPP programs is enhanced by the ready access of the Parliament and the public to reliable and up to date information about SPP programs and their performance results.

2.104 Report 342 noted the findings of the joint ANAO-JCPA survey of SPPs that only a small number of SPPs required separate reports to be provided to Parliament, no time limits were specified for the tabling of some of these reports and there were long delays before reports were tabled. Commonwealth departments indicated that information on other SPPs was provided in departmental annual reports, portfolio budget statements, budget papers and other means.¹¹²

2.105 The Report proposed that Commonwealth departments include performance data on individual SPPs in the supplementary annual report papers available to the Parliament and the public on request. It recommended that annual report requirements for departments be amended to require them to prepare information for each SPP program, indicating the SPP objectives and associated performance indicators, performance towards objectives during the reporting period and the use of any sanctions for

110 JCPA, *Report 342*, p.65.

111 Department of Finance, *Finance Minute*, paras.177-198.

112 ANAO, *Audit Report No.21 1994-95*, p.14, Figure 4, p.15; JCPA, *Report 342*, pp.69-70.

non-compliance with the terms of SPP agreements.¹¹³ The Department of the Prime Minister and Cabinet responded that the recommendation would be considered in the context of the future revision of requirements for departmental annual reports.¹¹⁴

Compendium of SPP information

2.106 The Commonwealth periodically published basic information on all SPP programs in a catalogue of SPPs during the 1990s. The publications contained data on the objectives of each SPP, its authority, method of operation, funding allocations and commitments, conditions on expenditure, reporting requirements, sanctions for non-compliance and review arrangements.¹¹⁵

2.107 Report 342 noted that responsibility for the continuing publication of the catalogue had recently passed to the Department of Finance. The Report recommended that SPP information in the catalogue be expanded to include basic performance data.¹¹⁶ The Department of Finance responded that an alternative approach would be to include this information in departmental annual reports. It proposed that the issue be addressed in the context of the review of requirements for these annual reports planned to be undertaken in 1997.¹¹⁷

113 JCPA, *Report 342*, pp.71-72.

114 Department of Finance, *Finance Minute*, para.206.

115 JCPA, *Report 342*, p.72.

116 JCPA, *Report 342*, p.72.

117 Department of Finance, *Finance Minute*, paras.207-208. Initially, the Department appeared to endorse the JCPA recommendation. It stated in the introduction to the 1995-96 SPP catalogue that future editions of the catalogue would provide a summary of the performance information available for individual SPPs, consistent with the JCPA recommendation. See Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1995-96*, p.1.

Further developments

2.108 Since the JCPA inquiry into SPP administration, the Department of Finance produced two editions of the SPP catalogue, for 1995-96 and 1996-97. The Department decided in 1997 that future editions would be produced on a three yearly basis and would exclude the financial information currently included in the catalogue. It stated that this change reflected the improvements in the provision of financial information on SPPs in budget papers in recent years.¹¹⁸

Committee comment

2.109 The Committee doubts whether the presentation of comprehensive SPP performance data in departmental annual reports is a realistic alternative to the JCPA recommendation for its inclusion in the SPP catalogue. While more SPP performance information undoubtedly can be included in these reports, space limitations may well limit the extent of this coverage.

2.110 The Committee also has reservations about the actions proposed by the Department of Finance to reduce the frequency of publication of the SPP catalogue and to limit the range of information contained in future editions. The production of the catalogue on an annual basis has meant that information on SPP is relatively up to date. It is important to include SPP performance data as well as retain SPP financial information in future editions of the catalogue to enhance its standing as a ready reference publication offering comprehensive, consolidated information on SPP arrangements, funding and performance results.

118 Department of Finance and Administration briefing paper on terms and conditions governing the administration of general purpose and specific purpose payments, prepared for the Joint Committee of Public Accounts and Audit, 10 March 1998, pp.3-4. See also Department of Finance, *Estimates Memorandum 1997/33 - 1996-97 Final Budget Outcome Document: Data on Specific Purpose Payments and Other Commonwealth Payments*, July 1997, para.6.

Broadbanding of specific purpose payments

2.111 Relatively small grants are payable to some State government agencies and educational institutions under SPP arrangements.

2.112 Report 342 expressed concern that the administrative burden on these agencies can be unduly onerous and disproportionate to the size of individual grants.¹¹⁹ The JCPA identified the merging of smaller SPPs into larger SPPs as a solution to this problem. It mentioned that such arrangements are generally known as 'broadbanding'.¹²⁰

2.113 Report 342 proposed the broadbanding of many ongoing small SPPs with larger SPPs, particularly in the health, community services and education areas. It noted that the merging of some small SPPs in other portfolio areas would not be appropriate.¹²¹ The Report also canvassed the possibility of introducing sunset arrangements for new small SPPs. These SPPs would be allocated separate funding for a specified period and then funded under allied larger SPPs where there was a demonstrated need for their continuation.¹²²

2.114 The Report recommended that Commonwealth departments administering SPPs should investigate the possibility of broadbanding existing SPPs within their portfolios and give consideration to inserting sunset clauses in agreements for new SPPs, to provide for their possible broadbanding with allied SPPs after a pre-determined period.¹²³ Departments generally supported the recommendations. Some departments indicated that broadbanding was not appropriate to the particular SPPs under their administration.¹²⁴

119 JCPA, *Report 342*, p.89.

120 JCPA, *Report 342*, p.91.

121 JCPA, *Report 342*, p.94.

122 JCPA, *Report 342*, pp.94-95.

123 JCPA, *Report 342*, pp.95-96.

124 Department of Finance, *Finance Minute*, paras.260-284.

Further developments

2.115 There have been several recent initiatives to introduce broadbanding arrangements to SPP programs. Three smaller housing assistance SPPs were merged in 1996 into base funding for the main housing assistance SPP.¹²⁵ The SPP providing targeted assistance to schools has had a more flexible program structure since 1997. The new structure streamlines more than 40 small program elements into five priority areas.¹²⁶ The Commonwealth also has been exploring the possibility of broadbanding a number of public health programs funded under separate SPPs. Discussions regarding future funding arrangements for these programs commenced with the States in 1997.¹²⁷

2.116 The Committee supports these recent initiatives aimed at merging smaller SPPs and streamlining SPP program elements. The Committee recognises that SPPs administered by some Commonwealth departments are less suited to broadbanding arrangements.

Guidelines for SPPs

2.117 Commonwealth departments can promote consistency and good practice in the design and management of SPPs under their administration, by developing and applying suitable departmental guidelines that deal with important features and practices for SPPs. Such guidelines can be separate from, or be part of, broader guidelines that include Commonwealth grants to individuals and community agencies under Commonwealth Own Purpose Outlays.

125 Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, p.13, pp.118-119; Senate Community Affairs Reference Committee, *Report on Housing Assistance*, December 1997, p.17.

126 Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, pp.20-21; Department of Employment, Education, Training and Youth Affairs, *Annual Report 1996-97*, p.51.

127 Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, p.12, p.51; Department of Health and Family Services, *Annual Report 1996-97*, p.38; Portfolio Budget Statements 1996-97, *Health and Family Service Portfolio*, Budget Related Paper No.1.8, p.16.

2.118 Report 342 noted that a number of Commonwealth departments had guidelines for negotiation of grants¹²⁸ and the ANAO had produced a recent guide on the administration of grants.¹²⁹ The ANAO also had previously issued an audit commentary on Commonwealth-State agreements that identified good SPP practice.¹³⁰

2.119 The Report mentioned that a draft general protocol for SPPs had been prepared by the Commonwealth in 1995, but this proposal did not proceed further, due to unfavourable responses from the States.¹³¹ The JCPA expressed concern that a Commonwealth wide protocol for SPPs could become a reductive checklist, that would not take into account the diversity of issues addressed by SPPs.¹³²

2.120 The JCPA supported the development of departmental guidelines for SPPs. Accordingly, the Report recommended that Commonwealth departments administering SPPs should ensure that they have departmental guidelines applicable for the negotiation of SPPs, the drafting of SPP agreements and the development of best practice administrative arrangements. It also recommended that the Department of Finance should assess, compile and distribute examples of best practice SPP agreements and associated administrative arrangements to Commonwealth departments and other interested parties.¹³³

2.121 Departments supported the recommendation for departmental guidelines on SPP arrangements.¹³⁴ The Department of Finance agreed to the recommendation concerning the identification and dissemination of best practice examples. It indicated that it would consult with the ANAO and selected agencies in undertaking a pilot

128 JCPA, *Report 342*, footnote 18, p.98.

129 JCPA, *Report 342*, p.98. The guide was ANAO, *Best Practice Guide for the Administration of Grants*, 1994.

130 ANAO, *Audit Report No.6 1993-94, An Audit Commentary on Aspects of Commonwealth-State Agreements*, September 1993.

131 JCPA, *Report 342*, p.97.

132 JCPA, *Report 342*, p.97.

133 JCPA, *Report 342*, p.98.

134 Department of Finance, *Finance Minute*, paras.285-294.

assessment of good practice SPP agreements and then evaluate the feasibility and cost-effectiveness of an ongoing assessment, compilation and distribution of good practice.¹³⁵

2.122 The Committee notes that the ANAO issued a revised guide on the administration of grants in 1997. While the main focus of the guide is on the administration of grants to individuals and community organisations, the principles outlined in the guide are relevant to other types of grants including SPPs.¹³⁶

Conclusions

2.123 From its examination of SPP program administrative arrangements, the Committee reached a number of conclusions regarding SPP payments and conditions which may appropriately be attached to them.

2.124 The Commonwealth financially supports the provision of a range of important services to the Australian community through a large number of specific purpose payments to and through the States. SPP payments involve significant outlays (\$18.1 billion in 1997-98).

2.125 The Commonwealth usually attaches conditions to the use of SPP funds and requires other conditions to be met by the States or other parties to SPP arrangements. These conditions are generally set out in Commonwealth legislation, agreements concluded between the parties or other program documentation.

2.126 The JCPA previously conducted a very comprehensive inquiry into Commonwealth administration of SPPs in 1995 and identified a number of ideal features for SPP program management. The Committee is pleased to note that Commonwealth departments administering SPPs indicated through the Finance Minute process that they were generally supportive of these principles.

135 Department of Finance, *Finance Minute*, paras.295-296.

136 ANAO, *Better Practice Guide - Administration of Grants*, May 1997, p.iii.

2.127 The Committee noted that a range of improvements have been made to SPP administration generally and in several specific functional areas since the previous Committee inquiry. These include initiatives to specify SPP program objectives more clearly, improve SPP performance measurement and broadband some SPP activities.

2.128 Through the Finance Minute process, Commonwealth departments have advised of specific actions taken or proposed to give effect to particular JCPA recommendations. The Committee recognises that changes to SPP arrangements necessarily take time to implement and must be done in full consultation with the other parties. The Committee expects that the ANAO audit of SPP performance information, which is expected to be finalised by October 1998, will provide a clearer picture of the extent to which departments have addressed previously identified shortcomings in SPP program administration.

2.129 The Committee believes that the ideal SPP features set out in Report 342 remain relevant to contemporary SPP program design and management and that Commonwealth departments should continue to draw upon them in preparing specific conditions to be attached to individual SPPs under their administration.

2.130 In the light of more recent information and commentary on particular issues available to the Committee during its current inquiry, the Committee has expanded and amplified its previous list of principles for sound SPP program administration, which is presented in the following box.

For the efficient and effective management of SPP programs, it is important that:

- SPP arrangements are administered under agreements between the parties or legislation where appropriate;
- the roles of the parties to SPP arrangements and their responsibilities for particular program management activities are clearly defined and the communication and consultation arrangements to operate between the parties are adequately specified;
- there is appropriate recognition of the contribution of the Commonwealth and other parties to the provision of SPP-funded services;
- SPP program objectives are specified in terms of clear, achievable and measurable outcomes;
- requirements regarding the financial contributions of the parties to SPP arrangements (input controls) are phased out, except where they are essential to the design and management of individual SPP programs;
- input controls that continue to be used for individual SPP programs are clearly identified and defined;
- SPP payments are released no earlier than necessary to meet the identified immediate funding needs of the other parties to SPP arrangements;
- measurable performance indicators are linked to and specified for each SPP program objective and basic data collection requirements are identified for each performance indicator;
- SPP financial accountability requirements are as streamlined as possible;
- there are graduated sanctions for non-compliance with SPP program conditions and appropriate processes are in place for apparent instances of non-compliance to be examined with other relevant parties to SPP arrangements before sanctions are applied;

- SPP programs and associated administrative activities are subject to periodic evaluation and review;
- the Parliament and the public have ready access to reliable and up to date information about SPP programs and their performance results; and
- smaller SPP programs are broadbanded in portfolio areas as far as practicable.

3

GENERAL PURPOSE PAYMENTS

Introduction

3.1 This chapter describes general purpose payments, amplifies the Committee's approach to the examination of general purpose payments during the inquiry and discusses conditions which may appropriately be applied to general purpose payments.

3.2 Four general purpose payment conditions expressly set out in States Grants (General Purposes) legislation are addressed in the chapter:

- State compliance with national competition policy and related reforms;
- State fiscal contributions to the Commonwealth's deficit reduction program;
- State contributions to any unfunded higher education superannuation liabilities required to be discharged; and
- States payments for any Commonwealth grants to higher education institutions or student organisations as a consequence of State actions affecting the collection of student organisation fees.

3.3 The chapter concludes with a discussion of general GPP funding conditions relating to:

- the roles and responsibilities of parties to general purpose payments;
- the authority for general purpose payments;
- funding amounts;
- funds disbursement;
- fiscal reporting; and
- funding review.

General purpose payments

3.4 As noted in Chapter 1, General Purpose Payments (GPPs) are payments for general revenue assistance to the States. They are not directly related to particular government activities. The Commonwealth does not require the States to use the funds on specific areas of government activity. However, the Commonwealth may stipulate that the States meet other conditions for receipt of the funds.¹

Purpose of GPPs

3.5 The Commonwealth provides GPPs as general budget support to the States, to supplement their own-source revenues.² The provision of GPPs to the States reflects the significant difference between the respective revenue-raising capacities and expenditure responsibilities of the Commonwealth and the States, often referred to as 'vertical fiscal imbalance'.³

Outlays on GPPs

3.6 Commonwealth general revenue assistance to the States is expected to be \$16.8 billion in 1997-98. This is an increase of more than 3 per cent on the previous year.⁴ GPPs account for around 48 per cent of gross Commonwealth payments to the States.⁵

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- 1 Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, p.6; Budget Paper No.3, *Federal Financial Relations 1997-98*, p.23.
 - 2 Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, p.6; Budget Paper No.3, *Federal Financial Relations 1997-98*, p.13.
 - 3 Budget Paper No.3, *Federal Financial Relations 1997-98*, pp.13-15.
 - 4 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.4, p.23.
 - 5 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.39.

3.7 State fiscal contributions totalling \$627 million are required to be paid to the Commonwealth in 1997-98. This 'reverse' financial flow is discussed later in the chapter. The States may decide to pay their fiscal contributions by deduction from GPPs, by reduction in SPP payments subject to certain other conditions, or by direct payment to the Commonwealth.⁶

Types of GPPs

3.8 There are currently three types of GPPs: financial assistance grants, special revenue assistance and national competition payments. A fourth type, identified road grants, was absorbed into financial assistance grants for 1997-98.⁷

3.9 *Financial Assistance Grants (FAGs)* constitute base Commonwealth general revenue assistance to the States. FAG funding arrangements have been operating since 1985-86, when they replaced the previous tax-sharing grant arrangements.⁸

3.10 The Commonwealth currently maintains FAGs in real per capita terms, by making adjustments for price increases and population growth.⁹ The indexed per capita component of FAGs is conditional on the States complying with their obligations to implement national competition policy and related reforms.¹⁰

3.11 FAGs account for the bulk of GPP payments. FAGs to the States were estimated to be \$16.1 billion in 1997-98. The real terms adjustment and the per capita adjustment were expected to contribute \$125 million and \$198 million respectively to total FAG funding.¹¹

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- 6 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.4, p.33.
 - 7 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.23, p.26.
 - 8 Dennis James, *Commonwealth Assistance to the States since 1976*, Parliamentary Research Service Background Papers (Economics, Commerce and Industrial Relations Group) No.5, 1997/98, 20 October 1997, p.11.
 - 9 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.4, pp.23-24.
 - 10 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.4, p.23.
 - 11 Budget Paper No.3, *Federal Financial Relations 1997-98*, pp.23-24.

3.12 *Special revenue assistance (SRA)* is one-off Commonwealth general revenue assistance paid to particular States where they demonstrate a particular budgetary need or require special treatment from the Commonwealth.¹²

3.13 The Commonwealth currently provides special revenue assistance in the form of Medicare guarantee payments to New South Wales and Victoria, and payments to the Australian Capital Territory for self-government transitional allowances and special fiscal needs.¹³ SRA payments were expected to amount to \$471 million in 1997-98.¹⁴

3.14 *National competition payments (NCPs)* are Commonwealth general revenue assistance paid to the States conditional on their satisfactory progress with the implementation of national competition policy and related reforms.¹⁵

12 Dennis James, *Commonwealth Assistance to the States since 1976*, p.16.

13 Budget Paper No.3, *Federal Financial Relations 1997-98*, pp.4-5, p.23, pp.30-31.

The Medicare guarantee payments result from Commonwealth guarantees regarding financial benefits to the two States from changed Medicare arrangements introduced in July 1993. The Medicare guarantee payments terminate in 1997-98. See Budget Paper No.3, *Federal Financial Relations 1997-98*, p.31 and Budget Paper No.3, *Commonwealth Financial Relations with Other Levels of Government 1993-94*, pp.46-47.

The transitional allowances are designed to assist the transition of the Australian Capital Territory from the generous levels of Commonwealth funding which existed before self-government. The payments for special fiscal needs are made in recognition that the Commonwealth does not otherwise fund certain functions in the ACT. Similar functions in other States are the subject of funding arrangements between the Commonwealth and the States. See Budget Paper No.3, *Federal Financial Relations 1997-98*, p.30.

14 Medicare guarantee payments and ACT payments for transitional allowances and special fiscal needs amount to \$436 million and \$35 million respectively. See Budget Paper No.3, *Federal Financial Relations 1997-98*, pp.4-5, p.23, p.30.

15 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.4, p.23, p.29.

3.15 NCP conditions were specified in an agreement between the Commonwealth and the States concluded in April 1995. Under the agreement, the States are eligible to receive three tranches of NCPs, commencing at a level of \$200 million per year in July 1997 and increasing to \$400 million in July 1999 and \$600 million in July 2001 (in 1994-95 prices). NCPs are expected to total \$215 million in 1997-98.¹⁶

Revenue replacement payments

3.16 Revenue replacement payments (RRPs) are Commonwealth payments to the States separate from GPP financial assistance. RRP are designed to replace revenues that the States previously collected from State business franchise fees on tobacco and petroleum products and alcoholic beverages. Arrangements for RRP were announced in August 1997 following a High Court ruling that cast doubt on the constitutional validity of these franchise fees.¹⁷

3.17 Under RRP arrangements, the Commonwealth collects revenue from increased rates of Commonwealth customs and excise duty and wholesale sales tax applied to these products and returns the revenue to the States. RRP are regarded as State taxes imposed and collected by the Commonwealth on behalf of the States.¹⁸ RRP were estimated to amount to \$5.1 billion in 1997-98.¹⁹

Conditions attached to GPPs

3.18 GPP are usually described as 'untied' grants because the States may spend the general revenue assistance as they see fit. The States are not required to spend GPP on particular areas of government activity.²⁰

16 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.4, p.29.

17 Budget Paper No.3, *Federal Financial Relations 1998-99*, p.32.

18 Budget Paper No.3, *Federal Financial Relations 1998-99*, p.32.

19 Budget Paper No.3, *Federal Financial Relations 1998-99*, Table 15, p.33.

20 Department of Finance, *Catalogue of Specific Purpose Payments to the States and Territories 1996-97*, p.6; Budget Paper No.3, *Federal Financial Relations 1997-98*, p.23.

3.19 Although the States' expenditure of GPP payments is not subject to conditions, the States are currently required to meet four conditions for the receipt of GPP funds which are set out in Commonwealth States Grants (General Purposes) legislation. These conditions are briefly described here and discussed in more detail later in the chapter.

3.20 *National competition payments:* The Commonwealth makes GPP payments in the form of indexed per capita FAGs and NCPs conditional on the States' compliance with requirements relating to the implementation of national competition policy and related reforms.²¹

3.21 *State fiscal contributions:* GPP funding is provided on the condition that the States make fiscal contributions to the Commonwealth as a contribution to the Commonwealth's deficit reduction program.²²

3.22 *State contributions to costs of higher education superannuation:* GPP funding is conditional on the States paying their share of any unfunded higher education superannuation liabilities required to be discharged in their State.²³

3.23 *Higher education funding condition:* Where the Commonwealth makes grants to higher education institutions or student organisations as a consequence of State actions affecting the collection of student organisation fees, the States must pay the amount of those grants to the Commonwealth as a condition of GPP funding.²⁴

3.24 Commonwealth general revenue assistance to the States is also provided under a range of more general funding arrangements, specified in Commonwealth legislation or intergovernmental agreements, or observed as intergovernmental conventions and accepted administrative practice. These include arrangements for negotiation and consultation between the parties on GPP funding and related issues, assessment of GPP funding allocations to the States,

21 *States Grants (General Purposes) Act 1994*, section 12. See also Budget Paper No.3, *Federal Financial Relations 1997-98*, p.4.

22 *States Grants (General Purposes) Act 1994*, section 15A. See also Budget Paper No.3, *Federal Financial Relations 1997-98*, p.4, p.33.

23 *States Grants (General Purposes) Act 1994*, section 14.

24 *States Grants (General Purposes) Act 1994*, section 15.

disbursement of GPP payments and fiscal reporting by the parties.

Committee approach

3.25 The Committee decided to focus on two main areas of GPP conditionality:

- the four GPP payment conditions expressly set out in States Grants (General Purposes) legislation; and
- general GPP funding conditions.

3.26 The Committee reviewed reference to GPP funding arrangements in recent budget papers and relevant reports of other parliamentary committees, government agencies and official inquiries. Coverage of federal fiscal arrangements in academic publications as well as specialist public administration journals also was examined.

3.27 The Committee intends to keep in view developments related to GPP funding, particularly NCPs, and may conduct further inquiries in this area at some future date.

National competition payment conditionality

3.28 As part of the examination of the four legislated GPP payment conditions, this report examines the condition relating to the States' implementation of national competition policy and related reforms. There were several reasons for the Committee's attention to this payment condition.

3.29 Firstly, the Committee noted the significance of this reform agenda to the Australian community and the magnitude of future Commonwealth financial assistance linked to the States' progress in reform implementation. Secondly, the Committee was interested in the circumstances in which NCP funding arrangements were agreed between the Commonwealth and the States and the possible wider application of such conditional GPP funding in the future. Thirdly, the Committee was keen to see whether there were any lessons which might be drawn from the design and administration of conditions attached to NCPs.

3.30 The Committee addressed:

- the circumstances of Commonwealth funding of NCPs;
- the objectives of NCP funding;
- the consultative arrangements between the Commonwealth and the States, and with community stakeholder organisations, in respect of national competition policy reforms;
- the assessment principles and processes related to NCP funding; and
- the review arrangements for the national competition policy reform package and the NCC.

3.31 In its consideration of NCP payment conditions, the Committee took note of the report of the House of Representatives Standing Committee on Financial Institutions and Public Administration's inquiry into aspects of the national competition policy reform package, tabled in the Parliament in June 1997.²⁵ The JCPAA also noted the Government response to the report, presented to the Parliament in May 1998.²⁶

Other legislated GPP payment conditions

3.32 The Committee decided to examine the other legislated GPP payment conditions, that require the States to make fiscal contributions, higher education superannuation contributions and payments for any Commonwealth grants for student organisations as a consequence of State actions.

²⁵ The Committee reported on a number of general issues that arose during the course of the inquiry and addressed specific aspects of the national competition policy reform package as set out in the inquiry terms of reference. The Committee's conclusions and recommendations on the general issues are of particular relevance to the JCPAA's current inquiry. See House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition. Report of the Inquiry into Aspects of the National Competition Policy Reform Package*, June 1997, esp. p.vii, pp.61-68.

²⁶ Government Response to the House of Representatives Standing Committee on Financial Institutions and Public Administration Report, *Cultivating Competition*. See House of Representatives Hansard, 26 May 1998.

3.33 The Committee observed that the three conditions differ from NCP conditionality in several important respects. They involve State payments to the Commonwealth, whereas NCPs flow to the States. Both the fiscal contribution and the higher superannuation contribution are intended to assist the Commonwealth's financial position, whereas NCPs are part of a wider national policy reform agenda.

3.34 The Committee's examination of the three conditions requiring State payments to the Commonwealth focused on the circumstances surrounding the enactment of the conditions and whether such conditions might appropriately have wider application in the future.

General funding conditions

3.35 The Committee took the view that there would be value in exploring as part of this inquiry the extent to which the ideal features which the JCPA previously identified for SPP programs are relevant and appropriate to GPP funding arrangements. Given that GPPs and SPPs are two forms of Commonwealth financial assistance to the States, they could be expected to share, or would benefit from sharing, some common features. That said, the Committee recognised that GPPs and SPPs serve distinctive Commonwealth policy purposes and different conditions apply to the States' use of GPP and SPP funds.

Conditions attached to the use of GPP funds

3.36 The Committee believed that little useful purpose would be served by pursuing in this inquiry whether conditions might be appropriately attached to the States' use of GPP funds. The provision of general revenue assistance on an untied basis is a long-standing, integral feature of GPP funding arrangements and the Commonwealth has not indicated any intention to modify this practice. SPP arrangements already provide an effective means by which the Commonwealth can direct financial assistance to particular areas of government expenditure. Further, given that the States have their own-source revenues, the States would not necessarily be prevented from engaging in certain activities as a result of any Commonwealth restrictions on the use of GPP funds.

National competition payments

3.37 The Commonwealth Parliament in 1996 amended the *States Grants (General Purposes) Act 1994* to provide for national competition payments to the States in 1997-98.²⁷

3.38 The NCPs were part of a comprehensive national competition policy reform package concluded by the Commonwealth and the States. The package comprised the enactment of the Commonwealth *Competition Reform Act 1995* and State complementary legislation, together with three intergovernmental agreements: the Code of Conduct Agreement, the Competition Principles Agreement and the Agreement to Implement the National Competition Policy and Related Reforms (the Implementation Agreement).²⁸

3.39 The package covered a wide range of competition policy reforms, including prices oversight of government business enterprises, competitive neutrality principles for government businesses, structural reform of public monopolies, review of legislation that restricts competition and third party access to significant infrastructure facilities. The package also included related reforms to the electricity, gas, water and road transport industries.²⁹ These reforms have been recognised as one of the most important developments in microeconomic reform in Australia in recent years and are expected to result in far-reaching changes across the Australian economy.³⁰

27 *States Grants (General Purposes) Amendment Act 1996*, No.69 of 1996, section 12A.

28 The intergovernmental agreements dealt with processes for amending Commonwealth and State competition laws, principles for implementing the reforms and arrangements for three key competition policy agencies: the Australian Competition and Consumer Commission (ACCC), the National Competition Council (NCC) and the Australian Competition Tribunal.

See National Competition Council, *Annual Report 1996-97*, pp.50-52 and House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, p.2 and Table 1.2, p.4.

29 National Competition Council, *Annual Report 1996-97*, p.50; House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, p.2 and Table 1.2, p.4.

30 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, p.1

3.40 The Commonwealth undertook to provide NCPs to the States as part of the reform package, on condition that the States comply with obligations relating to the implementation of national competition policy and related reforms.³¹ These payments are expected to amount to \$16 billion over the period from 1997-98 to 2005-2006.³² A new agency, the National Competition Council, was vested with responsibility for assessing the States' progress on the reforms and advising the Commonwealth Treasurer of their eligibility for NCPs.³³

Introduction of NCP funding

3.41 The Committee observed that the introduction of NCP funding had several notable features.

Independent inquiry, government commitment and community support

3.42 The Commonwealth and the States operating through the Council of Australian Governments (COAG) endorsed the package of national competition policy and related reforms in April 1995. This followed extensive intergovernmental consultations and discussions on reform proposals over several years. The competition policy agreements committed the Commonwealth and State governments to implementing competition reforms broadly in line with the recommendations of an independent committee of inquiry (the Hilmer Committee), as well as related industry reforms previously agreed by the governments.³⁴

3.43 The Hilmer Committee had been established in October 1992. During the inquiry process it received many written submissions from and consulted widely with

and Productivity Commission, *Stocktake of Progress in Microeconomic Reform*, p.59.

31 National Competition Council, *Annual Report 1996-97*, p.52; House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, p.2 and Table 1.2, p.4.

32 National Competition Council, *Annual Report 1996-97*, p.52.

33 National Competition Council, *Annual Report 1996-97*, pp.51-52.

34 National Competition Council, *Compendium of National Competition Policy Agreements*, January 1997, pp.1-3.

government, industry and community organisations. It found strong and widespread support for implementing an effective national competition policy and significant awareness of its potential benefits. The Committee report, presented to the COAG heads of government in August 1993, contained comprehensive and detailed proposals for national competition policy reforms.³⁵

3.44 Drawing on the NCP example, the JCPAA considers that conditional GPP funding may be appropriate where the Commonwealth and the States have a shared commitment to the implementation of key national reforms that require Commonwealth and State cooperation. Ideally, the proposed reform measures would have been the subject of extensive public discussion, through official inquiries, stakeholder consultations, parliamentary scrutiny and debate, or other similar processes. Any intergovernmental reform proposals should be based on widespread recognition of the need for reform and acceptance and support for the proposed reform measures in the Australian community.

Demonstrable benefits to the community

3.45 The national competition policy and related reforms were expected to benefit ordinary Australians through price reductions, lower inflation, more growth and more jobs. The cumulative effect of the reforms on the national economy was estimated by the Industry Commission to be a long run annual gain in real GDP of \$23 billion and increased Commonwealth and State government revenues totalling \$8.9 billion. While there was considerable agreement that the reforms would be beneficial to the economy, there was some criticism of the modelling used to prepare these estimates and disagreement about the extent of the economic gains. No major analysis was undertaken of possible broader socio-economic costs of the reforms across the community.³⁶

35 F.G. Hilmer, *National Competition Policy. Report by the Independent Committee of Inquiry into National Competition Policy*, August 1993, transmittal letter and p.xx, p.xxxix.

36 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, pp.1-2 and Table 1.1, p.3. The Industry Commission analysis of the growth and revenue implications of the Hilmer and related reforms recognised limitations in its methodology and underlying assumptions. The Commission subsequently acknowledged that some criticisms of its modelling had substance. See Productivity

3.46 From the NCP example, the Committee considers that the magnitude and distribution of demonstrable economic and other benefits to the Australian community expected from reform measures should be a prime consideration in any future conditional GPP funding for reform implementation.

Recognition of the interests of the States and the Commonwealth

3.47 As noted earlier, the competition policy reform package provided the States with significant additional Commonwealth financial assistance. They also were afforded considerable flexibility in determining their own agendas and timetables for implementing the agreed reforms. These arrangements helped to ensure the States' cooperation with the reform initiatives. The States earlier had indicated some concerns that their revenue streams from government business enterprises might be adversely affected by the reforms and that the bulk of additional government revenues generated by the reforms would accrue to the Commonwealth.³⁷

3.48 The competition policy reform package stipulated that the Commonwealth would retain NCPs where the States were assessed as not having made satisfactory progress with reform implementation. The Commonwealth also could review NCP funding arrangements should Australia experience a major deterioration in its economic circumstances.³⁸

Commission, *Stocktake of Progress in Microeconomic Reform*, Box 3.2, p.61.

37 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, p.5; Brendan Bailey and Gavin Lee, *Competition Policy Reform Bill 1995*, Bills Digest Service, No.76/1995, 29 March 1995, p.5, p.8; Rolf Gerritsen, 'Some Progress Was Made: Intergovernmental Relations in the Second Keating Government 1993-1996', esp.pp.131-134, in Gwynneth Singleton (ed), *The Second Keating Government. Australian Commonwealth Administration 1993-96*, Centre for Research in Public Sector Management, University of Canberra, 1997.

38 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, pp.126-127.

3.49 In the Committee's view, the NCP example points to the importance of balancing the interests of the States and the Commonwealth in any conditional GPP funding in the future. The Committee considers that it may be appropriate to institute such arrangements where the States are reasonably entitled to financial compensation for the administrative costs associated with, or expected revenue losses from, implementation of agreed reforms. Given the sovereign power of the States, they should be free to pursue their own reform policies and actions, consistent with agreed overall reforms. It is also important that the States regard Commonwealth financial incentives for compliance or sanctions for non-compliance with reforms as fair and reasonable.

3.50 The Committee considers that future conditional GPP funding may be appropriate where it is reasonable for the Commonwealth to have assurance that the States have made satisfactory progress in implementing agreed reforms. It also seems reasonable that the Commonwealth makes any long-term GPP funding arrangements conditional on continuation of a positive national fiscal outlook.

NCP objectives

3.51 Where GPP funding is conditional on the States' compliance with the implementation of reform commitments, it is important that the reform objectives are clearly stated and expressed in terms of measurable outcomes.

3.52 The national competition policy implementation agreement listed one or more objectives for each discrete reform area, that had to be realised by the time the three tranches of NCPs were due to be paid.³⁹

3.53 The Committee observed that the NCC, which has the responsibility of assessing the States' progress in implementing the reforms, found it necessary to amplify, interpret and update first tranche reform commitments. While some reform commitments for the first tranche had precise deadlines for carrying out particular actions, other reform commitment objectives were stated in more general terms.

39 The implementation agreement is reproduced in the report of the House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, Appendix 6. For reference to the reform objectives for the first tranche NCPs, see pp.127-128 and pp.132-133.

Some original first tranche reform commitments also were explicitly or implicitly modified by the parties to the implementation agreement.⁴⁰

3.54 The NCC identified the broad statements of intent in the national competition policy agreements and the subsequent changes to reform timetables and agendas as two of the factors which contributed to the complexity and difficulty of the task of assessing whether the States had made satisfactory progress in implementing reform commitments for the first tranche payment.⁴¹

3.55 The Committee believes that some useful lessons can be drawn from the NCP example. Any future agreements for conditional GPP funding should aim to specify reform commitments as clearly and as comprehensively as possible. The Committee recognises that this is not always easy to achieve. Agreements also should contain express provisions for varying reform commitment agendas and timetables by formal agreement of the parties, in the light of subsequent developments that render original reform commitments inappropriate.

NCC consultative arrangements

3.56 Effective communication and consultation arrangements between the Commonwealth and the States, and between relevant government agencies and other interested parties underpin cooperative federal fiscal arrangements.

3.57 The Committee noted that there are protocols for formal consultation between the parties to the national competition policy reform package and that the NCC liaises and consults with various bodies and organisations interested in national competition policy reform issues. The conduct code agreement and the competition principles agreement contain

40 The report of the National Competition Council, *Assessment of State and Territory Progress with Implementing National Competition Policy and Related Reforms*, June 1997, pp.3-15, sets out the NCC's amplification and interpretation of first tranche reform commitments and describes subsequent developments affecting particular reform areas.

41 National Competition Council, *Annual Report 1996-97*, p.38.

specific provisions for the Commonwealth and the State to initiate consultations and convene meetings in relation to matters for discussion.⁴² At an operational level, the NCC and its secretariat staff periodically meet with representatives of State governments and State competition policy units.⁴³ Meetings are also held with local government and private sector representatives.⁴⁴

3.58 The House of Representatives Standing Committee on Financial Institutions and Public Administration in its report on some aspects of the national competition policy reform package referred to criticism from various organisations regarding the level of NCC consultation with industry, community and local government groups.⁴⁵ The Committee recommended that the NCC adopt a more open approach to its work and be more active in disseminating information about the activities of the Council and the national competition policy.⁴⁶

3.59 In its response to the Committee report, the Commonwealth Government agreed with the recommendation and stated that the NCC had begun to take a more pro-active role. It made specific mention of the NCC's publication of a monthly newsletter and maintenance of a website that provide information on developments in national competition policy reforms. The Government also drew attention to the NCC's publication of its assessment of the States' implementation of national competition policy reforms for the first tranche payments.⁴⁷ A further initiative mentioned by the NCC in its most recent annual report was the proposed conduct of a

42 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, p.107, p.122.

43 National Competition Council, *Annual Report 1996-97*, p.206.

44 National Competition Council, *Annual Report 1996-97*, p.216.

45 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, p.63.

46 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, p.63.

47 Government Response to the House of Representatives Standing Committee on Financial Institutions and Public Administration Report, *Cultivating Competition*, 26 May 1998, pp.12-13.

program of consultative meetings with key interest groups across Australia during 1997-98.⁴⁸

3.60 The Committee supports the recent efforts of the NCC to improve consultative arrangements with interested organisations in the community. The NCP example suggests to the Committee that, as part of any similar future arrangements for conditional GPP funding, early consideration should be given to instituting appropriate consultative processes with stakeholder groups in the community and establishing suitable means of providing the community with access to information, via the internet, newsletter or other media.

N C P assessments

3.61 GPP funding agreements and associated administrative arrangements ideally set out the principles and the processes to be observed in determining whether the States have complied with GPP funding conditions.

Assessment principles

3.62 The Committee noted that the national competition policy implementation agreement provided for the NCC to assess the States' compliance with conditions for NCPs. The agreement also stated that the Commonwealth would retain NCPs in the event of the States' non-compliance.⁴⁹ The agreement did not detail any further requirements regarding assessment principles or the assessment process.

3.63 The Committee noted that in the course of the assessment process for the first tranche payment, the NCC worked out operational principles for assessing the States' progress with reform obligations and for making recommendations on their eligibility for the NCPs. The NCC looked for substantial compliance with national competition policy reform obligations rather than complete

48 National Competition Council, *Annual Report 1996-97*, p.218.

49 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, p.127.

implementation of every particular reform commitment.⁵⁰ It also identified several possible types of non-compliance with reform obligations and developed possible options, other than not paying NCP instalments, to deal with particular types of non-compliance.⁵¹ The Council ultimately recommended that all States receive full payment of 1997 first tranche instalments, but that several matters should be examined further prior to the payment of the second instalment in 1998. The NCC recommendations were accepted by the Treasurer and NCPs were made in July 1997.⁵²

3.64 It seems to the Committee that the NCC adopted a reasonable, commonsense approach in exercising flexibility and discretion in its assessment of the States' compliance. Its approach was consistent with the cooperative framework for national competition policy reform implementation.

3.65 Drawing on the NCP funding example, the Committee believes that any future agreements for conditional GPP funding should state clearly what constitutes compliance with reform obligations. Parties to the agreement would thereby know at the outset whether total or substantial compliance with all or most of the reform objectives was required.

3.66 The Committee considers that any future agreements for conditional GPP funding should expressly provide for a range of graduated sanctions in the event of partial non-compliance with reform obligations. Possible sanctions might include part-payment or temporary suspension of payment.

50 National Competition Council, *Annual Report 1996-97*, p.40; National Competition Council, *Assessment of State and Territory Progress with Implementing National Competition Policy and Related Reforms*, pp.16-17.

51 National Competition Council, *Annual Report 1996-97*, p.40; National Competition Council, *Assessment of State and Territory Progress with Implementing National Competition Policy and Related Reforms*, pp.17-18.

52 National Competition Council, *Annual Report 1996-97*, p.40.

Assessment processes

3.67 The Committee noted that the NCC established a multi-step process for the assessment of the States' progress with national competition policy and related reforms. These steps included the NCC's preparation and circulation of preliminary and draft final assessments. The States had several opportunities to discuss and respond to NCC appraisals of their implementation actions, and their views were taken into account during this process.⁵³

3.68 The Committee considers that the NCC had a structured and transparent assessment process that provided natural justice to the parties affected by its recommendations.

3.69 The Committee believes that it is important that natural justice provisions are formally prescribed in assessment processes. To this end, any future conditional GPP funding agreements should contain provisions for the circulation of proposed assessments to the States and the finalisation of assessments taking into account their responses.

NCC reviews

3.70 Reviews and evaluations assist the efficient and effective management of government activities and promote accountability for program outcomes and the use of public moneys.

Program evaluation

3.71 Periodic program evaluation of the national competition policy reform package and the implementation of the national competition policy and related reforms can be beneficial in identifying areas where the reform framework needs revision or further reform implementation action is required.

53 National Competition Council, *Annual Report 1996-97*, pp.38-39.

3.72 The Committee notes that the conduct code agreement and the competition principles agreement forming part of the national competition policy reform package required the Commonwealth and the States to review the operation and terms of the agreements once they have operated for five years. The agreements were signed in April 1995.⁵⁴

3.73 The Productivity Commission in 1996 favoured an independent review of the outcomes achieved from key elements of the national competition policy reform framework. It noted that the NCC would play a major role in monitoring reform implementation. The Commission indicated that the NCC's limited ability to undertake work outside a work program agreed by the Commonwealth and the States might limit its effectiveness in the broader task of assessing the operation of the policy framework. The Commission proposed an independent review of the operation of key elements of the national competition policy framework and outcomes achieved commencing in 1998, ahead of the review of the NCC scheduled in 2000.⁵⁵

3.74 The Committee believes that it would be appropriate for the Commonwealth and the States to arrange for a review of the reform framework and reform implementation to be undertaken in 2000. By then, sufficient time will have elapsed for the progress of the national reform process to be reasonably assessed. These arrangements also would accord with the original agreements concluded by the parties.

3.75 The Committee sees merit in the Commonwealth and the State commissioning an external review, independent of the key competition policy institutions - the ACCC, the NCC and the Australian Competition Tribunal. This would provide a more detached and objective assessment of reform progress. The Committee is not inclined to suggest that the Productivity Commission conduct the inquiry. While the Commission is an independent research and advisory body on microeconomic reform, it is also an active and interested party to the reform process. The Commission has previously expressed general

54 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, pp.107-109, pp.123-124.

55 Productivity Commission, *Stocktake of Progress in Microeconomic Reform*, pp.65-66.

views on national reform implementation.⁵⁶ It also has made submissions to a number of NCC inquiries.⁵⁷ The Committee expects that the independent inquiry would draw on the expertise of the full range of bodies with an interest in the national competition policy and related reforms.

3.76 The Committee notes that program evaluation is applicable to NCPs, any similar future conditional GPP funding components, as well as SPPs. It is not suited to existing GPP funding components such as FAGs and SRA because these forms of Commonwealth financial assistance are not provided to achieve specific program outcomes.

Organisation review

3.77 Review of the performance of the NCC in assessing the States' compliance with the implementation of national competition policy reforms and discharging its other responsibilities could identify ways to improve its operational efficiency and effectiveness. The continuing need for the NCC to exist and perform specific functions also could be addressed through organisation review.

3.78 The Committee noted that, under the national competition policy reform package, the Commonwealth and the States are required to review the need for and operation of the NCC after it has been in existence for five years.⁵⁸ The NCC commenced operation in November 1995.⁵⁹

3.79 The report of the inquiry of the House of Representatives Standing Committee on Financial Institutions and Public Administration into aspects of the

56 Productivity Commission, *Stocktake of Progress in Microeconomic Reform*, pp.59-71.

57 One recent example was the Commission's submission to the NCC review of legislation governing the operations of Australia Post. This review was undertaken by the NCC as part of the Commonwealth Government's national competition policy review of legislation which restricts competition. See Industry Commission, *Industry Commission Submission to the National Competition Council Review of the Australian Postal Corporation Act 1989*, September 1997.

58 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, p.122.

59 National Competition Council, *Annual Report 1996-97*, p.37.

national competition policy reform package in June 1997 recommended that the review of the NCC be an independent review.⁶⁰ In its response to the report, the Commonwealth Government agreed in principle to the recommendation.⁶¹

3.80 The JCPAA supports the proposal for an independent review of the NCC, but believes that the timing of the review warrants careful consideration. The NCC is required to undertake further major assessments of the States' compliance with national competition policy and related reforms for third tranche payments prior to July 2001.⁶² The Committee believes that there may be benefit in the Commonwealth and the States bringing the review forward to the first half of 2000, four years after the Council commenced operations. This would enable any agreed changes to NCC operations resulting from the review to be in place well ahead of the assessment process scheduled for the third tranche of NCPs.

3.81 The Committee notes that benefits may also result from periodic organisation reviews of the various government authorities and departments with responsibilities for developing policy advice on Commonwealth financial assistance to the States, advising on GPP funding assessments and administering GPP payments. Such reviews may identify ways to improve the operational performance of these agencies.

Other legislated general purpose payment conditions

3.82 Commonwealth States Grants (General Purposes) legislation sets out three general purpose payment conditions other than the NCP payment condition. These conditions relate to: State fiscal contributions, State higher education

60 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, p.64.

61 Government Response to the House of Representatives Standing Committee on Financial Institutions and Public Administration Report, *Cultivating Competition*, 26 May 1998, p.13.

62 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, pp.127-128.

superannuation contributions and the higher education funding condition.

State fiscal contributions

3.83 The Commonwealth Parliament in 1996 and 1997 enacted legislation that required the States to make fiscal contributions to the Commonwealth as a condition of financial assistance grants for 1996-97 and 1997-98.⁶³

3.84 The States' fiscal contributions totalled \$619 million in 1996-97 and an estimated \$627 million in 1997-98. The States are expected to make fiscal contributions amounting to \$313 million in 1998-99.⁶⁴

3.85 The decision to introduce State fiscal contributions was taken at the 1996 Premiers' Conference. The new Commonwealth Government had advised the States of the Commonwealth's financial position and the Government's fiscal strategy of reducing the underlying Budget deficit of \$8 billion to achieve balance in 1997-98. The States agreed to contribute to the Commonwealth's deficit reduction program over three years, in recognition of the fiscal challenge facing the Government. It was also decided that the need for the States' fiscal contributions would be reviewed annually at future Premiers' Conferences, in light of the Commonwealth's fiscal position at that time.⁶⁵

3.86 Other important matters affecting the budgetary situation of the States were discussed at the 1996 Premiers' Conference. The Commonwealth agreed to maintain and extend until 1998-99 the real per capita financial assistance grants introduced at the 1995 COAG meeting of Commonwealth and State heads of government. This provided the States with maximum funding certainty through

63 *States Grants (General Purposes) Amendment Act 1996*, No.69 of 1996, section 15A and schedule 3 and *States Grants (General Purposes) Amendment Act 1997*, No.131 of 1997, section 15B and schedule 4.

64 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.4, p.33; Budget Paper No.3, *Federal Financial Relations 1998-99*, p.4, p.34.

65 Budget Paper No.3, *Federal Financial Relations 1996-97*, p.3, p.25; The Treasurer (Hon.Peter Costello), 'Premiers' Conference and Loan Council meeting', *Ministerial Document Service*, 12 June 1996, p.2848; The Treasurer (Hon.Peter Costello), 'Funding arrangements with the States', *Ministerial Document Service*, 17 June 1996, p.2908.

guaranteed base general revenue assistance for three years.⁶⁶ The Commonwealth modified its proposal that the real per capita guarantee be conditional on the removal of the States' wholesale sales tax exemption status. The Premiers' Conference agreed that the tax would apply to road vehicles provided wholly or partly for private use as part of government remuneration packages.⁶⁷

3.87 The Commonwealth provided the States with flexibility regarding the timing and method of payment of their fiscal contributions. It accepted their contributions in the form of direct State weekly payments, weekly deductions from GPP payments or reductions in SPP payments. Contributions were not required on the same weekly basis as general revenue assistance paid to the States.⁶⁸

3.88 Deferral of part of the fiscal contributions due in the second year of the contribution arrangements also was allowed. The 1997 Premiers' Conference decided to maintain the previously agreed fiscal contribution schedule other than for Tasmania and the Australian Capital Territory. In recognition of the difficult economic circumstances facing the two jurisdictions, payment of half of their scheduled fiscal contributions was deferred until 1998-99. This reduced the total fiscal contribution from the States in 1997-98.⁶⁹

3.89 The Committee considers that it is unlikely that the State fiscal contribution condition has wider application for future GPP funding. It was introduced in special circumstances and applies to GPP payments for three years only, from 1996-97 to 1998-99.

66 Budget Paper No.3, *Federal Financial Relations 1996-97*, p.3, p.25; The Treasurer (Hon.Peter Costello), 'Premiers' Conference and Loan Council meeting', *Ministerial Document Service*, 12 June 1996, p.2848.

67 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.3; The Treasurer (Hon.Peter Costello), 'Removal of sales tax exemption', *Ministerial Document Service*, 12 June 1996, p.2849; The Treasurer (Hon.Peter Costello), 'Premiers' Conference and Loan Council meeting', *Ministerial Document Service*, 12 June 1996, p.2848; The Treasurer (Hon.Peter Costello), 'Funding arrangements with the States', *Ministerial Document Service*, 17 June 1996, p.2909.

68 Budget Paper No.3, *Federal Financial Relations 1996-97*, p.25; Budget Paper No.3, *Federal Financial Relations 1997-98*, p.33.

69 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.4, p.33.

3.90 The Committee notes that it would be prudent for the Commonwealth to make any future medium to long-term financial assistance commitments to the States conditional on no significant deterioration of the national fiscal outlook. This was done in the intergovernmental implementation agreement for NCPs.

3.91 If exigent circumstances require the Commonwealth to vary previously agreed GPP funding arrangements some time in the future, the Committee believes that it would be incumbent on the Commonwealth to work out revised arrangements which accommodate the interests of the States as far as possible. The Committee noted the flexibility afforded the States in respect of fiscal contributions.

State higher education superannuation contributions

3.92 The Commonwealth Parliament in 1987 amended States Grants (General Revenue) legislation to require the States to share in the costs of unfunded superannuation liabilities required to be discharged in their State in the first half of 1988, as a condition of Commonwealth general revenue assistance.⁷⁰ Current States Grants (General Purposes) legislation contains similar provisions for State higher education superannuation contributions.⁷¹

3.93 State higher education superannuation payments to the Commonwealth were estimated to total \$51 million in 1997-98. Contributions were required in 1997-98 from all jurisdictions other than Queensland, the Northern Territory and the Australian Capital Territory.⁷²

3.94 The State higher education superannuation contributions were introduced to provide for the sharing of superannuation costs to reflect the respective responsibilities of the States and the Commonwealth which prevailed when the superannuation liabilities were incurred. The Commonwealth undertook to provide full funding for the

70 *States Grants (General Revenue) Amendment Act 1987*, No.95 of 1987, section 5.

71 *States Grants (General Purposes) Act 1994*, section 14.

72 Budget Paper No.3, *Federal Financial Relations 1997-98*, Table A1, p.51, Table A2, p.81.

discharge of superannuation liabilities in its grants to higher education institutions and to recover the States' shares.⁷³

3.95 The Committee does not envisage the wider application of arrangements similar to State higher education superannuation contributions. The superannuation contributions are a unique form of ongoing payment from the States to the Commonwealth. Given that superannuation liabilities are involved, these arrangements can be expected to continue into the next decade.⁷⁴

Higher education funding condition

3.96 The higher education funding condition refers to the granting of general revenue assistance to the States on the condition that the States reimburse the Commonwealth for any payments made by the Commonwealth to higher education institutions or student organisations as a result of State actions affecting the collection of student organisation fees.

3.97 The Commonwealth Parliament incorporated the higher education funding condition in States Grants (General Purposes) legislation in 1993 and 1994.⁷⁵ The higher

73 Changes in Commonwealth and State responsibilities for higher education result in a complex formula to work out the States' shares, set out in the *States Grants (General Purposes) Act 1994*.

The basis of the formula was outlined in debate in the House of Representatives on the States Grants (General Revenue) Amendment Bill 1987. The States and the Commonwealth share the cost of accrued liabilities relevant to the period prior to 1974 on the same basis as the Commonwealth matched State funds for higher education at that time. The Commonwealth bears the full cost of accrued liabilities between 1974 and 1981, and the States and the Commonwealth share the cost of accrued liabilities after 1981 on the basis of the Commonwealth meeting all costs up to a limit of 14 per cent of salaries of staff in superannuation schemes. See Minister for Employment Services and Youth Affairs and Minister Assisting the Treasurer, The Hon. A.C. Holding, House of Representatives *Hansard*, 15 September 1987 and Mrs E.E. Darling, House of Representatives *Hansard*, 20 October 1987.

74 Budget Paper No.3, *Federal Financial Relations 1997-98*, Table A1, p.51.

75 *States Grants (General Purposes) Act 1993*, No.92 of 1993, section 20 and *States Grants (General Purposes) Act 1994*, No.122 of 1994, section 15.

education funding condition was introduced after some States had taken various actions in relation to the imposition, collection and use of student organisation fees, to implement voluntary student unionism in higher education institutions.⁷⁶

3.98 The Commonwealth provided for the continued financial support of existing higher education student services by amending the *Higher Education Funding Act 1988* to allow payments directly to student organisations affected by such State actions. The higher education funding condition enabled the Commonwealth to recover any payments to student organisations from general revenue assistance paid to the States.⁷⁷

3.99 The Committee considers that there is a remote possibility that at some time in the future a State might initiate actions that prevent or hinder Commonwealth payments to third parties. Such circumstances could give rise to Commonwealth consideration of the imposition of further GPP funding conditions similar to the higher education funding condition. The Committee would hope that the parties could resolve matters in dispute without recourse to such conditionality.

Some broad conclusions on circumstances for conditional GPP funding

3.100 The Committee has drawn some broad conclusions on circumstances where conditional GPP funding might be appropriate in the future, based on the foregoing examination of the circumstances relating to Commonwealth funding of NCPs and the enactment of the three other legislated GPP conditions.

76 Assistant Treasurer, The Hon. G. Gear, House of Representatives *Hansard*, 25 August 1994 and Parliamentary Secretary to the Minister for the Environment, Sport and Territories and Parliamentary Secretary to the Minister for Employment, Education and Training, The Hon. W.E. Snowdon, House of Representatives *Hansard*, 21 September 1994.

77 Assistant Treasurer, The Hon. G. Gear, House of Representatives *Hansard*, 25 August 1994 and Parliamentary Secretary to the Minister for the Environment, Sport and Territories and Parliamentary Secretary to the Minister for Employment, Education and Training, The Hon. W.E. Snowdon, House of Representatives *Hansard*, 21 September 1994.

3.101 The Committee notes that the Commonwealth Government and the Parliament are the arbiters of the conditions which may appropriately be attached to GPP funding. Section 96 of the Constitution provides that the Parliament may grant financial assistance to any State on such terms and conditions as it sees fit.

3.102 The Committee underscores the importance of regular consultation and sustained cooperation between the Commonwealth and the States for effective intergovernmental relations. Accordingly, the Committee believes that it is proper for the Commonwealth and the States to consult, negotiate and where possible agree to any future conditional GPP funding arrangements, as was done in respect of NCPs.

3.103 The Committee considers that the appropriateness of attaching particular conditions to GPP funding can be reasonably determined on a case-by-case basis only. It is not possible to state categorically the circumstances where conditional GPP funding would be appropriate or otherwise in the future. The Committee expects that GPP payments would be made conditional in only a narrow range of circumstances, given that the primary purpose of Commonwealth general revenue assistance is to provide general budgetary support to the States. Such circumstances may include where there is shared Commonwealth and State commitment to regulatory reform, demonstrable economic and other national benefits from cooperative action, and agreed arrangements that protect and advance the particular interests of the Commonwealth and the States.

General conditions relating to GPPs

3.104 The Committee observed that GPP payments to the States are administered under a range of more general funding arrangements, other than the four legislated payment conditions discussed in the previous section of this chapter. These funding arrangements are specified in Commonwealth legislation, set out in intergovernmental agreements or applied as good management practice.

3.105 The Committee found that a number of the ideal features for SPP programs identified by the JCPA in Report 342 and restated in the previous chapter of this report are pertinent to GPP funding. These include conditions relating to the roles and responsibilities of the parties to GPPs, the authority for GPPs, mechanisms for determining funding

amounts, funds disbursement, fiscal reporting and arrangements for periodic review of GPPs.

Roles and responsibilities

3.106 GPP funding arrangements require effective institutional arrangements between the Commonwealth and the State governments, as well as within each sphere of government.

Commonwealth-State institutional arrangements

3.107 Established and accepted processes for consultation and negotiation between the Commonwealth and the States help the parties to reach agreed decisions regarding the provision of Commonwealth general revenue assistance to the States.

3.108 Commonwealth GPP funding and its associated conditions are considered and determined through the Premiers' Conference process. Since Federation, the Premiers' Conference has been at the apex of the machinery of intergovernmental relations in Australia.

3.109 The Premiers' Conference operates under arrangements voluntarily agreed between the Commonwealth and the States. The Prime Minister, State Premiers and Territory Chief Ministers, together with their Treasurers, usually attend the Conferences. Meetings are normally held annually.⁷⁸

3.110 The Premiers' Conference does not have an ongoing secretariat. The Commonwealth Treasury has had departmental responsibility for substantive issues coming before the Conferences and the Department of Prime Minister and Cabinet has coordinated meeting arrangements.⁷⁹

78 Department of Prime Minister and Cabinet, Commonwealth-State Relations Secretariat, *Commonwealth-State Ministerial Councils - A Compendium*, May 1994, p.10.

79 Department of Prime Minister and Cabinet, Commonwealth-State Relations Secretariat, *Commonwealth-State Ministerial Councils - A Compendium*, p.10.

3.111 The Commonwealth and the State Departments of Treasury have in place a range of consultative, joint working party and liaison arrangements in relation to GPP funding. Treasury heads meet regularly to discuss matters of mutual interest, including fiscal reporting issues and preparation for the annual Premiers' Conference.⁸⁰ Treasury officials work together to prepare the annual report on the national fiscal outlook for the Premiers' Conference.⁸¹ Commonwealth Treasury officials also liaise with their State counterparts in the course of formulating departmental advice for the Commonwealth Budget.⁸²

3.112 The Committee notes that the division of program management responsibilities between the Commonwealth and other parties, which is an important issue for SPP programs, does not apply to GPP funding arrangements.

Roles and responsibilities within Commonwealth administration

3.113 The respective roles and responsibilities of Commonwealth agencies advising on and managing GPP funding arrangements need to be adequately specified and delineated.

3.114 The Department of Treasury has responsibility for developing Commonwealth fiscal policies, including arrangements for the distribution of resources between the Commonwealth and the States, and for administering the provision of general revenue assistance to the States.⁸³

3.115 As noted elsewhere in this chapter, a range of other agencies, including the NCC, the Australian Bureau of Statistics and the Commonwealth Grants Commission, perform specific activities in relation to GPP funding.

80 Department of the Treasury, *Annual Report 1996-97*, p.46.

81 Department of the Treasury, *Annual Report 1996-97*, p.45; Department of the Treasury, *National Fiscal Outlook. Report to the 1998 Premiers' Conference*, 1998, p.1.

82 Department of the Treasury, *Annual Report 1996-97*, pp.43-44.

83 Department of the Treasury, *Annual Report 1996-97*, p.41.

3.116 The Committee notes that the report of the inquiry of the House of Representatives Standing Committee on Financial Institutions and Public Administration into certain aspects of the national competition policy reform package highlighted concerns about the dual roles of the NCC in advising the Commonwealth and the States on national competition policy and assessing their implementation of the national competition policy reforms. The House Standing Committee recommended that the dual roles of the NCC be evaluated to determine whether both roles were appropriate.⁸⁴

3.117 In its response to the Committee report, the Government disagreed with the recommendation. It acknowledged the tensions between the roles but pointed out the importance of utilising the specialised skills of the NCC. The Government also noted the requirement for the formal NCC work program to be approved by the Commonwealth and the States.⁸⁵

3.118 The JCPAA is inclined to accept the Government response. The Committee considers that the possible creation of another agency to discharge one of the existing roles of the NCC would add to Commonwealth administrative costs and also might result in overlap and duplication in the functions of the NCC and the other agency.

Authority for general purpose payments

3.119 Executive intergovernmental agreement on Commonwealth revenue assistance is crucial for effective cooperative relations between the Commonwealth and the States. The Commonwealth Parliament must authorise Commonwealth expenditure on GPP payments.

3.120 The Committee notes that current GPP funding arrangements have been put in place through several kinds of intergovernmental agreement. The Commonwealth and the

84 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, p.63.

85 Government Response to the House of Representatives Standing Committee on Financial Institutions and Public Administration Report, *Cultivating Competition*, p.12.

States customarily negotiate and reach decisions on ongoing GPP funding each year at the Premiers' Conference.⁸⁶

3.121 Some GPP funding components have been agreed through other executive intergovernmental processes. NCP funding principles were first established under the national competition policy implementation agreement, concluded between the Commonwealth and the States through COAG in April 1995.⁸⁷

3.122 The Committee notes that GPP funding has appropriate legislative authority. GPP payments, including the NCP component, are authorised by the Parliament through States Grants (General Purposes) legislation.⁸⁸

3.123 The broader question of the effectiveness of parliamentary scrutiny of executive intergovernmental agreements is noted by the Committee, but has not been pursued during this inquiry.

Funding amounts

3.124 The Commonwealth and the States have a vital interest in the overall level of annual general revenue assistance to the States and the distribution of GPP funds between the States.

3.125 Current GPP funding principles are intended to maintain the real value of general revenue assistance, allocate funds fairly to State populations and take account of the relative funding needs of individual States. Three technical measures are employed to give effect to these funding principles: the real terms adjustment factor, the per capita

86 See, for example, Budget Paper No.3, *Federal Financial Relations 1997-98*, pp.4-5 for reference to GPP and SPP funding decisions taken at the 1997 Premiers' Conference.

87 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, p.126.

88 GPP funding for grant years from 1994 to 1997 is set out in four schedules in the *States Grants (General Purposes) Act 1994*. Section 12 A of the Act authorises NCPs. Schedule 4 of the Act set out the formula for NCP amounts to be paid to the States in 1997-98.

adjustment factor and the per capita relativity factor (described below).

3.126 It is important that the principles for determining GPP funding allocations are adequately specified, the methodologies used are sound and the technical calculations and assessments prepared are accurate. The overall processes need to be transparent and accepted by the parties.

Real terms and per capita adjustments

3.127 The real terms adjustment factor and the per capita adjustment factor are intended to adjust the amount of financial assistance otherwise payable to the States, for the effects of inflation and changes in State populations.

3.128 The Commonwealth and the States agreed at the 1997 Premiers' Conference to maintain the level of financial assistance grants in real per capita terms for the period from 1997-98 until 1999-2000.⁸⁹ The NCP implementation agreement made in 1995 provided for ongoing real per capita adjustment of NCPs.⁹⁰ States Grants (General Purposes) legislation describes the technical index factors for making real terms and per capita adjustments.⁹¹

3.129 The official national statistical agency, the Australian Bureau of Statistics, prepares the annual index factors for the national population and price changes, as well as the State population series.⁹² These figures are published in the Commonwealth budget papers.⁹³

89 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.4.

90 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, p.127.

91 *States Grants (General Purposes) Act 1994*, section 4 defines key index factor terms. Section 6 refers to the index factor for capital city consumer price increases. Sections 7 and 8 refer to the index factor for population changes.

92 Budget Paper No.3, *Federal Financial Relations 1997-98*, pp.1-2.

93 Budget Paper No.3, *Federal Financial Relations 1997-98*, pp.1-2.

Per capita relativities

3.130 The per capita relativity factor is designed to give each State the capacity to provide the average standard of State public services. Horizontal fiscal equalisation (HFE) between the States is achieved by identifying influences beyond the control of individual States that affect their relative capacity to raise revenue or their relative expenditure on government services.⁹⁴

3.131 The Commonwealth and the States through the 1988 and 1990 Premiers' Conferences agreed to the current arrangements for five-yearly review of the methodology for assessing relativities and an annual update of relativities using latest available data.⁹⁵ These relativities are considered and adopted at the Premiers' Conference each year.⁹⁶ The relativities for particular grant years are incorporated in States Grants (General Purposes) legislation through legislative amendments.⁹⁷

3.132 An independent Commonwealth advisory body, the Commonwealth Grants Commission (CGC), carries out the assessment of the relativities of the States. It uses a complex methodology that has been developed in response to the requirements of the Commonwealth and the States for a comprehensive and rigorous approach to HFE.⁹⁸ The parties have provided positive feedback to the CGC on the quality of its technical analysis.⁹⁹

94 Budget Paper No.3, *Federal Financial Relations 1997-98*, pp.15-16; Commonwealth Grants Commission, *Annual Report 1996-97*, pp.7-8.

95 Commonwealth Grants Commission, *Annual Report 1996-97*, p.6; Budget Paper No.3, *Federal Financial Relations 1997-98*, p.17.

96 Commonwealth Grants Commission, *Annual Report 1996-97*, p.6.

97 Relativity factors for particular grant years from 1994 to 1997 are set out in the schedules in the *States Grants (General Purposes) Act 1994*.

98 Budget Paper No.3, *Federal Financial Relations 1997-98*, pp.16-17; Commonwealth Grants Commission, *Annual Report 1996-97*, p.1, p.6. For an outline of the CGC assessment methodology, see Commonwealth Grants Commission, *Annual Report 1996-97*, pp.7-11.

99 Commonwealth Grants Commission, *Annual Report 1996-97*, p.25.

3.133 The Commonwealth usually consults with the States regarding the terms of reference for the CGC annual updates. During the assessment process, the CGC circulates a discussion paper setting out its views on issues under consideration and the Commonwealth and the States normally make submissions on these issues and other related matters.¹⁰⁰ The CGC assessments on the States' relativities are formally reported to the Commonwealth Government. The annual update report and the accompanying working papers are then immediately made available to the States.¹⁰¹ The assessments, and their redistributive effect on GPP funding allocations (amounting to about \$1.5 billion in 1997-98), are summarised in the Commonwealth budget papers each year.¹⁰²

3.134 The Committee is satisfied that there are adequate arrangements in place for determining GPP funding allocations. The Commonwealth and the States have agreed to the arrangements and the index factors are set out in States Grants (General Purposes) legislation. The methodology for assessing the relative funding needs of the States is well-established, independently carried out and transparent to the parties and the wider community.

3.135 The Committee recognises that there are some differences of view about the principle of fiscal equalisation based on capacity and regarding specific features of the CGC assessment methodology, particularly the treatment of SPP payments in assessments and the time lag in the equalisation system. It has sometimes been contended that equalisation should be based on the performance of the States in improving their fiscal position rather than on their fiscal capacity.¹⁰³ It also has been suggested that the inclusion of most SPPs in the assessments tends to override the Commonwealth's intentions in directing higher SPP shares to particular States and that the use of revenue, expenditure and other data which is between two and seven years old in the assessments means

100 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.17; Commonwealth Grants Commission, *Annual Report 1996-97*, p.6, pp.12-13, p.25, p.72.

101 Commonwealth Grants Commission, *Annual Report 1996-97*, p.6, pp.72-73.

102 Budget Paper No.3, *Federal Financial Relations 1997-98*, pp.17-18.

103 Commonwealth Grants Commission, *Annual Report 1996-97*, p.7.

that the relativities are not up to date.¹⁰⁴ The Commission has set out its views on these issues in its annual reports.¹⁰⁵

3.136 The Committee decided not to pursue these issues further in its current inquiry. The Committee noted that the issues relating to fiscal equalisation principles and methodology have previously been examined or are currently under examination. A working party of Commonwealth and State heads of Treasuries established in 1992 reported on its examination of fiscal equalisation principles and methodology to the 1994 Premiers' Conference. The report noted that fiscal equalisation was justified on equity grounds, which was primarily addressed at the political level and determined by political consensus. The working party considered alternative ways of determining the distribution of GPP payments to the States but made no recommendations on alternative distributional arrangements, as there was an absence of consensus among the States as to their desirability.¹⁰⁶ The Committee also noted that CGC is now carrying out its five-yearly comprehensive review of the assessment methodology and a range of issues relating to the methodology are again under consideration.¹⁰⁷

Funds disbursement

3.137 Commonwealth scheduling of GPP payments to the States ideally minimises the requirement for Commonwealth short-term borrowing while meeting the cash flow needs of the States.

3.138 The Committee is not aware of any intergovernmental agreement stipulating the timing of GPP payments, other than NCP payments. The national competition policy implementation agreement required NCP

104 Commonwealth Grants Commission, *Annual Report 1996-97*, pp.10-11; Budget Paper No.3, *Federal Financial Relations 1997-98*, p.20.

105 Commonwealth Grants Commission, *Annual Report 1996-97*, p.7, pp.10-11.

106 Commonwealth Grants Commission, *Annual Report 1996-97*, p.11; Budget Paper No.3, *Commonwealth Federal Financial Relations with Other Levels of Government 1994-95*, pp.22-23.

107 Budget Paper No.3, *Federal Financial Relations 1998-99*, p.17.

payments to be made on a quarterly basis.¹⁰⁸ States Grants (General Purposes) legislation provides for the payment of general revenue assistance at such times as the Commonwealth Treasurer determines. The Treasurer also may make advance payments to the States.¹⁰⁹

3.139 The Committee considers that there appear to be satisfactory arrangements in place for the disbursement of GPP payments. The Department of the Treasury makes payments of general revenue assistance in equal weekly amounts as far as practicable. Treasury has stated that it received no adverse feedback from the States on its administration of these arrangements during 1996-97.¹¹⁰

Fiscal reporting

3.140 Up to date, comparable information on the fiscal position of the Commonwealth and the States assists the Commonwealth to develop appropriate fiscal policies, including the provision of financial assistance to the States.

3.141 The Committee noted that the Commonwealth and the States have made several agreements relating to fiscal reporting. An agreement concluded at the 1991 Premiers' Conference provides the basis of current arrangements for the uniform presentation of financial information. A revised fiscal reporting framework was agreed at the Australian Loan Council in March 1997 and will come into effect in 1998-99.¹¹¹

3.142 Under the revised framework the Commonwealth and the States will continue to report core financial information in their budget papers. Reporting will be enhanced by requiring governments to present three-year forward estimates for the general government sector in budget reports, as well as to provide updated financial information in a mid-year report. The Commonwealth regards the new

108 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, p.127.

109 *States Grants (General Purposes) Act 1994*, sections 16 and 18 refer to advance payments and the timing of payments of general revenue assistance to the States.

110 Department of the Treasury, *Annual Report 1996-97*, p.46.

111 Budget Paper No.1, *Budget Strategy and Outlook 1997-1998*, p.7-5; Budget Paper No.3, *Federal Financial Relations 1998-99*, p.44.

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framework as a significant improvement on existing reporting arrangements.¹¹²

3.143 The Committee supports the recent cooperative efforts of the Commonwealth and the States in reviewing existing fiscal reporting practices and developing more comprehensive and frequent reports.

3.144 The Committee notes that the States are not currently required to provide information on their fiscal position as a condition of GPP funding. There is nothing to suggest that any State might cease to participate in agreed reporting arrangements in future. In the unlikely event that a State took such action, the Committee believes that it would be reasonable for the Commonwealth to consider making GPP funding conditional on the States' presentation of up to date financial information in a specified format.

Future developments

3.145 Accrual accounting, whole of government reporting and accrual budgeting are important ways of enhancing public scrutiny of public finances and improving fiscal policy development. The JCPA has strongly argued the case for their adoption in a number of previous reports.¹¹³

3.146 The Committee observed that the Commonwealth has decided to implement an integrated accrual budgeting and reporting framework from 1999-2000.¹¹⁴ The Committee has previously noted that the States were moving in a similar direction and proposed that the Commonwealth take the lead in this area.¹¹⁵

112 Budget Paper No.1, *Budget Strategy and Outlook 1997-1998*, p.7-5; Department of the Treasury, *Annual Report 1996-97*, pp.45-46.

113 JCPA, *Report 338, Accrual Accounting-A Cultural Change*, August 1995 examined accrual accounting and reporting for the Commonwealth.

JCPA, *Report 341, Financial Reporting for the Commonwealth: Towards Greater Transparency and Accountability*, November 1995 examined whole of government reporting and fiscal responsibility legislation for the Commonwealth.

114 Budget Paper No.3, *Federal Financial Relations 1998-99*, p.44; Department of the Treasury, *Annual Report 1996-97*, p.45.

115 JCPA, *Report 341*, p.122, p.141, pp.153-158.

3.147 The Committee believes that the Commonwealth should continue to work with the States to encourage further fiscal reporting reforms. The Committee intends to monitor future developments in federal fiscal reporting arrangements.

Funding review

3.148 Periodic reviews of GPP funding arrangements are useful in assessing the appropriateness of the various types of general revenue assistance and the funding principles for these GPP components, as well as the soundness of methodologies used to calculate funding amounts.

3.149 The Committee noted that current GPP funding components have agreed funding for specified periods ranging from one to nine years.

3.150 The real per capita indexation arrangement for FAGs was introduced in April 1995 for the forthcoming year and the following two years.¹¹⁶ The three year rolling guarantee has since been extended at successive Premiers' Conferences each year and now applies until 2000-2001.¹¹⁷ The methodology that the CGC uses to determine the relative funding needs of the States for FAGs is reviewed every five years. The last review was completed in 1993 and the current one will be reported in 1999.¹¹⁸

3.151 Special revenue assistance in the form of Medicare guarantee payments to New South Wales and Victoria was agreed for the five year period of the Medicare agreements, from 1993-94 until 1997-98.¹¹⁹ Payments for transitional allowances and special fiscal needs for the Australian Capital Territory have been determined on an annual basis.¹²⁰

116 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.24.

117 Budget Paper No.3, *Federal Financial Relations 1998-99*, p.25.

118 Commonwealth Grants Commission, *Annual Report 1996-97*, p.6.

119 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.31.

120 Budget Paper No.3, *Federal Financial Relations 1997-98*, p.30.

3.152 NCPs are payable over a nine year period from 1997-98 until 2005-2006. The series of payments is split into three tranches that run for two to five years. Compliance with payment conditions is assessed prior to the commencement of each tranche.¹²¹

3.153 The Committee regards these arrangements as acceptable. Commonwealth commitment to GPP funding beyond the forthcoming year assists the States in their medium-term fiscal planning. In the case of NCPs, the implementation of agreed national competition policy reforms is necessarily extended over a longer time-frame.

Conclusions

3.154 From its examination of GPP payments to the States, the Committee reached a number of conclusions.

3.155 The Commonwealth provides substantial general budget support to the States, through Commonwealth general revenue assistance (\$16.8 billion in 1997-98). GPPs differ from SPPs in that the States may spend general revenue assistance on any area of government activity.

3.156 The States are currently required to meet four payment conditions for receipt of GPP funds. These conditions are set out in States Grants (General Purposes) legislation.

3.157 The most significant of the four conditions requires the States to comply with obligations relating to the implementation of national competition policy and related industry reforms. The Commonwealth will make payments totalling some \$16 billion over nine years to the States if they make satisfactory progress in implementing the reforms. Reform implementation will result in major changes to the Australian economy.

3.158 The other GPP payment conditions require the States to make payments to the Commonwealth in the form of fiscal contributions, higher education superannuation contributions or payments for any Commonwealth grants to

121 House of Representatives Standing Committee on Financial Institutions and Public Administration, *Cultivating Competition*, pp.127-128, p.131.

higher education student organisations as a consequence of State actions preventing or hindering the collection of student organisation fees. Each of these conditions was enacted to deal with special circumstances and is not likely to have more general application to GPP funding in the future.

3.159 Constitutionally, the Commonwealth may grant financial assistance to the States on such terms and conditions as the Parliament sees fit. In practical terms, Australia's federal system of government works best when the Commonwealth and the States act cooperatively. The primary purpose of Commonwealth general revenue assistance has been to supplement the States' own-source revenues, not to pursue particular Commonwealth policy objectives.

3.160 The recent example of national competition payments indicates that conditional GPP funding can advance broader agreed reform agendas under particular circumstances. This suggests to the Committee that there is potential for greater conditional GPP funding in the future, particularly where there is shared Commonwealth and State commitment to regulatory reforms, there are demonstrable economic or other benefits to the Australian people and the national economy, and agreed funding conditions satisfactorily address the particular interests and concerns of the Commonwealth and the States.

3.161 There is little to be gained from attempting to prescribe a definitive list of specific conditions which might be appropriately applied to hypothetical future conditional GPP funding arrangements. Those conditions would need to be determined for each case. Experience to date with the administration of NCP funding, however, suggests that the features set out in the following box are important.

Where future GPP funding is conditional on the States' compliance with the implementation of agreed reforms, it is important that:

- the reform objectives are clearly stated and expressed in terms of measurable outcomes;
- there are effective consultative arrangements between the Commonwealth and the States and with other interested parties;
- the principles and processes for assessing the States' compliance with funding conditions are adequately specified; and
- reform implementation and funding assessment processes are subject to periodic independent review.

3.162 Commonwealth general revenue assistance is provided under a range of more general funding arrangements, specified in legislation and intergovernmental agreements or otherwise observed as good management practice. Many of the ideal features which the JCPA previously identified for SPP programs are relevant and appropriate to GPP funding arrangements. The Committee's examination of GPP payments to the States highlighted the importance of the ideal features presented in the box opposite.

For the efficient and effective management of GPP funding, it is essential that:

- the processes for consultation, negotiation and decision-making between the Commonwealth and the States are adequately defined and accepted, and the roles and responsibilities of Commonwealth agencies advising on and managing GPP funding arrangements are clearly specified;
- GPP payments have appropriate executive inter-governmental agreement and legislative authority;
- principles for determining funding allocations are adequately specified and competently applied, and assessment processes are transparent and accepted by the parties;
- GPP payment disbursement arrangements are in line with sound cash management principles;
- up to date, comparable information on the fiscal position of the States is available to the Commonwealth; and
- the continuing appropriateness of the various types of GPP payments and associated principles for determining fund allocations are reviewed at predetermined time intervals.

4

CONDITIONS RELATING TO THE ROLE OF STATE AUDITORS- GENERAL

Introduction

4.1 This chapter begins with a brief description of the roles of Commonwealth and State Auditors-General and then presents the Committee's views on attaching conditions relating to the role of State Auditors-General, drawing on previous relevant JCPA inquiries.

4.2 The chapter highlights problems encountered by State Auditors-General when financial certification responsibilities have been imposed on them as part of SPP accountability requirements. It also addresses possible ways of improving accountability for SPP performance through, for example, the conduct of coordinated Commonwealth and State Auditors-General performance audits of SPP programs.

Roles of the Commonwealth and State Auditors-General

4.3 A fundamental characteristic of general purpose and specific purpose payments is that once the funds pass *to* or *through* the States they cease, as a matter of law, to be Commonwealth funds.¹

4.4 The Commonwealth Auditor-General has a mandate to provide an independent assurance and evaluation of the economy, efficiency and effectiveness of administration of Commonwealth public sector entities. The mandate extends to allowing the Auditor-General to conduct reviews of the

1 JCPA, *Report 342, The Administration of Specific Purpose Payments: A Focus on Outcomes*, November 1995, p.66.

performance of the *Commonwealth component* of SPP administration, identifying best practices and recommending ways of improving the economy, efficiency and effectiveness of SPP administration.

4.5 Given that the Auditor-General's mandate is generally limited to reviewing the activities of Commonwealth agencies,² the Auditor-General cannot therefore conduct performance audits of the activities of other levels of government or non-government agencies involved in SPP administration.³

4.6 Hence the Commonwealth Auditor-General's role is concerned with the relevant Commonwealth agencies' disbursement of funds in accordance with arrangements agreed with the States and with relevant parliamentary appropriations. The Commonwealth Auditor-General has no effective jurisdiction after the Commonwealth has made a grant to State governments.

4.7 State Auditors-General, on the other hand, are responsible for auditing the operations of State agencies administering State government activities, including programs receiving Commonwealth financial assistance through SPP arrangements. The roles and duties of State Auditors-General are set down in the respective audit acts of the States and Territories.

4.8 Thus the roles of the Commonwealth and the State Auditors-General in the scrutiny of government payments reflect their respective mandates. The Commonwealth and State Auditors-General are not subject to control or direction by the Commonwealth government in the discharge of their statutory responsibilities.

2 In particular circumstances the Auditor-General may undertake audits of other agencies by arrangement. The powers of the Auditor-General under new audit legislation to enter into arrangements with other agencies to carry out such audit work are discussed in para.4.31 of this report.

3 JCPA, *Report 342*, p.66.

Committee approach

4.9 The Committee has considered the issue of attaching conditions relating to the role of State Auditors-General in several previous inquiries.

4.10 In 1988-89, the JCPA conducted a major review of the Australian Audit Office which culminated in Report 296, *The Auditor-General: Ally of the People and Parliament, Reform of the Australian Audit Office*. The Committee took substantial and comprehensive evidence on the issue of attaching conditions relating to the role of State Auditors-General and made a number of recommendations.

4.11 The Committee again considered this issue in 1994-95 in Report 342, *The Administration of Specific Purpose Payments: A Focus on Outcomes*. The JCPA recommended that State Auditors-General be consulted regarding financial accountability arrangements during the SPP negotiation process. The JCPA also recommended that the possibility of coordinated SPP performance audits with State Auditors-General be investigated.

4.12 The Committee considers that its previous views on desirable arrangements regarding the role of State Auditors-General in SPP financial and performance accountability arrangements, set out in Reports 296 and 342, continue to be relevant. The Committee's views on these issues are restated and amplified in light of more recent developments in the following sections of this chapter.

Imposition of responsibilities on State Auditors-General

4.13 The JCPA addressed the issue of the imposition of responsibilities on State Auditors-General in relation to SPP programs in Report 296. The Committee found that:

Commonly, what occurs is that the Commonwealth Government department or agency, as part of its program design, inserts a clause in an agreement with State government agencies, requiring the State Auditor-General to audit the use of Commonwealth finance by that State

government agency, or by local government or community organisations within the State.⁴

4.14 The JCPA found that this practice of attaching conditions relating to the role of State Auditors-General created a number of significant problems, for example:

- an increase in the workload of State Auditors-General;
- duplication of audit by Commonwealth and State Auditors-General;
- State Auditors-General uncertainty over whether their audit certificates should be provided to the Commonwealth Government department funding the program or to the Commonwealth Auditor-General;
- State Auditors-General being requested to provide audit certificates outside their normal area of competence or jurisdiction. For instance, the Victorian Auditor-General made the point that he was asked to provide certificates on the effectiveness of grants for rural financing including whether or not particular properties were commercially viable. State Auditors-General were also at various times asked to audit the accounts of community organisations and lobby and interest groups, which is a task they would not normally undertake;
- Commonwealth requests for more detailed information from State Auditors-General than the latter were accustomed to provide. An example was given by the South Australian Auditor-General who stated that, for a Commonwealth language program for children in a disadvantaged area, the Commonwealth required certification that its grant was spent by teachers in the classroom providing instruction to the particular disadvantaged students eligible for special assistance. Under normal circumstances, the State Auditor-General's

⁴ JCPA, *Report 296, The Auditor-General: Ally of the People and Parliament, Reform of the Australian Audit Office*, March 1989, p.121.

responsibilities would have required him to certify only that the education authority received and applied the Commonwealth grant. Another instance was of how the New South Wales Auditor-General was expected to provide the Commonwealth Government with certificates for the salaries of Vice-Chancellors;

- lack of uniformity in Federal audit requirements;
- the pressure exerted on State accounting systems by requests from Commonwealth departments for more detailed information than they could provide;
- interruptions to the planned schedule of work of State audit departments through unexpected and unforeseeable Commonwealth demands for audit certificates; and
- inadequate attempts by Commonwealth agencies to communicate the objectives of programs they funded through the States. Thus, State Auditors-General were often not sufficiently informed about the programs and expenditures they were auditing.⁵

4.15 The JCPA concluded in Report 296 that:

The reality is that audits of section 96 grants to the States are impossible without the co-operation of State Auditors-General. For too long it appears that some Commonwealth agencies have taken the cooperation of State Auditors-General for granted ... it also appears that State government agencies in receipt of Commonwealth funds have not always been conscious of the implications for their Auditors-General of agreements they sign. This is a matter to which the Committee would like to draw attention but which is beyond its jurisdiction in terms of recommendations.⁶

4.16 The JCPA's inquiry into the administration of SPPs in 1994-95 found that many of the problems concerning obligations on State Auditors-General in relation to SPP financial accountability requirements persisted.

⁵ JCPA, *Report 296*, pp.123-124.

⁶ JCPA, *Report 296*, p.126.

4.17 The results of the ANAO-JCPA survey of SPP administration indicated that, in 1994, State Auditors-General were required to provide certification for a number of SPPs. The survey also reported that they were not consulted about providing certifications for some of these SPPs.

4.18 The Committee found that State Auditors-General were concerned that they had not been consulted before they were obliged to provide the certifications. This was despite a Finance Direction which stated that Commonwealth departments must not attempt to impose tasks on State Auditors-General for the audit or acquittal of program expenditures, unless the State Auditors-General have first agreed to accept the task.⁷

4.19 In Report 342 the JCPA expressed concern that the Finance Direction was not being applied by some Commonwealth departments and endorsed the Auditor-General's recommendation that departments respect the statutory independence of State Auditors-General.

Recent developments

4.20 The Committee notes that since the previous JCPA inquiry, guidance on the attachment of conditions concerning State Auditors-General continued to be provided to Commonwealth agencies by the Department of Finance and Administration (DoFA) through (the now superseded) Finance Direction 13F,⁸ which stated:

7 JCPA, *Report 342*, pp.82-83.

8 Finance Direction 13F was issued under the *Audit Act 1901* which was repealed as from 1 January 1998. The *Financial Management and Accounting Act 1997* (FMA Act) now provides for the proper use and management of public money, public property and other Commonwealth resources. Finance Minister's Orders have replaced Finance Directions.

Under the FMA Act, section 52 and FMA Regulation No.6, Chief Executive Officers are permitted to give instructions to officials in their agencies for carrying out the new FMA legislation. The Committee is not aware as to whether agency instructions refer to the audit and acquittal of payments made to or through State government agencies. An acceptable alternative could be to refer to this matter in agency guidelines on SPP arrangements, proposed by the JCPA in Report 342. See para.2.120 of this report.

AUDIT/ACQUITTAL OF PAYMENTS MADE TO OR THROUGH STATE GOVERNMENT AGENCIES

The Commonwealth has no right to direct that a State Auditor-General become involved in providing audit certificates or performing other tasks to satisfy the Commonwealth's need for acquittal of moneys paid to or through State Government agencies for the purposes of implementing Commonwealth programs. State Auditors-General are creatures of their own State Parliaments and to that extent, they are functionally independent of governments. It is generally inappropriate, therefore, for the Commonwealth or State Governments to compromise the statutory independence of State Auditors-General by attempting to direct them in such a way. If a Department considers that special reasons exist that might warrant a State Auditor-General's involvement in the acquittal of a particular Commonwealth program that is to be made subject to Commonwealth legislation or agreements executed with the States, the Department should ensure first that the State Governments have obtained the prior agreement of their respective Auditors-General to that involvement.

4.21 The Committee reiterates its support for the principles embodied in the Finance Direction.

4.22 The Committee awaits the results of the ANAO's current survey of SPPs, to see whether Commonwealth departments have addressed previous JCPA concerns regarding the imposition of audit and acquittal tasks on State Auditors-General. As noted earlier in this report the ANAO survey, expected to be reported in October 1998, will provide a longitudinal analysis of progress in SPP administration since the joint ANAO-JCPA survey undertaken in 1994-95.

Coordinated performance audits

4.23 The JCPA's inquiry into SPP administration in 1994-95 found that a number of constraints stood in the way of conducting joint audits between the Commonwealth and State Auditors-General, including:

- the varying mandates of the States to conduct performance evaluations of SPP activity taking place within States; and

- legal constraints which prohibit actions beyond those specified in the statute.

4.24 The JCPA observed that:

State Auditors-General have varying mandates to conduct performance evaluations of SPP activity taking place within their own States. For example, while the Commonwealth Auditor-General can review programs for their economy, efficiency and effectiveness, the South Australian Auditor-General can only review South Australian programs for their economy and efficiency, but not their effectiveness. The Queensland Auditor-General can review the systems that a Queensland public sector entity has in place to measure its own performance, but not the entity's actual performance. The Western Australian Auditor-General, however, has a similar performance audit mandate to the Commonwealth Auditor-General, but is also required to audit the performance indicators that all Western Australian public sector agencies are required to use.⁹

4.25 The Committee believed that the ultimate goal should be the implementation of uniform audit legislation in all Australian jurisdictions. The Committee considered that a less ambitious, but more achievable, goal would be the harmonisation of audit legislation to allow Auditors-General to conduct joint performance audits of SPPs.

4.26 The Committee recognised, however, that the practical difficulties associated with amending all audit acts suggests that neither of these objectives is likely to be realised without a coordinated approach by State governments.

4.27 The JCPA therefore recommended in 1995 that the Council of Australian Governments should consider the possibility of harmonising the enabling legislation of the Commonwealth and State Auditors-General to allow for joint performance audits of SPP administration. The Committee also recommended that, in the interim, the Auditor-General should investigate the possibility of conducting coordinated performance audits of SPPs with State Auditors-General.¹⁰

9 JCPA, *Report 342*, pp.66-67.

10 JCPA, *Report 342*, p.69.

4.28 In its response to Report 342 the ANAO provided an example of how the ANAO and the Victorian-Auditor-General's office had conducted simultaneous audits of the Building Better Cities Program (BCP). The ANAO audited the Commonwealth funds as used by Commonwealth agencies and transferred to State government agencies. The Victorian Auditor-General's Office audited State government agencies' use of Commonwealth funds and their matching financial contributions. The result of these two audits were the ANAO's *Audit Report No.9 1996-97, Building Better Cities* tabled in Parliament in October 1996 and the Victorian Auditor-General's Office Special Report No.45, *Building Better Cities: A Joint Approach to Urban Development*, tabled in the Victorian Parliament in November 1996.

4.29 The ANAO commented that:

Although our audit jurisdiction and that of the Victorian Auditor-General differ, cooperation between our two offices enabled a more complete picture to be gained of the BCP. In our view, this kind of cooperation adds significant value to the audit products of both agencies.¹¹

4.30 The ANAO also told the Committee that it would continue to explore options for increasing the number of coordinated audits undertaken with State and Territory Audit Offices in order to further add value at both levels of public administration. This was most likely to occur in the performance audit area. These links were recognised by the ANAO's strategic management of the audit function, particularly within the context of the approach to Commonwealth/State program development and service delivery being taken by the Council of Australian Governments.

Recent developments

4.31 The Committee notes that the *Auditor-General Act 1997* (which replaced the *Audit Act 1901*) has extended the powers of the Commonwealth Auditor-General to enter into an arrangement with any person or body to:

11 ANAO Response to Report 342, dated 10 December 1996, attached to the Finance Minute on Report 342.

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- audit financial statements of the person or body;
- conduct a performance audit of the person or body; and
- provide services to the person or body that are of a kind commonly performed by auditors.

4.32 The Act also allows the Auditor-General to enter into agreements to provide services for purposes which are within the Commonwealth's legislative power and where, in the Auditor-General's opinion, it is in the interests of the Commonwealth so to do. Audits by arrangement may include joint audits with State Auditors-General of Commonwealth/State activities.

4.33 The Committee welcomes this move towards improving accountability and urges that further steps be taken at an intergovernmental level to remove any existing obstacles to the conduct of joint audits.

Conclusions

4.34 The Committee reached the following conclusions concerning conditions relating to the role of State Auditors-General.

4.35 State Auditors-General are responsible for auditing the operations of State agencies administering State government activities. Their mandate is set down in the audit legislation of their respective States and Territories. They are not subject to control or direction by the Commonwealth Government.

4.36 Previous JCPA inquiries have highlighted problems encountered by State Auditors-General when financial audit and acquittal responsibilities have been imposed on them under SPP agreements between the Commonwealth and the States.

4.37 Commonwealth departments have been advised by DoFA not to attempt to direct State Auditors-General to perform such tasks. The Committee reiterates its support for this advice. It intends to monitor any recent changes in the imposition of duties on State Auditors-General in relation to SPP programs, through examination of the results of the ANAO's survey of SPPs expected to be reported in October 1998.

4.38 The JCPA's inquiry into SPP administration in 1994-95 identified a number of statutory constraints on joint performance audits by the Commonwealth and State Auditors-General in relation to SPP programs.

4.39 Within existing jurisdictional constraints, there is potential for coordinated performance audit coverage of SPP programs, through cooperative effort by the Commonwealth and State Auditors-General. This was demonstrated by the example of the conduct of simultaneous audits of the Better Cities Program by the Commonwealth and Victorian audit offices.

4.40 The new Commonwealth Auditor-General Act 1997 extends the powers of the Commonwealth Auditor-General to undertake audits by arrangement, including joint audits with State Auditors-General. Further steps need to be taken at an intergovernmental level to provide for such joint audits.

4.41 The Committee concludes that the effective discharge of the responsibilities of Commonwealth and State Auditors-General for the audit of SPP programs is promoted through the ideal features set out in the box below.

In the interests of enhancing the public accountability of Commonwealth and State government agencies for SPP programs without compromising the statutory independence of State Auditors-General, it is important that:

- responsibilities for the financial certification of SPP payments are not imposed on State Auditors-General; and
- opportunities for the conduct of coordinated or joint audits of SPP programs by the Commonwealth and State Auditors-General continue to be actively pursued.

4.42 This report has drawn attention to the range of conditions attached to general purpose and specific purpose payments and identified ideal features of these conditions. It has highlighted the significant and special place of Auditors-General in the overall accountability framework for the administration of these payments.

4.43 The Parliament is ultimately both the arbiter of the conditions attached to general and specific purpose payments and the institution to which government agencies are accountable for the administration of these payments.

Bob Charles MP
Chairman