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Auditor-General
of Victoria

Parliamentary control and management of appropriations

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VICTORIA

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Under the provisions of section 15 of the *Audit Act* 1994, I transmit my report on *Parliamentary control and management of appropriations*.

Yours faithfully

J.W. CAMERON
Auditor-General

29 April 2003

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Part 1

Executive summary

OVERVIEW

Parliament's role in exercising control over public finances and holding Executive Government to account for the use of the powers bestowed upon it by law, is pivotal to the proper functioning of our democratic system of government.

In October 1997, as part of a Management Reform Program, the Government approved the implementation of an accrual output-based management framework for the Victorian Budget Sector (now termed as the General Government Sector). Under the new framework, Victoria's appropriation arrangements involve the authorisation by Parliament of accrual-based appropriations and their subsequent application by the Treasurer, based on service delivery by departments. The appropriations represent "the price paid" by the Government for service delivery based on the full cost of such delivery, including costs incurred but not yet paid (such as creditors) and depreciation (representing the consumption/depletion of asset capacity associated with output delivery).

During 2001-02, State expenditure, excluding local government, totalled $29 989 million, of which $21 760 million (72 per cent) was funded from parliamentary appropriations.

Given the impact of the wide-ranging reforms to the State's financial management and accountability framework, we examined the current legislative and administrative arrangements associated with parliamentary appropriations to assess whether Parliament's interests are being preserved, and whether there is scope for improvement in the administration of appropriations. This report presents the results of that examination.

The report identifies that the ultimate impact of successive reforms to the State's financial management and accountability framework has been that Parliament has provided the Executive Government with substantial discretion over the spending of taxpayers' funds, but substantial scope remains to strengthen the associated scrutiny and accountability arrangements so as to facilitate effective transparency and accountability to Parliament over public spending.

This report provides the opportunity for Parliament to re-assess how well it is placed to discharge its key role of exercising effective control over public finances and holding Executive Government to account, and identifies opportunities to strengthen the effectiveness of such control.

SUMMARY OF MAJOR FINDINGS

OPERATION OF CURRENT APPROPRIATION FRAMEWORK

Operation of global appropriations

- In Victoria, annual appropriations to departments since 1993-94 have been provided on a global basis, for application towards specified purposes (e.g. for the provision of all outputs of a department), providing substantial resource management flexibility to the Government and departments.

Paras 4.3 to 4.13

- Given the diversity of portfolios and programs managed by Victorian government departments (e.g. the Department of Human Services incorporates the Ministerial portfolios of Health, Aged Care, Housing and Community Services), Parliament currently exercises little directive control over spending on key areas of public services delivered by individual departments, due to annual appropriations being provided to departments on a global basis.

Para. 4.14

- Consideration needs to be given to the role of Parliament in directing government expenditure to major areas of public service and/or policy, including the disaggregation of current global departmental appropriations to levels such as Ministerial portfolios or major public sector agencies within those portfolios.

Para. 4.14

Budget management provisions

- Substantial flexibility is available to the Government, beyond that available through the global appropriation arrangements, with around $2 950 million or 13 per cent of total appropriation expenditure incurred under the authority of the various discretionary budget management provisions in 2001-02.

Paras 4.15 to 4.17

- There is scope to further enhance the quality of current disclosures in relation to annotated receipts ($1 451 million in 2001-02) which represent the largest source of budgetary flexibility exercised by the Government under the available discretionary budget management provisions.

Paras 4.18 to 4.20

- With the exception of the Treasurer's Advance, temporary advances and borrowing against future appropriations, the extent to which budget management provisions can be accessed by the Government to increase spending without further parliamentary sanction is not capped under legislation.

Paras 4.21 to 4.23

OPERATION OF CURRENT APPROPRIATION FRAMEWORK *– continued*

Impact of accrual-based appropriations

- The practical effect of the new accrual appropriation regime is the creation of substantial financial assets available to departments which represent the value of appropriations that have been applied, but for which money has not been drawn from the Consolidated Fund.

  Paras 4.24 to 4.27

- An amount of $1 567 million was available to departments from the Consolidated Fund as at 30 June 2002, to be drawn over future years, including $220 million relating to departmental surpluses, resulting from the operation of accrual-based appropriations.

  Para. 4.28

- Given that these financial assets represent increasingly significant resources available to departments and the Government generally, which are available to be drawn over future years, consideration could be given to improving the disclosures provided in financial reports in relation to these balances.

  Paras 4.29 to 4.30

- To enhance parliamentary control over appropriations, consideration could be given to such measures as establishing an upper limit for surpluses that may be retained by departments for subsequent draw-down from the Consolidated Fund.

  Para. 4.31

Special appropriations

- While the level of expenditure incurred under the authority of special appropriations has been reasonably steady over recent years, given the ongoing and generally uncapped nature of such appropriation authorities, it is important that they be continually reviewed to ensure that they remain appropriate.

  Paras 4.32 to 4.36

Parliamentary scrutiny and oversight of budget estimates and outcomes

- Under the current appropriations framework in Victoria, the Government is required to table supplementary information in Parliament (via the Budget Papers) in support of the annual appropriations. However, it is not legally bound to direct its spending in accordance with the plans and priorities foreshadowed in the Budget Papers – given that they represent supplementary information which is not appended to the Appropriation Acts.

  Paras 4.37 to 4.38

OPERATION OF CURRENT APPROPRIATION FRAMEWORK *– continued*

Parliamentary scrutiny and oversight of budget estimates and outcomes *- continued*

- A core element of Parliament's Public Accounts and Estimates Committee (PAEC) work program involves the annual scrutiny of departmental estimates incorporated in the Budget Papers. However, the PAEC hearings are not finalised and the report which sets out its conclusions is not available to Parliament until after the appropriation bills are debated and passed by Parliament. Therefore, maximum value from the PAEC's estimates scrutiny process is not derived by Parliament when voting on the Government's Appropriation Bills.

  Para. 4.39

- The Budget Papers do not include a reconciliation of the aggregate expenditure detailed in these Papers with the value of appropriations subject to parliamentary consideration. As a result, when voting on the Annual Appropriation Acts, Members of Parliament are not in a position to readily ascertain the extent to which Budget expenditure (as disclosed in the Budget Papers) is subject to parliamentary control through the appropriation process.

  Para. 4.39

- Consideration needs to be given to:
  - enhancing the utility of departmental financial reports by requiring departments to disclose within their audited financial reports information on both the actual and budgeted revenues and expenditures for each output class; and
  - establishing requirements for all public sector agencies to table in Parliament their corporate plans, including key performance indicators and targets.

  Paras 4.39 to 4.40

Administration of appropriations

- The integrity of the output performance information provided by service delivery departments to the Department of Treasury and Finance, as part of the revenue certification process, is critical to the overall effectiveness of ensuring that informed and accurate assessments are made of departmental performance against targets. These assessments ultimately support the Treasurer's decisions on the value of appropriation revenue to be provided to departments.

  Paras 4.41 to 4.48

OPERATION OF CURRENT APPROPRIATION FRAMEWORK – *continued*

Administration of appropriations - *continued*

- To enhance the effectiveness of the revenue certification processes, appropriate strategies and processes should be developed and implemented which provide periodic and independent assurance ultimately to the Treasurer regarding the reliability and integrity of the underlying management information systems from which reported performance data is drawn.

  Para. 4.49

- The current performance measures and targets seek to capture major aspects of output delivery by departments, including quantity, quality, timeliness and cost. However, the diversity of activity, quality and cost drivers are not always captured within the small number of performance measures and targets which are currently used to facilitate accountability for performance and support the funding/appropriation certification process. This represents an inherent limitation of the current output management regime.

  Paras 4.50 to 4.55

- Better focused performance measures are required to enhance performance and accountability.

  Paras 4.56 to 4.57

- A comprehensive methodology needs to be developed by the Department of Treasury and Finance (in consultation with the other departments) to better guide assessments of departmental output performance and ultimately drive the delivery of improved outcomes. The methodology should aim to enhance the objectivity, consistency and defensibility of such assessments.

  Paras 4.58 to 4.67

- Under the pricing arrangements established for the funding of public hospital services, TAFEs and State-owned Arts agencies, "the price paid" to the respective departments for the provision of services includes the cost of depreciation for the delivery of such services. However, the output funding arrangements established between these departments and the individual hospitals, TAFEs and Arts agencies do not include depreciation funding.

  Paras 4.77 to 4.78

- As a result of the above funding arrangements, the ability of TAFEs, hospitals and Arts agencies to effectively manage operational capability is reduced, with responsibility for strategic decisions regarding the funding of asset replacement and investment divested from the service providers to the departments.

  Paras 4.79 to 4.80

USE OF THE TREASURER'S ADVANCE

- The Treasurer's Advance represents a specific appropriation given to the Treasurer each year as part of the Annual Appropriation Act, to meet any "… *urgent claims that may arise before Parliamentary sanction is obtained*".

  Paras 5.1 to 5.4

- Our examination highlighted that a clear definition of what could be deemed to constitute "urgent claims" has not been established in the Appropriation Acts or in other legislation. Accordingly, the type of expenditure that is able to be funded from the Advance has been open to wide interpretation - at the discretion of the Government.

  Paras 5.5 to 5.13

- An example of items funded from the Treasurer's Advance in 2001-02 was $118 million provided to finance special power rebates to householders, small businesses and farmers in outer suburban, regional and rural areas aimed at mitigating the impact of electricity price rises. This item represented a discretionary payment made in the year and, at 30 June 2002, an amount of $106 million remained in a trust account, to be paid in 2002-03.

  Para. 5.12

ROLE OF THE TRUST FUND

- As at 30 June 2002, $1 041 million was held in 77 trust accounts in the Trust Fund, with the majority of this balance ($867 million) relating to accounts established to administer funds which emanate from State sources.

  Paras 6.1 to 6.11

- To facilitate adequate transparency and accountability over the activities of the Trust Fund, which has annual aggregate expenditure exceeding $7 700 million, we recommend that the current annual reporting requirements at a whole-of-government and departmental level be enhanced to incorporate additional disclosures for trust accounts.

  Paras 6.12 to 6.14

- There is a need for ongoing assessment/review by individual departments, and the Department of Treasury and Finance in its central agency role, of the operations of individual trust accounts, to ensure they remain relevant and appropriate in the context of any changes in the operating, accounting and accountability environment, including the associated resource management framework.

  Paras 6.15 to 6.20

Part 2

Introduction

PARLIAMENT AND THE APPROPRIATION PROCESS

2.1 It is generally accepted that 2 of the most fundamental cornerstones of our system of parliamentary democracy, which is modelled on the Westminster system, are the rule of law and the principle of parliamentary approval of government spending. These powers are exclusively held by Parliament, given their wide-ranging effects on the lives and welfare of individuals and the community as a whole.

2.2 Parliament's role in exercising control over public finances and holding the Government of the day to account for the use of the powers bestowed upon it by law, is pivotal to the proper functioning of our democratic system of government.

2.3 The key means by which parliamentary approval is given to government spending is through the annual appropriation process. This process involves having Members of Parliament annually debate and vote on the Government's funding requests, which are specified in annual Appropriation Acts and supported by supplementary information provided in the Government's Budget Papers. The annual Appropriation Acts provide the legal authority for the Government to make payments from the Consolidated Fund (the account into which all revenues of the State which Parliament has the power to appropriate are paid), in accordance with the purposes specified in the Acts.

2.4 In addition to the spending authority provided under the annual Appropriation Acts, further authority is given by various special (standing) appropriations which are instituted in specific legislation. These standing appropriations are a feature of most Westminster-based appropriation frameworks and generally relate to payments which need to be made on an ongoing basis independent of the Government's annual budget priorities.

2.5 To provide the Government with budgetary flexibility in managing the State's financial affairs and responding to emerging demands and developments, the current legislative framework also includes various provisions which enable it to re-allocate and augment existing appropriations, as circumstances may require. These provisions include the annotation of receipts, borrowing against future appropriations, the carry-forward of unused appropriations, transfers between items of departmental appropriations, Treasurer's Advance and temporary advances. These are discussed later in this report.

2.6 Since 1993-94, annual appropriations have been generally provided to departments on a global basis; that is though generic budgetary allocations for broad operating and capital purposes - which has provided substantial resource management flexibility to the Government. In 1998-99, the Government adopted an accrual-based budgeting and appropriation framework which fundamentally changed the nature of appropriations and the way that they are managed.

2.7 The new framework is based on a purchaser/provider model, under which Parliament provides appropriation authority to the Treasurer (acting as the purchaser on behalf of the Government) to purchase outputs from departments (the providers), based on the agreed accrual cost of delivering such outputs. The appropriations are applied by the Treasurer once he is satisfied that the agreed outputs have been delivered by the relevant departments.

2.8 In 2001-02, parliamentary appropriations with an aggregate value of $21 760 million were applied by the Government towards the delivery of services and outputs by departments.

WHY DID WE DO THE AUDIT ?

2.9 Given the wide-ranging reforms that have been implemented over recent years to the State's financial management and accountability framework, we undertook an examination of the current legislative and administrative arrangements associated with parliamentary appropriations to assess whether Parliament's interests are being protected, and whether there is scope for improvement in the administration of appropriations.

2.10 Accordingly, the purpose of this report is twofold. First, to promote Parliament's awareness of the issues impacting on its control and scrutiny of Executive Government spending and, second, to point to opportunities for improvement in the framework and its administration. The audit:

- examines the current appropriation framework and the level of parliamentary control exercised over public finances, including:
  - the operation of "annual global" appropriations and "special" (standing) appropriations;
  - the identification and assessment of any major administrative issues requiring attention to ensure the effective administration of appropriations; and
  - the use of various legislative provisions which enable the application of funds for purposes not anticipated at the time of the tabling of the State Budget;
- examines the use of the Treasurer's Advance; and
- assesses the role of the Trust Fund in departmental financial operations.

WHAT DID THE AUDIT COVER ?

2.11 The audit included an examination of:

- the requirements set out in the *Constitution Act* 1975, *Financial Management Act* 1994, *Audit Act* 1994, Annual Appropriation Acts and Acts containing "special" (standing) appropriations, and other relevant legislation associated with the administration and reporting of appropriations;
- the appropriation frameworks operating at other comparable Australian and overseas jurisdictions;

- the adequacy/effectiveness of administrative arrangements operating at central agency level over the certification of "output delivery" and the consequent application of parliamentary appropriations;
- the adequacy of administrative arrangements for the issuance of funds for previously applied appropriations;
- the extent of use of the relevant legislative budget management provisions, and the accountability thereof;
- the use of the Treasurer's Advance to assess whether its application has been restricted to urgent or previously unforeseen items at the time of the tabling of the State Budget; and
- the scope of Trust Fund operations and their impact on parliamentary oversight of departmental financial operations.

2.12 The audit was complemented by interviews with key central agency and departmental staff, and specialist advice obtained on certain legislative interpretation issues. Recent reports issued by audit offices and relevant parliamentary committees across Australian and overseas jurisdictions were also considered, as well as other relevant material identified through literature searches.

Part 3

Appropriation framework

3.1 In common with all other Australian jurisdictions, the Victorian system of democratic government is based on the Westminster model whereby Parliament (comprising the Crown represented by the Governor, the Legislative Assembly and the Legislative Council) is established as the supreme body with responsibility to make laws, raise taxes and determine how public funds are to be spent.

3.2 The role of Parliament in exercising ultimate control over public finances, and holding the Government of the day to account for the use of powers bestowed upon it by law and the use of resources, is pivotal to the proper functioning of our system of democracy. Parliament, through the authority of Appropriation Acts, authorises the Treasurer on behalf of the Government to apply the revenues of the State towards funding the delivery of government programs and services.

3.3 Public sector finances in Victoria are administered on behalf of the Government by various administrative and statutory bodies, including departments and a range of other public sector agencies. Departments are responsible for the implementation of government policy and the administration of the Government's core economic, social and environmental programs and services, which are mainly funded from public funds rather than user charges. They are established under administrative orders and, through the departmental secretaries, are responsible to particular Ministers. Other public sector agencies are mainly funded from grants provided by departments, user charges and other self-generated revenues. They are usually established and operate under specific legislation, and report to their responsible Ministers.

3.4 Table 3A outlines the elements of the Victorian public sector, excluding local government which is regarded as a separate tier of government.

TABLE 3A
STATE OF VICTORIA – MAJOR SECTORS AND KEY ENTITIES*(a) (b)*

General government (the Budget Sector)			
Public Account (Consolidated Fund/Trust Fund)	*Other*	*Public non-financial corporations*	*Public financial corporations*
Includes - • All government departments; and • Other administrative units, including Office of the Chief Commissioner of Police.	Includes - • TAFE institutes; • Public hospitals and community health services; • Metropolitan and rural ambulance services; • Docklands Authority; • Victoria Legal Aid; and • Metropolitan Fire and Emergency Services Board.	Includes - • Water sector authorities; • Alpine Resort Management Boards; • Australian Grand Prix Corporation; • Public Transport Corporation; and • Urban and Regional Land Corporation.	Includes - • State Trustees Ltd; • Transport Accident Commission; • Treasury Corporation of Victoria; • Victorian Funds Management Corporation; and • Victorian WorkCover Authority.

(a) While the table does not provide a full listing of public sector agencies, it includes some of the key agencies within each of the sectors for illustrative purposes. A full listing of public sector agencies forming the State of Victoria reporting entity is presented annually in the Government's Annual Financial Report.

(b) The definition of sectors forming the State of Victoria reporting entity is based on the national reporting framework employed by the Australian Bureau of Statistics to provide statistics for all Australian jurisdictions, which, in turn, is based on a framework developed by the International Monetary Fund for the presentation of national financial statistics.

Source: Victorian Auditor-General's Office.

3.5 The vast majority of Victorian public sector expenditure is incurred by entities within the "general government sector" which, in the main, is represented by the departments - which are predominantly funded from parliamentary appropriations.

3.6 During 2001-02, expenditure by entities within the general government sector totalled around $25 090 million (2000-01, $22 580 million), of which $21 760 million was funded from parliamentary appropriations (2000-01, $20 944 million) and the balance mainly funded from Trust Fund and non-departmental agency revenues. This compares with total State expenditure - which includes the operations of State-controlled financial and non-financial corporations (but excludes local government) of $29 989 million (2000-01, $28 471 million).

LEGISLATIVE FRAMEWORK

3.7 The legislative framework under which public finances are administered, including the financial management and accountability responsibilities of the Government, are set out in the *Constitution Act* 1975, the *Financial Management Act* 1994, Annual Appropriation Acts and the *Audit Act* 1994.

Constitution Act 1975

3.8 The *Constitution Act* 1975 establishes the framework within which Parliament must operate and includes a number of important financial provisions which establish its supreme role in the control of public finances.

3.9 In particular, the Act provides that "… *all taxes, imposts, rates and duties and all territorial casual and other revenues of the Crown in right of the State of Victoria (including royalties) which the Parliament has power to appropriate shall form one Consolidated Revenue* …". Furthermore, the Act provides that this revenue can only be appropriated for such specific purposes as Parliament directs through legislation.

3.10 These provisions jointly establish the principal mechanism through which Parliament is able to exercise control over "the public purse" and enshrine a fundamental principle of Westminster systems that only Parliament may raise taxes and appropriate (authorise expenditure of) the Consolidated Revenue.

3.11 Finally, the Act provides that the Government shall not issue any moneys from the Consolidated Fund (the account into which all Consolidated Revenue is paid) unless authorised by warrants approved by the Governor. This provision, together with a complementary requirement in the *Financial Management Act* 1994, provides a further constitutional control over the expenditure of Consolidated Revenues. Warrants are prepared by the Treasurer and examined by the Auditor-General, to determine whether the requested funds are legally available, prior to approval by the Governor for the release of funds from the Consolidated Fund.

Annual Appropriation Acts

3.12 Annual Appropriation Acts provide the key mechanism through which Parliament directs the expenditure of public moneys and exercises control over the public purse. These Acts provide authority to the Treasurer to issue funds from the Consolidated Fund for the stated purposes, and within the specified upper limits of authority.

3.13 Annual appropriations represent the "global" spending authorities available to the Government, to be applied by the Treasurer (from the Consolidated Fund) for the following 3 purposes in respect of each department:

- *Provision of outputs* – the production or acquisition of goods and services;
- *Additions to net asset base* – the acquisition or construction of assets, or the injection of capital funding; and
- *Payments on behalf of the State* – transfer payments, central financing costs and other expenditure not directly related to the purchase of goods and services by the Government.

3.14 In a small number of cases, these spending authorities are supplemented by specific appropriations within the annual Appropriation Act relating to such things as environment protection, regional infrastructure development and law reform.

3.15 Appropriations are provided on an accrual basis, covering all costs incurred in service provision (including the cash components and other accrual costs such as asset depreciation and accrued employee entitlements). As certain of these incurred costs (such as long service leave) may not become payable within the same year, the annual Appropriation Acts and the *Financial Management Act* 1994 (the FMA) provide for them to be met from the Consolidated Fund over future financial periods (which is further discussed later in this Part of the report).

3.16 The annual Appropriation Acts also contain a contingency provision which is available to the Government to cover unanticipated increases in employee-related costs. In particular, section 3(2) of these Acts provides authority for the Treasurer to issue additional amounts from the Consolidated Fund if, in the financial year, the amount payable for salaries and related costs is increased as a result of any industrial award or determination, and the relevant appropriation sum is insufficient to cover these additional cost.

3.17 In addition, the annual Appropriation Acts also include a specific amount available for use as an Advance to the Treasurer (known as the Treasurer's Advance) to meet *"… urgent claims that may arise before Parliamentary sanction is obtained, which will afterwards be submitted for Parliamentary authority"*. The Acts include 2 Schedules which provide a summary of urgent expenditures made by the Government in the most recently completed financial year, from temporary advances (issued under the authority of section 35 of the FMA, which are discussed later in this report) and from the Treasurer's Advance. This expenditure is deemed to have been duly appropriated from the Consolidated Fund through the passing of the Acts. This provides the accountability mechanism for the Government to account for its use of the discretionary funds provided by way of Treasurer's Advances and temporary advances.

Special Appropriations

3.18 In addition to the appropriations authorised by Parliament under annual Appropriation Acts, around 30 Acts of Parliament contain "special" appropriation provisions for payments that need to be made by departments, either on a one-off or ongoing basis, independent of the Government's annual Budget priorities. These provisions cover such expenditures as the costs of Parliament and the judiciary, and electoral expenses. Special appropriations represent a standing authority and do not lapse until the relevant Acts are amended or repealed.

Financial Management Act 1994

3.19 The *Financial Management Act* 1994 (the FMA) is the State's principal financial legislation and establishes the framework for:

- the collection, expenditure and management of public moneys and other public resources, including the operation of the Consolidated Fund and the Trust Fund; and

- the financial accountability responsibilities of the Government and individual public sector agencies for their administration and stewardship of public resources.

3.20 The following are the more significant elements of the FMA.

Financial responsibility

3.21 The FMA includes a number of provisions which enshrine the Government's obligation to ensure the sound management of public financial resources. In particular, it requires the Government to establish and maintain a budgeting and reporting framework that is consistent with various principles of sound financial management which are set out in the Act.

3.22 It also establishes a comprehensive reporting regime to facilitate transparency over the Government's financial operations. This includes requirements for the Government to present to Parliament:

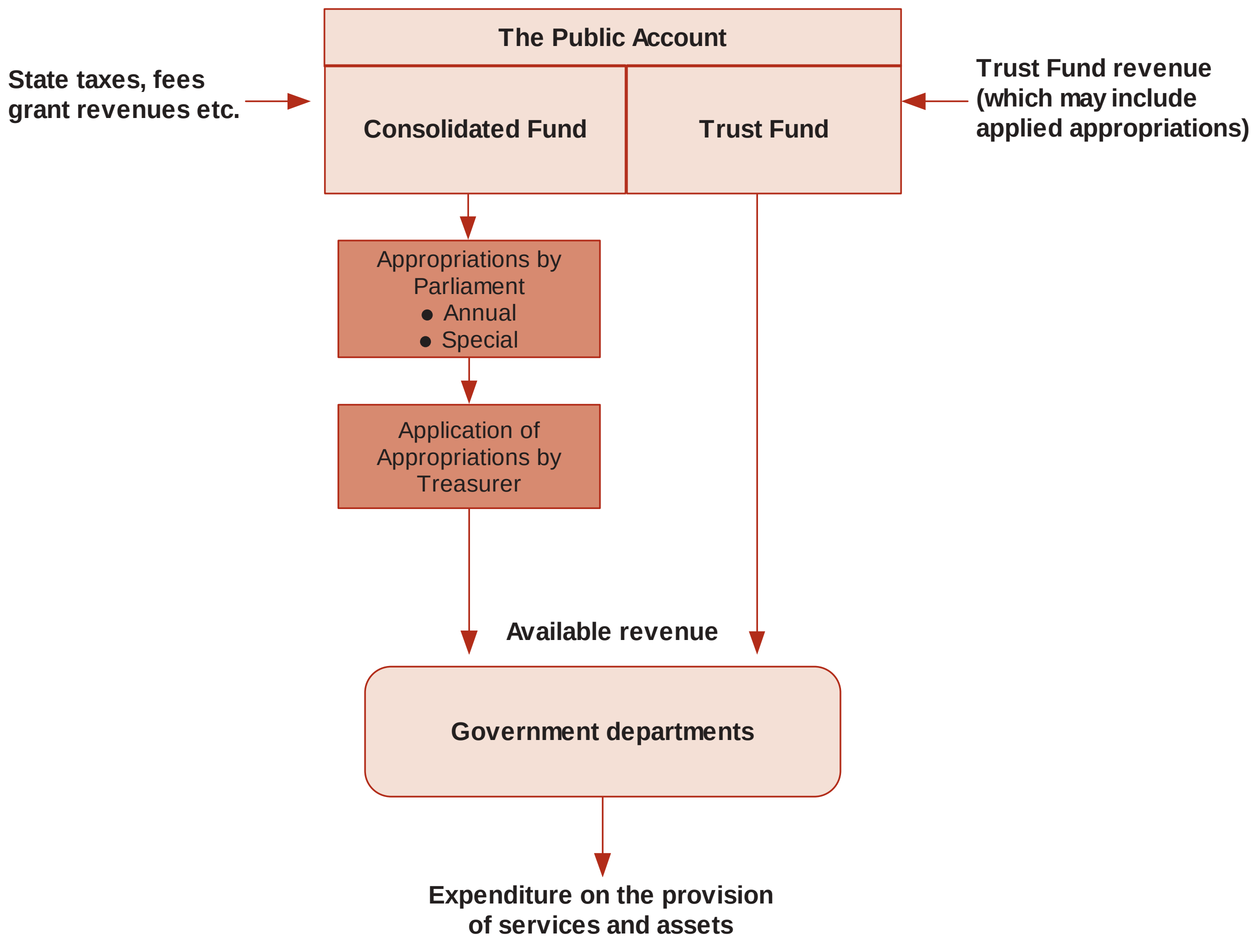
- its key financial policy objectives and strategies;
- the Estimated Financial Statements for the Victorian Budget Sector, which are subject to the Auditor-General's review;
- a mid-year Budget update, which updates the earlier Estimated Financial Statements taking into account the impact of any subsequent government decisions and circumstances which may have a material impact on them;
- an Annual Financial Report, which presents the audited consolidated financial statements of the State of Victoria and the Victorian General Government (Budget) Sector, together with certain additional disclosures - including the transactions and balances of the Public Account (which comprises the Consolidated Fund and the Trust Fund);
- a mid-year consolidated financial report, which provides similar disclosures to the annual financial report;
- quarterly financial reports for the Victorian General Government (Budget) Sector;
- updated information on the estimated financial statements prior to State elections; and
- annual reports of each department and public body.

3.23 This reporting regime provides a wealth of information to Parliament (and the community) to facilitate its oversight of government financial operations.

The Public Account

3.24 The FMA establishes the Public Account as the Government's central bank account, which includes the transactions of the Consolidated Fund and the Trust Fund. Chart 3B outlines the role and relationship of the Public Account with parliamentary appropriations and the financing of departmental operations.

CHART 3B
THE PUBLIC ACCOUNT AND PARLIAMENTARY APPROPRIATIONS



Source: Victorian Auditor-General's Office.

3.25 The Consolidated Fund represents the Government's main operating account. All money forming part of the Consolidated Revenue under the *Constitution Act* 1975 and all other money raised by or on behalf of or received by the State (which is not required by the FMA or any other Act to be paid into the Trust Fund) is required to be paid into the Consolidated Fund.

3.26 Moneys can only be appropriated and issued from the Consolidated Fund with the expressed authority of Parliament. This authority is provided in 2 forms, either as a standing authority (special appropriations) or annually through annual Appropriation Acts (annual appropriations).

3.27 Under section 17 of the FMA, public money forming part of the Consolidated Fund can only be drawn under warrant/s approved by the Governor. This provision complements the previously mentioned requirement of the *Constitution Act* 1975.

3.28 The FMA establishes the Trust Fund and provides for its operation. The Minister for Finance may establish trust accounts within the Trust Fund and define the purposes for which they are established. These mainly relate to the on-passing of certain Commonwealth grants to specified recipients, the operation of departmental suspense and working accounts, and the receipt and payment of moneys of a trust nature (such as specific purpose donations etc.). Trust accounts which form part of the Trust Fund may also be established under the provisions of other legislation. Moneys standing to the credit of a trust account in the Trust Fund can only be spent for the purposes of that account.

3.29 The Minister for Finance may direct that moneys standing to the credit of a trust account may be invested, with such a decision generally dependent upon whether a business case exists for interest on these balances to be returned to the particular trust account within the Trust Fund. Of course, this ministerial discretion does not apply where the crediting of interest to a trust account is provided for in specific legislation. All interest earned on Trust Fund balances, other than that required to be paid into specific trust accounts, is credited to the Consolidated Fund.

3.30 As all public money received by the Government is required to be paid into the Public Account (that is, either the Consolidated Fund or the Trust Fund), except for the transactions of a number of bank accounts that, with the approval of the Minister for Finance under the FMA, operate outside the Public Account (such as State school bank accounts), the financial operations of departments are reflected in the transactions of the Public Account.

Budget management

3.31 Parts 2 and 6 of the FMA contain a number of provisions which, under specified conditions, provide flexibility for the Government to manage its financial affairs. These mainly include:

- *Appropriation of additional Commonwealth grants (section 10)* – Where money is, or will be, made available by the Commonwealth to the State by way of a grant or otherwise, under an Act of the Commonwealth or an arrangement between the Commonwealth and the State, the Treasurer (with the approval of the Governor-in-Council) may issue out of the Consolidated Fund such amount as is required to be expended in the year and the amount is to the necessary extent appropriated (i.e. a special appropriation);
- *Borrowing against future appropriations (section 28)* – The Governor-in-Council, on the recommendation of the Treasurer, may approve the allocation to a department of amounts in addition to the amounts appropriated under the annual appropriation. The Treasurer must not recommend an allocation under this provision unless satisfied that it is for purposes considered prudent and advantageous in the current year, and that the benefit of that allocation will accrue or continue in the next financial year. The amount allocated/approved must not exceed 3 per cent of the relevant department's annual appropriation, or exceed 0.5 per cent of total annual appropriations for the year. This authority represents a special appropriation;

- *Annotation of receipts (section 29)* – Certain amounts received by departments may be credited against specified "net" annual appropriation items to the extent, and on the conditions, agreed between the Treasurer and the responsible Minister. An amount equal to that credited is deemed to have been appropriated for the purposes of that appropriation item. This increases the value of appropriations available to departments. Annotated receipts may include amounts collected from the provision of outputs (user charges), the sale of assets, or specific purpose payments by the Commonwealth or municipal councils. The key administrative principles underpinning the type of receipts suitable for annotation are commented upon later in this report;
- *Transfers between items of departmental appropriation (sections 30 and 31)* – Appropriation amounts may be transferred between individual items of appropriation for the same department, with the consent of the Treasurer or, in the case of parliamentary departments, the relevant presiding officers;
- *Carry-forward of unused appropriations (section 32)* – Where an appropriated amount for a financial year is not applied, or is not likely to be applied, the Treasurer may determine prior to the end of that financial year that the amount, or part thereof, may be carried-forward and applied by the respective department in the following financial year;
- *Draw-down of appropriations in future years (section 33)* –Moneys may be drawn-down from the Consolidated Fund in future years in the discharge of the expenses incurred, or obligations or arrangements made in relation to appropriations previously applied – which facilitates the operation of accrual appropriations. The section also provides that, where part of an appropriation amount applied relates to depreciation of assets, funds equivalent to that amount may only be drawn from the Consolidated Fund for the purpose of acquiring assets; and
- *Temporary advances (section 35)* - An amount not exceeding 0.5 per cent of the total amount appropriated by the annual Appropriation Act for that year may be advanced from the Public Account to the Treasurer to meet urgent claims before parliamentary approval is obtained. Such advances are repaid to the Public Account once parliamentary approval is obtained via the passing of the subsequent year's annual Appropriation Act.

3.32 In addition to these provisions, section 11 of the FMA provides the Treasurer with a standing appropriation authority to cover any sums required to fulfil any guarantee provided in the name of the State of Victoria under an Act, contract, agreement etc.

3.33 Further, section 40H provides the Treasurer with a standing authority to issue from the Consolidated Fund any sums required to fulfil any liability arising under any indemnity given by the Treasurer under Part 6 of the Act. Such indemnities include those provided to officers or directors of public bodies or State companies, and indemnities provided to those bodies or companies themselves.

3.34 The above budget management provisions contained within the FMA, except those associated with temporary advances and transfers between items of departmental/parliamentary appropriations have, in the main, been operative since 1994-95.

3.35 While sections 30 and 31 of the FMA facilitate transfers between items of departmental appropriations, section 4 of the Administrative Arrangements Act 1983 allows transfers of appropriation between departments with the approval of the Governor-in-Council, where departmental operations or responsibilities are transferred between departments as a result of changed administrative arrangements.

3.36 **All of the above legislative provisions enable the Government to re-allocate appropriations or to apply additional resources towards purposes deemed appropriate by the Government in the management of the State's affairs, within specified conditions.**

Audit Act 1994

3.37 The *Audit Act* 1994 provides for the independent audit of Victorian public sector operations by the Auditor-General, on behalf of Parliament.

3.38 The Auditor-General's mandate includes annual financial audits of the State's consolidated financial report (the Government's Annual Financial Report) and the financial reports of individual departments and public bodies, and the review of the Government's Estimated Financial Statements in the annual Budget Papers. It also provides authority for the Auditor-General to report to Parliament on the finances of the State of Victoria, and the results of performance audits and other audit inquiries.

ACCRUAL OUTPUT MANAGEMENT – ADMINISTRATION OF APPROPRIATIONS

3.39 Historically, parliamentary appropriations have represented an entitlement for departments to spend cash in a financial year for specified purposes, which were generally input focused (e.g. for recurrent or capital purposes).

3.40 In October 1997, as part of a Management Reform Program aimed at improving the management of public sector resources, the Government approved the implementation of an accrual output-based management framework for the Victorian Budget Sector (now also termed as the General Government Sector).

3.41 The adoption of this new framework as from the 1998-99 financial year has required significant changes in:

- the way that departmental finances (including parliamentary appropriations) are administered, managed and reported; and

- the relationships between the Treasurer (including the responsible central agency – the Department of Treasury and Finance), and the respective portfolio Ministers (and the related service delivery departments) in relation to resource management.

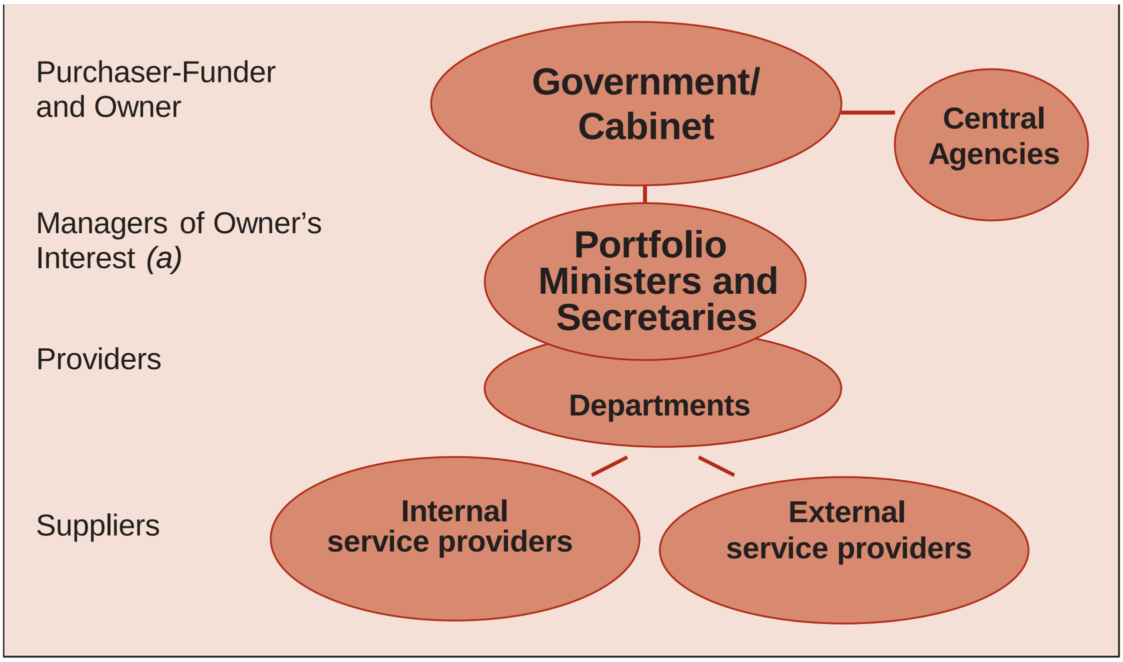
3.42 The fundamental elements of change incorporated in the output-based management framework were:

- a full accrual approach to planning, budgeting, resource allocation and reporting;
- a focus on the outputs that departments provide, rather than the inputs required to provide services; and
- a focus on managing the total resources available to departments.

3.43 The new arrangements are based on a purchaser/provider model, under which Parliament provides appropriation authority to the Treasurer (acting as the purchaser on behalf of the Government) to purchase outputs from departments (acting as the providers), based on an agreed accrual "price" (funded under the authority of appropriations) to be paid to departments in return for delivering such outputs. The quantity, quality and timeliness of outputs to be delivered by departments are agreed between the Government and each of the respective portfolio Ministers and departmental secretaries at the commencement of each financial year, and are outlined in the State Budget Papers.

3.44 Chart 3C outlines the respective roles and relationships of the various parties under this framework.

CHART 3C
ROLES AND RELATIONSHIP UNDER THE ACCRUAL OUTPUT MANAGEMENT FRAMEWORK



(a) Relates to departmental operations.
Source: Adopted from Department of Treasury and Finance, *Accrual Accounting Manual*, October 1998.

3.45 More specifically, under the current arrangements the Government performs the combined role of purchaser, funder and owner – with the Treasurer on behalf of the Government performing the role of purchaser under the Appropriation Acts in relation to the application of appropriations. The central agencies (the Department of Treasury and Finance, and the Department of Premier and Cabinet) provide support and advice to the Government in the discharge of these roles.

3.46 Portfolio Ministers and departmental secretaries perform the role of providers of goods and services, which may be supplied either internally or by external service providers, and the role of managers of the "ownership" interest in departments.

3.47 These roles are borne out through the relationships and accountabilities of the respective parties, under which departments, through the respective portfolio Ministers and departmental secretaries:

- are responsible for the delivery of agreed outputs and services and are ultimately accountable for such delivery to the Government, via the Minister for Finance and the Treasurer; and
- are accountable to the Government for their operating results and the management of assets and other resources (i.e. the management of the ownership interest).

3.48 The operation of large departments in Victoria which service multiple portfolio Ministers and the related output groups (for example, the Department of Infrastructure – which services the portfolios of the Minister for Transport, Minister for Energy Industries, Minister for Major Projects, and Minister for Information and Communication Technology), acts to complicate the relationships and associated accountabilities between portfolio Ministers, and the Minister for Finance and the Treasurer (acting as purchaser on behalf of the Government in relation to the application of appropriations). However, the role of departmental secretaries, in assisting portfolio Ministers in the discharge of their responsibilities, serves as the single conduit between the portfolio Ministers, and the Minister for Finance and the Treasurer in relation to the accountability responsibilities associated with the appropriation process. In addition, the senior or lead Ministers generally assume a co-ordinating role in dealing with corporate and cross-departmental issues.

3.49 For administrative purposes, a "State Administration Unit (SAU)" account has been established within the Consolidated Fund to meet the accounting and accountability needs that arise from the introduction of the new accrual-based output management arrangements. These include the recording of the Treasurer's transactions (acting as "the purchaser" on behalf of the Government), and the departmental entitlements to draw-down applied appropriations (which may be accessed to cover incurred costs when they become due and payable). The SAU account is administered by the Department of the Treasury and Finance.

3.50 The application of appropriations by the Treasurer to departments (for the purposes specified in the respective Appropriation Acts) is based on an assessment of whether the agreed outputs and other services have been delivered. The arrangements established to facilitate this process include the following key elements:

- Departmental expenditure on outputs is initially funded from available departmental financial resources. Generally, these represent the department's share of the SAU account balance, being the value of appropriations that have been previously applied but not fully drawn-down by departments from the Consolidated Fund due to certain accrual costs not becoming payable until future financial periods. Simply put, these departmental financial assets represent cash entitlements from the Treasurer for accrual costs incurred in previously delivering services;
- Departments issue quarterly invoices to the Treasurer for the application of appropriations in respect of the outputs delivered in the previous quarter; and
- The Treasurer approves the quarterly application of appropriations - representing the agreed price/revenue paid to departments for the delivery of agreed outputs, based on an assessment of output/service delivery claimed by departments against the agreed targets.

3.51 A significant feature of the arrangements is that, while historically appropriations were directly related to departmental expenditure, under the accrual output management framework, appropriations represent "the price paid" (revenue earned) for the delivery of agreed outputs. Accordingly, departments may generate surpluses or deficits in the delivery of outputs where the cost of delivery is greater or lower than the agreed price. The costs of delivery include:

- all direct costs in producing outputs;
- a share of the amortised expense of assets consumed in the production of outputs (e.g. depreciation); and
- a surrogate for the cost of capital tied up in the net assets employed (i.e. the capital assets charge).

3.52 In cases where deficits are generated, departments are expected to recover these deficits over future periods though efficiencies in output production. Conversely, where surpluses are generated, departments are able to access these funds, with the Treasurer's agreement, to provide additional outputs. This is intended to provide an incentive to departments to improve operating efficiency.

3.53 Table 3D provides a summary of appropriations applied by the Government over the period 1998-99 to 2001-02.

TABLE 3D
TOTAL APPROPRIATIONS APPLIED
($million)

Item	*1998-99*	*1999-00*	*2000-01*	*2001-02*
Annual appropriations -				
Net appropriations applied for specified departmental purposes *(a)*	14 535	14 196	16 128	17 192
Appropriations applied associated with budget management provisions *(b)*	1 714	1 750	2 189	2 566
Sub-total	*16 249*	*15 946*	*18 317*	*19 758*
Special appropriations -				
Standing appropriations	*(c)* 10 534	2 420	2 464	1 683
Appropriations applied associated with budget management provisions	130	200	163	319
Sub-total	*10 664*	*2 620*	*2 627*	*2 002*
Total	**26 913**	**18 566**	**20 944**	**21 760**

(a) Net appropriations refer to “base” appropriation amounts applied under the authority of annual Appropriation Acts, which excludes the effect of the operation of other legislative budget management provisions.

(b) This item does not include amounts transferred between items of departmental appropriations under FMA sections 30 and 31, which do not increase the aggregate level of parliamentary authority.

(c) In 1998-99, standing appropriations include the impact of the application of proceeds from the Government’s privatisation program.

Source: Victorian Auditor-General’s Office.

Part 4

Operation of current appropriation framework

4.1 The key means by which parliamentary authorisation is given to government spending is either through standing legislation (known as special appropriations) or the passing of annual Appropriation Acts. In examining the nature and extent of control exercised by Parliament in the authorisation of government expenditure through the appropriation process, we considered the following key factors:

- the manner in which annual Appropriation Acts specify the purposes for which moneys may be spent;
- the extent of expenditure funded under the authority of special (standing) appropriation arrangements;
- the flexibility available to the Government to re-allocate approved appropriations from one purpose to another, and to supplement annual appropriations under the authority of discretionary budget management provisions; and
- the accountability requirements on the Government for its use of powers to determine the purpose and extent of spending of public funds.

4.2 Our findings against these criteria are discussed below. This Part of the report also discusses the major impacts of the new accrual-based output management arrangements, their implications in the context of parliamentary control and oversight exercised over government expenditure, and the available opportunities to further enhance the arrangements.

OPERATION OF GLOBAL APPROPRIATIONS

4.3 Global appropriations, also referred to as “one line” appropriations, are provided to departments for application towards specified purposes (e.g. for the provision of all outputs of a department) and provide substantial resource management flexibility to the Government and departments.

4.4 In Victoria, annual appropriations to departments since 1993-94 have been provided on a global basis, albeit with differences in focus. Between 1993-94 and 1997-98, appropriations were generally provided to departments for 2 generic purposes, namely, current/recurrent and capital/works and services. From 1998-99, annual appropriations have generally been provided for each of the following 3 purposes:

- *Provision of outputs* – the production or acquisition of goods and services;
- *Additions to net asset base* – the acquisition or construction of assets, or the injection of capital funding; and
- *Payments on behalf of the State* – transfer payments, central financing costs and other expenditure not directly related to the purchase of goods and services by the Government.

4.5 These appropriations represent the base amount that the Government can spend. That is, they represent “base” parliamentary appropriations, with the authority limits able to be increased through the operation of various legislative budget management provisions as outlined previously in this report, including section 29 of the *Financial Management Act* (FMA) which enables the parliamentary authority to be increased by amounts equivalent to the value of “annotated receipts” collected by departments.

4.6 The following is an extract from the 2002-03 annual Appropriation Act.

Sch. 1

Appropriation (2002/2003) Act 2002

Act No. 33/2002

DEPARTMENT OF INFRASTRUCTURE

Item		2001/2002 *Budget*	2002/2003 *Estimate*
		$'000	$'000
1.	Provision of outputs (section 29 of the **Financial Management Act 1994** applies)	2 101 532	2 276 491
2.	Additions to the net asset base	208 701	299 883
3.	Payments made on behalf of the State	11 383	16 720
	Total Appropriation	2 321 616	2 593 094

Example: Global Annual Appropriations to the Department of Infrastructure, 2002-03.
Source: Appropriation (2002/2003) Act 2002.

4.7 To put these global appropriations into context, the Appropriation (2002/2003) Act 2002 authorises $19.6 billion of expenditure on 30 individual items across the various departments, including the Treasurer’s Advance. Of these appropriation items, 9 relate to the provision of outputs by departments and account for $17.1 billion, or 87 per cent of the annual appropriation to departments. The balance mainly relate to appropriations for additions to net assets ($792 million or 4 per cent), payments on behalf of the State ($932 million or 5 per cent) and the Treasurer’s Advance ($622 million or 3 per cent).

4.8 In support of these global appropriations, the Government is required, under section 40 of the FMA, to provide certain supplementary information to Parliament in the State Budget Papers. This includes the outputs/services expected to be produced or provided by each department, and a description of the total funds available to each department during the relevant period. However, supplementary information is not binding, in that the Government is free to shift moneys between departmental outputs within the broad appropriations without recourse to Parliament.

4.9 Under the Directions of the Minister for Finance issued pursuant to the FMA, departments are required to include in their Annual Reports (which are tabled in Parliament subsequent to the end of each financial year) a comparison of the output targets specified in the State Budget Papers with actual performance achieved. This represents the accountability mechanism to Parliament for output performance achieved by departments in the preceding year. As this information is included in the report of operations section of annual reports, it is not subject to audit by my Office.

4.10 Table 4A presents a summary of global appropriations applied by the Treasurer between 1998-99 and 2001-02 under the authority of the annual Appropriation Acts.

TABLE 4A
NET ANNUAL APPROPRIATIONS APPLIED
($million)

	Annual net appropriations applied (a)				
Financial year	*Provision of outputs*	*Net additions to asset base*	*Payments on behalf of the State*	*Other*	***Total annual net appropriations applied** (a)*
2001-02	15 649	509	1 016	18	**17 192**
2000-01	14 714	187	1 205	22	**16 128**
1999-00	13 617	231	333	15	**14 196**
1998-99	12 821	307	1 392	15	**14 535**

(a) Does not include the Treasurer's Advance, and other amounts applied in the respective financial years under section 3(2) of the relevant Appropriation Acts to cover additional employee-related costs associated with industrial awards and determinations (including: 2001-02 - $264 million; 2000-01 - $245 million; 1999-00 - $39 million; and 1998-99 - $19 million), and funds applied under other legislative budget management provisions.

Source: Victorian Auditor-General's Office.

4.11 While these global appropriation arrangements provide substantial flexibility to the Government in managing the State's financial affairs, including decisions as to the quantity, quality and mix of outputs/services to be delivered, and major asset investment choices etc., the level of direct control exercised by Parliament over government spending is limited – representing the trade-off between control and management flexibility.

4.12 In determining the extent of flexibility to be provided to the Government, Parliaments respond through their legislative frameworks in different ways, shaped by the preferred administrative philosophy, and the historical and political influences of the day. Appendix A of this report provides an outline of the appropriation frameworks adopted by a number of Australian jurisdictions, New Zealand and the United Kingdom - highlighting similarities and differences in the approaches taken by the respective jurisdictions to the control of government expenditure.

4.13 As shown in Appendix A, there are differences between jurisdictions in the level of aggregation at which appropriations are provided. For example, while in Victoria global appropriations are provided at a departmental level (which incorporates multiple Ministerial portfolios and provides funding for on-passing to other major public sector agencies such as Victoria Police), at the Commonwealth Government level separate global appropriations are provided for each major public sector agency within portfolios (for example, within the Treasury portfolio, individual appropriations are provided for the specific purposes of the Department of Treasury, the Australian Bureau of Statistics, the Australian Taxation Office etc.). In New Zealand, appropriations are provided at the output group level.

4.14 In the above context, and **given the diversity of portfolios and programs managed by Victorian departments (for example, the Department of Human Services incorporates the Ministerial portfolios of health, aged care, housing and community services), Parliament currently exercises little directive control (though the current global appropriations) over spending on key areas of public services delivered by individual departments. Accordingly, consideration needs to be given to the role of Parliament in directing government expenditure to major areas of public service and/or policy, including the disaggregation of current global departmental appropriations to levels such as Ministerial portfolios or major public sector agencies within those portfolios.**

BUDGET MANAGEMENT PROVISIONS

4.15 In addition to the flexibility provided under the global appropriation arrangements, further flexibility is available to the Government to re-allocate and augment existing parliamentary appropriations as circumstances require, without further express parliamentary approval. The key budget management mechanisms available to the Government under the current legislative framework, as outlined previously in this report, cover:

- *Treasurer's Advance* – included in schedule 1 of the Annual Appropriation Act;
- *Salary and related cost increases* – under section 3(2) of the Annual Appropriation Act;
- *Appropriation of additional Commonwealth grants* – under section 10 of the FMA;
- *Borrowing against future appropriations* - under section 28 of the FMA;
- *Annotated receipts* - under section 29 of the FMA;
- *Transfers between items of departmental appropriation* - under sections 30 and 31 of the FMA;
- *Carry-forward of unused appropriations* - under section 32 of the FMA;
- *Draw-down of (accrual-based) appropriations in future years* - under section 33 of the FMA*;* and
- *Temporary advances* - under section 35 of the FMA.

4.16 The extent of use of these discretionary budget management provisions in the funding of departmental operations over the 4 year period to 30 June 2002 is shown in Table 4B.

TABLE 4B
UTILISATION OF BUDGET MANAGEMENT PROVISIONS
(Applied Appropriations, $million)

Description	*1998-99*	*1999-00*	*2000-01*	*2001-02*
Annual Appropriation Act -				
Treasurers advance (Appn Act) *(a)*	342	360	427	464
Unanticipated salary and related costs	19	39	245	264
FMA -				
Annotated receipts	1 072	1 101	1 149	1 451
Carried-forward (unused) appropriations	209	181	285	299
Temporary advances	72	70	83	88
Appropriation of Commonwealth grants	94	8	54	145
Borrowing against future appropriations	36	-	-	-
Draw-down of prior year (accrual-based) applied appropriations	-	192	109	174
Transfers between appropriation items *(a)*	375	38	37	65
Total	**2 219**	**1 989**	**2 389**	**2 950**
Total appropriations applied in the year	*(b)* **26 913**	**18 566**	**20 944**	**21 760**
Budget management-related appropriations as a percentage of total appropriations applied *(per cent)*	*(b)* **8%**	**11%**	**11%**	**13%**

(a) These items do not increase the aggregate level of parliamentary appropriation authority.
(b) The value of 1998-99 appropriations includes additional payments in that year of around $8.5 billion (compared with 1999-2000), made under special appropriation provisions for the application of privatisation proceeds towards the reduction of State debt and superannuation liabilities.
Source: Victorian Auditor-General's Office.

4.17 The above table demonstrates that substantial flexibility is available to the Government, beyond that available through the global appropriation arrangements, with around $2.9 billion or 13 per cent of total appropriation expenditure incurred under the authority of the various discretionary budget management provisions in 2001-02. The extent of utilisation of such provisions was generally consistent in the period up to 2000-01, however, increased during 2001-02 from around 11 per cent to 13 per cent of the total appropriations applied.

4.18 To facilitate the Government’s accountability to Parliament for the application of these discretionary budget management provisions, the following reporting requirements have been established:

- annual Appropriation Bills customarily include accompanying schedules which provide a summary of payments made in the most recently completed financial year from the Treasurer's Advance and temporary advances under section 35 of the FMA, with payments made deemed to be appropriated once the Bills are passed by Parliament;
- the Government's Annual Financial Report is required to include details of annotated receipts; borrowing against future appropriations; transfers of appropriations between items; the carry forward of unused appropriations and expenditure made against carried-forward appropriations; and expenditure made against the Treasurer's Advance and temporary advances; and
- departmental annual reports are required to present a compliance statement which provides a summary of the available appropriation authorities, and the value of appropriations applied against these authorities.

4.19 These reporting mechanisms establish a strong ex-post accountability to Parliament for the application of available appropriation authorities. However, in our view, there is scope to further enhance the quality of current disclosures in relation to annotated receipts ($1.4 billion in 2001-02) which represent the largest source of budgetary flexibility exercised by the Government. In particular, under the current reporting regime, only the total amounts of such receipts for each department are disclosed in the Budget Papers and financial reports, with the users of these reports unable to ascertain the key receipt sources subject to annotation.

4.20 **Given the authority provided by Parliament to the Government for the exercise of budgetary flexibility through the utilisation of annotated receipt arrangements, we believe that there should be greater disclosure of the use of such authority by the Government, through the inclusion of summary information of the composition of such receipts, both within the State Budget Papers, the departmental financial statements and the Government's Annual Financial Report.**

4.21 We also observed that, with the exception the Treasurer's Advance, temporary advances and borrowing against future appropriations, the extent to which budget management provisions can be accessed by the Government to increase spending without further parliamentary sanction is not capped under legislation. For example, there are no legislated limits on the level of unspent appropriations that may be carried forward into a subsequent year, the extent to which annotated receipts can augment approved net appropriations and the transfer of approved appropriations between purposes.

4.22 Other jurisdictions (such as the United Kingdom) that impose legislated cap/limits on the authority available to the Government through budget management provisions, such as revenue retention arrangements, typically utilise supplementary appropriations as the mechanism to facilitate Parliament's consideration and approval of expenditure beyond that previously approved under Appropriation Acts. In Victoria, the flexibility that is available under the current budget management provisions is such that supplementary parliamentary appropriations have not been required.

4.23 **While we recognise that the imposition of legislated caps/limits for the use of budget management provisions, in addition to those already in place, would act to reduce government financial flexibility, consideration could nevertheless be given to this avenue as a means of strengthening Parliament's oversight and control over public spending**. Under this approach, Parliament would establish clear boundaries for the exercise of discretionary expenditure authority by the Government, with expenditure requirements beyond such boundaries required to be explicitly considered and, to the extent that additional appropriation authority is required, approved by Parliament.

Impact of accrual-based appropriations

4.24 A major development over recent years has been the progressive movement by Australian jurisdictions from cash to accrual-based budgeting and appropriations, resulting in a reduced focus on financial inputs and increased attention to outputs and outcomes achieved.

4.25 The implementation of accrual-based output appropriations in Victoria as from 1998-99 has had a major impact on the nature of the appropriations and how they are administered. The key features of the new regime include:

- appropriations cover the full cost of service provision (including cash and non-cash components) and, once applied, may be drawn-down over future years to meet these costs as they become payable;
- appropriations are not directly linked to departmental expenditure but represent the "price paid" by the Government (through the Treasurer) to departments for the provision of agreed outputs/services; and
- departments may generate surpluses or deficits from the provision of outputs, with surpluses available for spending by departments without further parliamentary approval.

4.26 This accrual-based funding regime has particular significance in the context of the traditional parliamentary appropriation processes. While in the past, appropriations were applied to directly fund departmental payments, under the new arrangements the nexus between the appropriations and departmental expenditure is broken. Appropriations represent "the price paid" to purchase agreed outputs and services. In simple terms, this means that once an appropriation is applied (i.e. the Treasurer agrees to pay for the services provided), to the extent that the value of the appropriation exceeds the expenditure incurred by the department in the production of the agreed outputs, the department is able to utilise such funding for other/additional purposes without further direct parliamentary approval.

4.27 The practical effect of the new accrual appropriation regime is the creation of substantial financial assets by departments which represent the value of appropriations that have been applied but for which money has not been drawn from the Consolidated Fund. These funds are available, without further parliamentary approval, for application towards the payment of creditors and other liabilities, the financing of asset replacements (reinvesting to maintain asset capacity as reflected in depreciation expenses), or the delivery of additional outputs - where surpluses are available from previous service delivery.

4.28 The value of these financial assets has grown over the past 3 years, reflecting the increasing maturity of the new accrual-based appropriation arrangements. As indicated in Table 4C, under these arrangements, **$1.6 billion was available to departments from the Consolidated Fund as at 30 June 2002, to be drawn over future years.**

TABLE 4C
PREVIOUSLY APPLIED APPROPRIATIONS REMAINING UNDRAWN FROM THE CONSOLIDATED FUND, AT 30 JUNE
($million)

Year	*Amount*
1999	949
2000 *(a)*	861
2001 *(a)*	1 176
2002 *(a)*	1 567

(a) The composition of these balances is outlined later in this report, with the 30 June 2002 balance including $52 million relating to depreciation equivalents and $220 million relating to departmental surpluses.

Source: Victorian Auditor-General's Office.

4.29 The aggregate value of these financial assets is disclosed in departmental financial reports as part of receivables and the Government's Annual Financial Report as part of the Consolidated Fund balance. However, such reports do not disclose the key components of these balances, such as the surplus component which may be used to fund outputs not of an ongoing nature, or the depreciation component which is available for the funding of asset replacement in future years.

4.30 **In our view, given that these financial assets represent increasingly significant resources available to departments and the Government generally, which are available to be drawn over future years, consideration could be given to improving the disclosures provided in financial reports in relation to these balances.** This could be effected through the establishment of specific requirements for the disclosure by departments and in the Government's Annual Financial Report of:

- the key components of such balances; and
- for the application of the components attributable to departmental surpluses and depreciation, a summary of the outputs funded and assets replaced from the application of these funds.

4.31 **In addition, to enhance parliamentary control over appropriations, consideration could be given to such measures as establishing an upper limit for surpluses that may be retained by departments for subsequent draw-down from the Consolidated Fund.**

SPECIAL APPROPRIATIONS

4.32 Special appropriations are standing spending authorities in specific legislation, for payments which need to be made either on a one-off or on-going basis. Special appropriations are established to fund protected expenditures such as the salaries of the judiciary, the costs of Parliament, electoral expenses, employer contributions to superannuation funds and debt retirements. They also facilitate the hypothecation of certain revenue towards specific purposes; for example, gambling revenue towards the funding of public hospitals.

4.33 While the application of special appropriations does not require annual authorisation by Parliament, the Government's annual Budget Papers include, for the sake of budgeting completeness, estimates of such appropriations expected in the year.

4.34 Table 4D indicates the extent and nature of special appropriations applied during the 4 financial years to 2001-02.

TABLE 4D
SPECIAL APPROPRIATIONS APPLIED
($million)

Purpose	*1998-99*	*1999-00*	*2000-01*	*2001-02*
Hypothecation of gambling revenues	1 219	1 318	1 139	1 213
Superannuation and debt payments	*(a)* 9 116	886	1 169	265
Salaries and expenses of the Judiciary, Parliament and independent positions	51	52	61	65
Budget management provisions *(b)*	130	200	163	319
Other miscellaneous *(c)*	148	164	95	140
Total special appropriations applied	**10 664**	**2 620**	**2 627**	**2 002**
Total all appropriations applied	**26 913**	**18 566**	**20 944**	**21 760**

(a) Reflects the part application of privatisation proceeds towards State debt retirement and the reduction of unfunded superannuation liabilities.

(b) Includes appropriations under the authority of the FMA section 10 (Commonwealth grants), section 28 (borrowing against future appropriations) and section 33 (draw-down of previously applied appropriations).

(c) Includes expenditure under various legislative authorities, such as electoral expenses, Crown proceeding settlements, assistance to victims of criminal crimes, etc.

Source: Victorian Auditor-General's Office.

4.35 As indicated in the table, substantial expenditure is funded each year under special (standing) appropriation authority, with this authority provided by around 30 individual Acts of Parliament. This expenditure represented around 9 per cent of total applied appropriations in 2001-02 and mainly comprised the automatic hypothecation of gambling revenues towards specified purposes, and payments made towards the reduction of State debt and unfunded superannuation liabilities.

4.36 **While the level of expenditure incurred under the authority of special appropriations has been reasonably steady over recent years, given the ongoing and generally uncapped nature of such appropriation authorities, it is important that they be continually reviewed to ensure they remain appropriate.**

PARLIAMENTARY SCRUTINY AND OVERSIGHT OF BUDGET ESTIMATES AND OUTCOMES

4.37 Under the current appropriations framework in Victoria, the Government is required to table supplementary information in Parliament (via the Budget Papers) in support of the annual appropriations. It is not, however, legally bound to direct its spending in accordance with the plans and priorities foreshadowed in the Budget Papers – given that they represent supplementary information which is not appended to the Appropriation Acts.

4.38 Nevertheless, the global appropriation approach places substantial weight on the effectiveness of Parliament's budget review processes, in ensuring an informed parliamentary debate and vote on the annual appropriation bills, and the related expenditure plans and priorities of the Government. Effective ex-post accountability to Parliament through the annual reports prepared by individual departments, which are required to include information on output performance compared with the targets presented in the Budget Papers, is also important – given that these ex-post reports facilitate Parliament's oversight of government spending and stewardship.

4.39 The following observations are made in relation to the current parliamentary review processes associated with annual appropriation Acts and ex-post reporting by departments:

- A core element of Parliament's Public Accounts and Estimates Committee (PAEC) work program involves the annual scrutiny of departmental estimates incorporated in the Budget Papers. However, the Committee's hearings are not finalised and the reports which set out its conclusions are not available to Parliament until after the appropriation bills are debated and passed by Parliament. Therefore, maximum value from the PAEC's estimates scrutiny process is not derived by Parliament when voting on the Government's Appropriation Bills.

In recognition of the need to advance the budget scrutiny processes, the PAEC brought forward its timetable for the conduct of estimates hearings in respect to the 2002-03 Budget, with such hearings held between May and July 2002 - compared with May to September in the previous year. While we acknowledge this positive initiative of the Committee, the outcomes of such hearings were still not reported to Parliament until after the Appropriation Acts were passed.

The approaches adopted by other jurisdictions to improve the timeliness of parliamentary scrutiny of budget estimates have included the establishment of multiple select committees which participate in intensive budget briefings/hearings within tight time frames, tasked to report to Parliament prior to the passing of the Appropriation Acts, and/or the establishment of "supply" arrangements which operate for an interim period into the financial year, pending Parliament's consideration, scrutiny and passing of the Appropriation Acts later in the year;

- In support of the Annual Appropriation Bills presented for parliamentary consideration, the Government's Budget Papers provide substantial information on the estimated expenditures and resources of the Victorian Budget Sector (also known as the General Government Sector) and the individual departmental portfolios. However, the Budget Papers do not include a reconciliation of the aggregate expenditure detailed in these Papers with the value of appropriations subject to parliamentary consideration. As a result, when voting on the annual Appropriation Acts, Members of Parliament are not in a position to readily ascertain the extent to which Budget Sector expenditure (as disclosed in the Budget Papers) is subject to parliamentary control through the appropriation process.

  In addition, while output performance measures and targets are presented by the Government in its Budget Papers, disclosures are not explicitly required in Budget Papers or subsequent departmental annual reports where changes are made to these measures or targets between years, in response to changes in output group mix, structures etc. - reducing the comparability of performance information and Parliament's capacity to assess performance trends between periods. Given that frequent changes to performance measures, and poor disclosures associated with such changes, substantially impair the utility of this information for assessing performance, it is important that changes should be kept to a minimum to facilitate comparability between periods;

- While substantial information is available to Parliament, through the Budget Papers, on the Government's and departmental objectives, and outputs and associated measures and targets, departments and other public sector agencies are not required to table or otherwise make publicly available ex-ante information which outlines their broader corporate objectives, priorities, key indicators of efficiency and effectiveness, and associated performance targets. The availability of this information to Parliament would assist in its assessment of government appropriation requests and facilitate effective ex-post accountability for performance; and

- Departmental annual reports include unaudited statements of output performance which provide comparisons of performance achieved with the measures and targets published in the Budget Papers, and audited information of actual revenues and expenditures associated with each output group for the current and previous years. These reports facilitate accountability to Parliament on the Government's application of available parliamentary authority, and are generally scrutinised and reported by the PAEC each year with the view to informing parliamentary debate and future budgetary considerations by Parliament. However, as the PAEC assessment of departmental outcomes has generally not been presented to Parliament until May of the following financial year, around the time that the State Budget is presented to Parliament for the subsequent financial period, there is limited opportunity available for Members to absorb and assess this information as part of the budgetary deliberations.

4.40 **In our opinion, the combination of these factors, in conjunction with the operation of global appropriation arrangements, act to reduce the effectiveness of parliamentary oversight over government spending. To enhance such oversight and accountability, we recommend that consideration be given to:**

- **the identification and pursuit of available avenues to facilitate the more timely conduct and finalisation of Parliament's scrutiny and reporting of budget estimates and outcomes**;
- **the disclosure of reconciliations of estimated expenditures contained in the Budget Papers with parliamentary appropriations sought by the Government** – to provide a linkage between the 2 documents;
- **the strengthening of the output performance reporting requirements, to explicitly provide for the reporting in subsequent periods of the rationale for discontinuing performance measures and, where ever possible, further information which assists in the comparability of performance information between periods**;
- **enhancing the utility of departmental financial reports by requiring all departments to disclose within their audited financial reports information on both the actual and budgeted revenues and expenditures for each output class, for the current and previous years; and**
- **the establishment of requirements for all public sector agencies to table in Parliament their corporate plans, including key performance indicators and targets.**

ADMINISTRATION OF APPROPRIATIONS

4.41 Under the current legislation, the Treasurer is assigned the authority under the annual Appropriation Acts to apply the appropriations approved by Parliament, in accordance with the purposes specified in the Acts. Consequently, the Treasurer is ultimately responsible for the establishment and effective operation of the framework used to administer appropriations.

4.42 This section of the report outlines the results of our examination of the current administrative arrangements for appropriations. It also identifies opportunities to enhance the effectiveness and transparency of the arrangements.

Application/certification of appropriations

4.43 The Treasurer is assigned the legal authority to apply appropriations and issue moneys from the Consolidated Fund. The following key processes support the Treasurer's application of appropriations:

- *Specification of output deliverables and targets* – Following the deliberative processes associated with the preparation of annual State Budget estimates, the agreed outputs to be delivered and targets to be achieved by departments during the year (including quantity, quality and timeliness) are set out in the annual Budget Papers, together with the agreed appropriation funding ("the price") to be provided to the departments by the Treasurer on behalf of the Government, once satisfied that the agreed outputs have been delivered.

  Once the Budget process is completed, agreement is reached between the individual departments and the Department of Treasury and Finance (DTF) on the targets to be used at the end of each quarter as the basis for assessing the department's performance and progress towards achieving the annual targets and, therefore, the value of appropriations that should be applied by the Treasurer for the relevant quarter;
- *Quarterly invoicing* - At the end of each quarter, departments submit an invoice/claim to the Treasurer setting out the outputs delivered, actual performance against agreed targets (including quantity, quality, timeliness and cost), any changes to the output mix, and comments on any major variations between actual performance and the agreed targets;
- *DTF assessment and advice* – The DTF undertakes an assessment of departmental invoices/claims to determine whether the agreed service delivery has occurred - drawing on the annual targets published in the Budget Papers and the previously agreed phased targets to be used for the quarterly assessment process. Based on its assessment, the DTF makes a recommendation to the Minister for Finance on the delivery (or non-delivery) of the agreed outputs and the value of appropriations to be applied for the quarter. There are 3 options relating to this recommendation, namely:

  - *Full certification* of departmental invoices/claims and application of the "agreed" appropriation sum – where departments are assessed as having fully delivered the agreed outputs;
  - *Partial certification* of departmental invoices/claims and part application of the "agreed" appropriation – where departments are assessed as having under-delivered the agreed outputs; and
  - *Approval* of departmental invoices/claims and application of the "agreed" appropriation – where output delivery cannot be reliably assessed as departments are unable to provide appropriate or sufficient information to support the delivery of outputs in a quarter. In such cases, departmental invoices/claims are approved but not certified and the "agreed appropriations" are applied, however, the figures are subject to subsequent verification and, if necessary, adjustment. This option is only available for the first three-quarters of a financial year, with the final quarterly assessment process resulting in either full or partial certification of departmental invoices/claims; and

- *Treasurer certification and application of appropriations* - Based on the certification/approval of the Minister for Finance and the supporting DTF assessments, the Treasurer formally applies the appropriations.

4.44 We examined the operation of these processes over the period from July 2000 to March 2002 for 2 departments, namely, the Department of Education and Training (known as the Department of Education, Employment and Training prior to March 2002) and the former Department of State and Regional Development (which is now known as the Department of Innovation, Industry and Regional Development, with certain of its functions transferred to the newly created Department of Victorian Communities). We also held discussions with senior staff involved in the revenue certification process, both at the DTF and a number of other departments, to confirm our understanding of the operation of the processes. Our examination identified the following issues.

Reliability of departmental output performance information

4.45 The integrity of the output performance information provided by service delivery departments to the DTF, as part of the revenue certification process, is critical to the overall effectiveness of ensuring that informed and accurate assessments are made of departmental performance against targets. These assessments ultimately support the Treasurer's decisions on the value of appropriation revenue to be provided to departments.

4.46 We identified that, while the DTF quarterly assessment process includes progressive discussions by analysts with departments on performance-related issues, the process does not incorporate any systematic and periodic independent validation of departmental performance information. Accordingly, while the conceptual underpinnings of the revenue certification process are similar to those relating to progress payment regimes established under long-term supply arrangements with external suppliers (which typically incorporate appropriate validation/assurance processes to ensure delivery prior to payment), the processes associated with the application of appropriations do not incorporate such structured and periodic validation/assurance processes.

4.47 In December 2000, the Government approved the establishment of a 5-year program involving the systematic evaluation of all departmental outputs, aimed at assessing the appropriateness of the pricing of the output, and enhancing their alignment with departmental objectives and overall government outcomes. The first 11 of these reviews were conducted in late 2001 by staff drawn from the relevant departments, the DTF and the Department of Premier and Cabinet. The output reviews raised a number of concerns regarding the availability and reliability of departmental data on output performance, which was a key hindrance to the effective evaluation of output targets. The reviews also identified that, in many cases, departments do not cost, manage or monitor their activities on an output basis. However, the review teams concluded that continuance of the output reviews should provide an ongoing incentive for departments to invest in enhanced data collection and monitoring systems to measure and improve performance.

4.48 Our research of other jurisdictions identified that the provision of specific assurances by agencies regarding the integrity of performance-related information is an important accountability feature of their frameworks. For example, in the United Kingdom, a series of measures were recently implemented to ensure the integrity of departmental performance targets, including a requirement for departments to facilitate the examination of all relevant data systems at least once during the "lifetime" of a public sector agency service agreement (3-year periods) and to publicly report on when the data systems were, or will be, subject to validation. In the United States, under legislation introduced in 1993, public sector agency annual performance plans are required to provide explanation of the procedures the agency will use to verify and validate its performance data.

4.49 **To enhance the effectiveness of the revenue certification processes, appropriate strategies and processes should be developed and implemented which provide periodic and independent assurance to DTF and the Treasurer regarding the reliability and integrity of the underlying management information systems from which reported performance data is drawn**.

Quality of output measure and target information used for the revenue certification process

4.50 In assessing the effectiveness of the appropriation certification (and the associated departmental accountability) process, it is also necessary to consider whether the output performance measures and targets are sufficient to facilitate effective accountability for departmental performance, and enable informed DTF assessments of such performance. Overall, performance measures and targets should provide a clear picture of what the department is seeking to deliver, including the key/significant aspects of such delivery. Performance measures and targets that focus on only part of the organisation's activity may lead to unmeasured activities being neglected and/or provide dysfunctional incentives to departments.

4.51 This issue is particularly difficult within the Victorian context, given that departmental operations over the past decade have been consolidated into a small number of very large departments which have responsibility for the delivery of a diverse and complex range of services to the community. Such services are grouped into a number of outputs for which departments are funded and are accountable through the appropriation certification process which focuses on performance achieved against the agreed performance measures and targets. For example, the Department of Human Services delivers a broad range of health and other community services, which are grouped into around 60 outputs with more than 250 measures of quantity, quality, timeliness and cost.

4.52 Over recent years, a number of DTF reviews have highlighted serious deficiencies with the published performance measures of departments. In particular, a DTF evaluation of the implementation of the Government's Management Reform Program in mid-2000 identified, as a common theme, the need to review and refine output performance measures in terms of relevance and accuracy, and particularly improve output costing. In response to these findings, the Government approved the implementation of the previously mentioned output review program to provide a systematic evaluation of service delivery, including output performance measures across the Budget Sector. Departments were also required to review a number of issues, in particular their output costing methodologies.

4.53 **A key observation of the first round of output reviews was that, in many cases, departments do not cost, manage or monitor their activities on an output basis.** The review teams considered that correcting this position would require investment in departmental information systems and a commitment to best practice service delivery, by the departments identifying appropriate indicators of performance and then targeting and measuring performance improvement. **The reviews also highlighted a shortage of evaluative skills and experience in departments. Limited evidence was also found of a dynamic or innovative service delivery culture which regularly tests whether outputs are having the desired effect on government outcomes and question whether the output or output mix continues to remain effective.**

4.54 We were advised by the Department of Treasury and Finance that the specific recommendations of the individual output reviews have been considered by the Government and have been fed into the decision-making process regarding the future delivery of such outputs.

4.55 Our examination of the appropriation certification process and discussions with senior staff of various departments identified similar issues to those identified during the output reviews. In particular, the current performance measures and targets seek to capture major aspects of output delivery by departments, including quantity, quality, timeliness and cost. However, the high level of output specification (under which outputs may cover a large number of activities and programs) means that the diversity of activity, quality and cost drivers are not always able to be captured within the small number of performance measures and targets which are used to facilitate accountability for performance and support the funding/appropriation certification process. This represents an inherent limitation of the current output management regime.

4.56 We identified cases where performance measures for particular outputs (such as those in the Education sector) only focused on particular aspects of output delivery generally related to current program and policy priorities (such as teacher-to-student ratios, computer-to-student ratios etc.). As such, in our view the set of such measures did not adequately capture (and facilitate effective departmental accountability for) overall output performance. This observation, which is illustrated in the following case study, was consistent with the findings of our performance audit of *Departmental Performance Management and Reporting*, the results of which were reported to Parliament in November 2001. It is clear from this case study that better focused performance measures are required to enhance performance and accountability.

Case Study

Department of Education and Training – Primary Education Output

While it is generally considered that the key cost driver of primary education is the number of students being educated within Victorian primary schools, this measure is not identified in the Government's Budget Papers or as part of the revenue certification process as a key quantitative performance measure for this output. Average class sizes and pupil-to-teacher ratios are identified as output measures, however, without the overall figure of the number of students and the numbers at relevant year levels, these ratios lack context.

For effective education to occur in our primary schools, students need to be in attendance at school, within class and paying attention. However, there is also no measure of student attendance for this output group.

The 'outputs' of the primary education system represent inputs into the secondary education system. At a minimum, these 'outputs'/students would be expected by the community to be literate and numerate enough to take-up the opportunities presented in their next stage of schooling. While the 2002-03 Budget Papers contain measures of Prep and Year 1 reading levels, there are no corresponding measures of mathematics/numeracy.

Measurement of literacy and numeracy levels at Years 3 and 5 were included in the 2001-02 Budget Papers, however, they were not presented in the 2002-03 Budget Papers. Hence, the output measures for primary education do not include any measurement or targets for student learning beyond Year 1.

Case Study - *continued*

Department of Education and Training – Primary Education Output - *continued*

Overall comment

The current regime of output measures in primary education focuses more on the implementation of government priorities, such as lowering class sizes, learning technologies and implementation of early years literacy, and does not capture core aspects of primary education output delivery.

Without key aspects of output delivery such as student numbers, student attendance and comprehensive measurement of student learning, departmental accountability for output performance is limited.

4.57 **To enhance departmental accountability and the effectiveness of the appropriation certification process, we recommend that the output measures and targets published in the Budget Papers (and used as part of the certification process to hold departments to account), should seek to capture the key aspects of output delivery, and be supplemented with brief supporting information outlining the underlying complexities and key drivers of quantity and quality impacting on the cost of each output. This information would provide an appropriate context from which meaningful assessments of output delivery and performance could be made by DTF, as part of the appropriation certification process, and by Parliament as part of the accountability process.**

Quality of quarterly output performance information and associated revenue assessments

4.58 The key objective of the quarterly reporting process is to ensure the provision of an appropriate level of information by departments to DTF to facilitate effective assessments of departmental performance and ultimately support the Treasurer's quarterly certification and application of appropriation revenue.

4.59 A major dilemma facing DTF analysts in the revenue certification process is that a significant number of key performance measures reported by departments, in particular the Department of Education and Training and the Department of Human Services, are only available on an annual or 6-monthly basis and, therefore, performance in relation to those measures is not able to be assessed on a quarterly basis. For example, data for the "Year 3 students reaching national benchmarks in reading" target for the Department of Education and Training - primary education output group (for 2000-01) was only available in the March 2001 quarter, for the 2000 school calendar year.

4.60 As indicated previously, once DTF assessments of departmental performance are completed, the options available to DTF analysts are to recommend to the Minister of Finance and the Treasurer, the “approval”, “certification” (in full or in part) or “rejection” of departmental revenue claims. Where limited performance information is provided by departments for certain output groups (in particular, in the first 3 quarters of the financial year), DTF generally recommends to the Minister of Finance and the Treasurer that the claim be “approved” - pending certification, when the performance information becomes available in the following quarter.

4.61 We observed that, for the first 2 quarters in 2000-01, 34.8 per cent of the aggregate departmental claim value was certified, 65.1 per cent was approved, and less than one per cent rejected. This compared with 33.3 per cent certified, 66.6 per cent approved, and less than one per cent rejected for the same period in 2001-02.

4.62 In cases where comprehensive output performance information is not provided or available to support the departmental quarterly revenue claims, judgements are made by DTF analysts on the percentage of the revenue claimed that should be “fully certified”, “partially certified” or “approved”, based on the performance measures reported. For example, if 80 per cent of the performance measures for an output group are reported and are on target, generally 80 per cent of the claim would be “fully certified” and 20 per cent of the claim “approved” pending the provision of further information. When analysing the output performance, the perceived importance of the performance measures reported and met for the quarter relative to the other targets in the output group where appropriate data is not available or where there has been under-performance are also taken into account. Rejection of claims is generally viewed as a last resort measure. In the period July 2000 to June 2002, only 4 claims were rejected in part by the Treasurer, with a value of $22.8 million – mainly due to under-performance compared with previously agreed targets or the non-availability of appropriate data to support performance.

4.63 While it is recognised that the delivery of some outputs cannot be readily related to specific quarters and annual business cycles, the high ratio of departmental claims approved but not certified during the course of a year nevertheless raises concerns regarding the quality of the quarterly performance measures used to facilitate the progressive monitoring of departmental performance under the current regime, and the overall effectiveness of the quarterly reporting/certification process. Accordingly, **a review of the current quarterly performance measures and targets is recommended to enable departments to more clearly demonstrate progress in the delivery of agreed outputs.**

4.64 We also observed that, based on DTF assessments of departmental performance against established output targets for the year ended 30 June 2001, departmental performance for 66 per cent of all outputs was assessed to be "on target", 19 per cent was assessed as being "above target", and 15 per cent was assessed to be "below target". The term "on target" was defined by DTF as meeting the majority of the "key" measures for outputs, as agreed between the departments and DTF at the commencement of the financial year. However, 98 per cent of the revenue claimed by departments was certified and the appropriation was applied ($15.7 billion). Of the 15 per cent of outputs where departmental performance was assessed to be below target, DTF considered that the variance between target and actual was not significant and, therefore, almost all the revenue claimed was certified.

4.65 For the year ended 30 June 2002, departmental performance for 62 per cent of all outputs was assessed by DTF to be "on target", 26 per cent of all outputs were assessed to be "above target", 11 per cent were assessed at "below target", the remainder (around one per cent) were not measured. However, we observed that 99 per cent of the revenue claimed by the departments was certified ($17.7 billion).

4.66 **We found that, in the absence of pre-determined weighted unit costs associated with individual output targets (relative to the agreed total output group cost) to guide revenue certification/approval decisions, it was difficult to objectively assess what portion of departmental claims should be certified, approved or rejected. Consequently, such assessments/decisions became quite subjective and open to differing interpretations.**

4.67 **We recommend that a comprehensive methodology be developed by DTF (in consultation with departments) to better guide/assist assessments of departmental output performance (particularly the value of revenue to be certified, approved or rejected) and ultimately drive the delivery of improved outcomes. The methodology should aim to enhance the objectivity, consistency and defensibility of such assessments.**

Operation of annotated receipt arrangements

4.68 As previously mentioned in this report, a key feature of the Victorian appropriation framework is the operation of annotated receipt arrangements whereby, under section 29 of the *Financial Management Act* 1994, the parliamentary authority limit for certain departmental appropriation items may be increased by an amount equal to the value of departmental receipts specified under an agreement between the Treasurer and the relevant departmental Minister.

4.69 Annotated receipt sources mainly include user charges, Commonwealth specific purpose grants and asset sale proceeds. The administrative rules that govern the operation of these arrangements include the following eligibility criteria:

- *User charges* – the receipt should stem from payments which are made for goods and services provided, and the payments made and the benefits gained by the user can be clearly linked to the cost of providing the goods and services;
- *Commonwealth specific purpose payments* – all Commonwealth specific purpose grants paid to the Consolidated Fund, except for certain general education grants, education building grants and health care grants; and
- *Asset sale proceeds* – based on individual business cases made by departments and agreed by the Treasurer in relation to physical assets controlled by the department.

4.70 During our examination of the revenue certification processes for the Department of Education and Training and the former Department of State and Regional Development, we observed that, for 2000-01, Commonwealth specific purpose payments were not specified as relevant receipts within the section 29 annotated receipts agreement entered into between the Treasurer and relevant departmental Ministers. However, these receipts were credited against the relevant appropriation items and applied by the Treasurer in the year. Accordingly, appropriations with a value of $870 million were applied and issued by the Treasurer contrary to the specific legislative requirements which require that such section 29 appropriations are only available where there is an agreement between the Treasurer and the relevant Minister.

4.71 In following-up this matter, DTF advised that Commonwealth specific purpose payments were not included in section 29 agreements for 2000-01 as it was then considered that they were implicitly covered due to their nature, that is, they represented agreements between governments for revenue to be paid to the State by the Commonwealth for specified purposes. However, following an internal review of this position by DTF, Commonwealth specific purpose payments were included in the section 29 annotated receipts agreements for 2001-02.

4.72 Our examination also identified that section 29 annotated receipts agreements were generally not signed prior to the commencement of the financial year and were signed well into the financial year. While our examination did not identify any issues of concern other than those stated above in relation to the operation of section 29 arrangements, these circumstances raise the risk that appropriations may be applied without the necessary legislative requirements being satisfied.

4.73 **To ensure compliance with the legislative requirements for annotated receipt arrangements, it is critical that appropriate agreements be signed by the Treasurer and relevant Ministers covering all receipt sources to qualify for such arrangements. In addition, to ensure the effective administration of such arrangements, it is also recommended that such agreements be finalised prior to the commencement of each financial year.**

Revenue certification ahead of output delivery

4.74 While the key principle underlying the current appropriation arrangements is that appropriations are applied by the Treasurer once satisfied that the required/associated outputs have been delivered, our examination identified 2 cases where outputs were assessed as delivered and appropriations were applied, yet certain deliverables/conditions associated with such funding (which were not explicitly incorporated into the output measures and targets) had not been met by departments at the time of application of the appropriations. This situation resulted in the departments reporting profits arising from the funding, even though the full associated expenditure had not been incurred during the same reporting period.

4.75 In particular, we identified that the appropriation revenue received by the Department of Human Services and the Department of Natural Resources and Environment during 2000-01 included amounts of $22.9 million and $6.9 million, respectively, received pursuant to annotated receipt arrangements (representing Commonwealth Government funds provided for specific programs/purposes). Funds had not been spent by the departments for the purposes for which the Commonwealth funding had been provided and, therefore, the required conditions had not been satisfied by the department at year-end. The amounts formed part of the departmental surplus in their SAU account, which were accessed during the subsequent financial year (i.e. during 2001-02) to deliver the outputs previously agreed with the Commonwealth Government.

4.76 **Given that the application of appropriations ahead of "output delivery" is inconsistent with the appropriation framework, we recommend that the appropriation authority associated with annotated receipts only be applied where the conditions/requirements associated with such receipts (e.g. the conditions of Commonwealth Government grant funding) have been satisfied. In cases where such conditions/requirements have not been met at year-end, it would be more appropriate for departments to seek approval to "carry-forward" the appropriation authority to the subsequent financial year under the authority of section 32 of the FMA.**

Inconsistencies between the basis of appropriations and funding of departmental outputs

4.77 Victoria's appropriation arrangements involve the authorisation by Parliament of accrual-based appropriations and their subsequent application by the Treasurer, based on service delivery by departments. The appropriations represent "the price paid" by the Government for service delivery based on the full cost of such delivery - including costs incurred but not yet paid (such as creditors) and depreciation, representing the consumption/depletion of asset capacity associated with output delivery.

4.78 Our audit identified the following inconsistencies between the above appropriation arrangements and the funding models adopted by departments:

- *Funding of tertiary education and training services (TAFE)* - Whereas the Department of Education and Training receives appropriations to fully fund the provision of tertiary education and training services, the funding arrangements between the department and tertiary and further education (TAFE) institutes (the service providers) for the delivery of these outputs/services do not provide for the funding of depreciation (i.e. the maintenance of asset capacity consumed during output/service provision). Instead, requests by institutes for capital funds are assessed by the Department independent of the output pricing regime and incorporated into the Department's capital program as deemed appropriate;
- *Funding of public hospital services* – Under the pricing arrangements established for the funding of public hospital services, "the price paid" to the Department of Human Services for the provision of services includes the cost of depreciation for the delivery of such services. However, the output funding arrangements established between the Department and the individual hospitals under health service agreements do not include depreciation funding. Again, requests by hospitals for capital funds are assessed by the Department independent of the output pricing regime and incorporated into the Department's capital program as deemed appropriate; and
- *Funding of State-owned arts agencies* – Similar to the above 2 cases, the output pricing arrangements established for the funding of the Arts agencies through appropriations to the Department of Premier and Cabinet include the cost of depreciation. However, the output funding provided to these agencies does not include depreciation funding. The funding made available to meet the cost of depreciation has been used to finance the major redevelopment projects within the Arts portfolio (such as the redevelopment of the Museum of Victoria, the National Gallery of Victoria and the State Library of Victoria). Requests by the Arts agencies for the replacement of operating assets have been assessed by the Department independent of the output funding regime, and incorporated into the Department's capital program as deemed appropriate.

4.79 The above funding arrangements have the following major implications:

- The ability for external service providers (such as TAFEs, hospitals and Arts agencies) to effectively manage operational capability is reduced, with responsibility for strategic decisions regarding the funding of asset replacement and investment divested from the service providers to the respective departments. While it is recognised that this practice facilitates greater central "input" control over such activities by departments, this can also result in reductions in service capability/capacity at a service provider level. In the case of TAFE institutions, our May 2001 report to Parliament entitled *Teaching equipment in the Technical and Further Education sector* identified a gap between depreciation costs incurred over recent years and capital funding provided, resulting in a run-down of the system's capability; and

- In the case of TAFE institutions, the funding model had also resulted in the build-up of financial assets held by the Department, representing applied appropriations which are available to the Department/the Government for spending over future years without the need for further parliamentary sanction. In particular, we identified that, as at 30 June 2001, the balance of that Department's SAU account included an amount of $102 million, representing the unspent depreciation component of appropriations previously provided to the Department for outputs delivered by TAFEs. While this appropriation funding had been implicitly provided Parliament for the maintenance of service delivery capacity (i.e. the replenishment of asset capacity consumed) in the TAFE sector, under the current funding practices the appropriations do not translate to funding entitlements (a receivable) of the individual TAFE institutes where such capacity is consumed but, rather, represent a resource which is centrally controlled and may be reallocated as considered appropriate by the Department.

  As at 30 June 2002, the "unspent" depreciation component of appropriations previously provided to the Department for TAFE outputs delivered totalled $118 million, however, the Department had spent $88 million of this amount on the acquisition of assets for primary and secondary schools, therefore leaving a net balance of $30 million of unspent depreciation funding entitlements held by the Department within its SAU account.

  As indicated above, while the practice of departments not on-passing depreciation funding to service delivery agencies facilitates greater central control over asset investment decisions, it also has a negative effect on the capacity of delivery agency managers to exercise effective asset management and planning, given the uncertainty created about the availability of asset replacement funding.

4.80 **Given the significance of these issues in the context of the current accrual-based (full cost) appropriations and the associated funding regime, we recommend that:**

- **the impacts of these and any other similar funding models on service provider operations/managerial behaviour should be examined with the view to assessing their sustainability, and their consistency with the current output-based purchaser/provider model associated with the administration of appropriations; and**
- **enhanced transparency be provided in the Government's Budget Papers in relation to the operation and impacts of such arrangements, to facilitate a more informed parliamentary debate of the annual appropriation bills.**

Management and application of SAU balances

4.81 The "State Administration Unit (SAU)" has been established within the Public Account to meet the accounting and accountability needs that arise from the introduction of the new accrual-based output management arrangements. These include the recording of the Treasurer's application of appropriations (which may be accessed over future financial periods to cover incurred costs that become due), and the departmental draw-down of moneys from the Consolidated Fund.

4.82 A further function of the SAU is to facilitate the achievement of effective cash management within the Budget Sector, whereby departmental entitlements to cash equivalent to the applied appropriations (representing receivables of departments) are held centrally within the Consolidated Fund until such time as they are required to be drawn-down to meet cash requirements. This avoids individual departments holding substantial cash balances across separate bank accounts.

4.83 Under the established arrangements, when departments require cash to meet their liabilities as they fall due, and for other purposes such as asset replacement, they draw on the balance of the SAU Account and corresponding amounts of cash are paid from the Consolidated Fund into the departmental bank accounts. In the event that the balances of the SAU are insufficient, the Treasurer is able to provide temporary advances to the department under the authority of the FMA.

4.84 The SAU is not a separate legal entity but takes the form of a ledger account which is administered by the Department of the Treasury and Finance on behalf of the Government.

Use of the SAU Account for working capital purposes

4.85 Notwithstanding the availability of various provisions within the FMA (such as sections 36 and 37 of the Act) which enable the Treasurer to issue temporary advances to departments to meet certain costs prior to the availability of appropriations, a key feature of the funding arrangements established under the current framework has been the use of the SAU Account balances by departments for working capital purposes. That is, during the course of each quarter, departments utilise/draw-down the SAU Account balances (which represent funds made available to meet the costs of previous service delivery) to finance their cash flow requirements associated with new service delivery in the quarter - pending the Treasurer's certification of service delivery and the associated application of appropriations at the end of the quarter.

4.86 Given that the value of annual appropriations applied is around $18 billion, cash flow requirements for departmental expenditure (on average) of around $4.5 billion per quarter are, therefore, met from SAU Account balances, prior to the Treasurer's application of the associated appropriations. Accordingly, the SAU balances are utilised by departments to temporarily fund the costs and prepayments associated with the production/provision of outputs for which appropriations are yet to be applied by the Treasurer.

4.87 The rationale advanced for the use of this funding mechanism for departments, rather than using Public Account Advances, is that under the current purchaser/provider arrangements, appropriations represent the "price paid" for service delivery and, once applied, are legally available to departments for use in the general management of their business – including for working capital purposes, without the need for advances.

4.88 We sought legal advice which confirmed that the above practice was not inconsistent with the current legislative provisions for the administration of appropriations. This advice concluded that, as the Appropriation Act provides authority to the Treasurer to apply and issue moneys from the Consolidated Fund for the purposes stated in that Act (which include the provision of outputs), and that the Act contains no detail as to what particular outputs the funds may be expended on, then the use of SAU Account balances associated with prior output delivery towards the temporary funding of "other" outputs does not represent an infringement of the requirements of the Appropriation Act.

Composition of SAU Account balance

4.89 As previously indicated in this report, **departmental financial assets represented by SAU Account balances totalled $1.6 billion as at 30 June 2002 - a significant resource available to the Government for future draw-down from the Consolidated Fund**. Table 4E provides a high level dissection of this balance over a 3 year period (30 June 2000 to 30 June 2002), as determined through an audit analysis of departmental reconciliations of SAU Account balances for these periods.

TABLE 4E
DISSECTION OF SAU ACCOUNT BALANCE (AT 30 JUNE)
($million)

Component	*2000*	*2001*	*2002*
Liabilities (including creditors, employee entitlements etc.)	396	742	*(a)* 1 278
Depreciation equivalents not yet spent	106	128	52
Retained surpluses	367	282	220
Sub-total	*869*	*1 152*	*1 550*
Add/deduct:			
Prepayments	(8)	(5)	(5)
Other balances *(b)*	-	29	22
Total	**861**	**1 176**	**1 567**

(a) Includes $250 million held within the SAU Account of the Department of Treasury and Finance at 30 June 2002, representing an unpresented cheque related to a Government contribution to the State Superannuation Fund.

(b) This item represents SAU Account balances which could not be readily dissected into their specific components.

Source: Victorian Auditor-General's Office.

4.90 As indicated in the table, the vast majority of the SAU Account balance as at 30 June 2002 ($1.3 billion or 81 per cent) represented accrued costs associated with previous output delivery, mainly relating to employee entitlements and creditors, for which money had not been drawn from the Consolidated Fund as they were yet to be paid. These costs will be funded from the SAU Account balance over future years as they become payable.

4.91 The remaining balance mainly represented:

- departmental surpluses ($220 million or 14 per cent) which have resulted from departments delivering outputs at a cost below that previously agreed with the Treasurer; and
- depreciation equivalent funding ($52 million or 3 per cent), which represents depreciation incurred in delivering outputs for which funds equivalent to this amount had not been drawn from the Consolidated Fund for the purpose of funding asset replacements.

4.92 **In recognition that the SAU Account balance represents a substantial resource which, in part, can be used to supplement future output delivery and asset replacement, we re-iterate our earlier comments that consideration should be given to:**

- **improving the disclosures in departmental annual reports and in the Government's Annual Financial Reports of the composition of SAU Account balances and the application of such balances; and**
- **establishing upper monetary limits for the appropriation surpluses that departments may be able to retain for subsequent draw-down from the Consolidated Fund.**

4.93 **In addition, it is important that SAU Account balances be monitored by departments and DTF to ensure their effective management and application in accordance with the legislative and administrative requirements.**

***RESPONSE** provided by Secretary, Department of Treasury and Finance*

This report presents a timely and comprehensive exposition of appropriations and budget management in the context of the management reform program introduced in Victoria in the late 1990s. The Department of Treasury and Finance believes that the report offers some valuable insights and areas for ongoing improvement in the evolving framework for resource and performance management of departments in Victoria.

The intentions of Parliament are expressed in 3 elements: the Appropriation Bills; the detailed supporting information on output delivery and asset investment in the Budget Papers; and the budget and financial management and reporting provisions of the Financial Management Act 1994. This report draws attention to a number of ways in which elements of this framework might be further improved in operation. However, the complex interaction of the 3 parts needs to be given full consideration when proposing changes.

RESPONSE *provided by Secretary, Department of Treasury and Finance - continued*

Ex ante control, ex post accountability

A key consideration in sound public management is the balance between ex-ante control of departmental operations and ex-post accountability for departmental performance. In assessing the merits of the findings and recommendations in the report, the Department believes that it is necessary to take both of these into account.

Ex-ante control, typically in the form of appropriation acts and supporting documentation, articulates the intent of Parliament both in terms of amount of money made available and purposes to which it can be put. Ex-post accountability uses a comprehensive reporting regime including independent audit reports, to monitor the fulfillment of Parliament's expressed intentions, and to evaluate how efficiently and effectively they contribute to the Government's desired outcomes. The space between ex-ante control and ex-post accountability is occupied by the devolution of responsibility to portfolio Ministers and departments, together with an accountability for performance to hold them publicly accountable for results.

The Department notes that while the report covers both ex-ante (in appropriations) and ex-post (in disclosure and certification) aspects of the framework, there is little discussion of their interaction. There appears to be an implicit assumption throughout the report that greater ex-ante parliamentary control, as opposed to improved monitoring, is inherently desirable. It could be argued that a broad measure of flexibility within a global appropriation framework in conjunction with robust ex-post accountability is essential to the workings of a modern State. The Department believes that the current arrangements, as they evolve over time, allow for a sound balance between control and accountability which supports high levels of departmental performance and service delivery in the VPS.

Operation of global appropriations

An important practical consideration relating to increased ex-ante control is the interaction between appropriations and the provisions for budget management, embodied in the Financial Management Act 1994 as noted in the report. Section 30 of this Act allows appropriation amounts to be moved between items of the appropriation within departments. It follows that disaggregation of the appropriations would have no material impact on parliamentary control of appropriation unless either the structure of departments or the provision of the Act were changed. This would also run counter to the fundamental structural principle of Victorian departments which cover a range of related portfolios to facilitate co-ordinated (or joined-up) delivery of services to Victorians.

Budget management provisions

The Department does not support any additional caps or limits on budget management provisions. Under current arrangements ex- post accountability is strong: the Financial Management Act 1994 requires departments to report on actual delivery at detailed output level compared with what they publish in Budget Papers for the scrutiny of Parliament.

Parliamentary scrutiny and oversight of budget estimates and outcomes

As a key element of ex-post accountability, the Department supports in principle greater disclosure of information relevant to assessing the performance of departments, and any practical means of facilitating more timely and informed scrutiny of budget estimates and outcomes. We note, however, that some information may be of limited use, difficult to interpret, and costly to produce. It is the Department's view that this is the case with:

- *detailed reconciliation of estimated Budget expenditures and parliamentary appropriations;*
- *ongoing reporting of discontinued performance measures; and*
- *the inclusion of actual and budget financial data for outputs.*

RESPONSE *provided by Secretary, Department of Treasury and Finance* - *continued*

Parliamentary scrutiny and oversight of budget estimates and outcomes - *continued*

As regards corporate planning, the Department believes the intentions and performance of departments are well reflected in the Budget Papers and annual reports which are tabled in Parliament. While the planning process is crucial to achieving government outcomes, their disclosure and details are internal matters for departmental consideration rather than a matter for Parliament.

Reliability of departmental output performance information

The Department supports more focused, relevant and comprehensive performance measures of outputs, as well as mechanisms for ensuring the integrity and reliability of management information systems for assessing them. Equally important is evidence-based evaluation of effectiveness to ensure that outputs are achieving the Government's desired outcomes as well as careful benchmarking and process analysis to ensure that outputs are being efficiently produced.

It is impossible to be completely objective in certification of outputs, and not particularly profitable to attempt to do so. As a performance and accountability mechanism, certification attempts to be as accurate and fair as possible. The Department provides regular training courses to assist officers in departments and Treasury develop the skills to apply certification consistently.

Revenue certification ahead of output delivery

The Department of Treasury and Finance is currently amending its administrative guidelines to ensure that that the appropriation authority associated with annotated receipts is only applied when the conditions associated with such receipts have been met.

Inconsistencies between the basis of appropriations and funding of outputs

An essential component of the model is that the Government purchases outputs from departments who may engage third parties either within government or in the private sector as providers. The report notes that the funding arrangements between departments and a number of service providers do not automatically involve passing on depreciation equivalents. It is not accurate to suggest that this decision is at the discretion of departments; it resides with the Government when it makes asset investment decisions in the Budget. The Department believes that this approach allows the Government the greatest flexibility as an owner in determining the quantum and timing of asset investment in its businesses, so as to best achieve its outcomes by varying the level of asset investment between various priority areas.

The Department acknowledges that greater disclosure of the composition of the State Administration Unit may be of use to Parliament.

Composition of SAU account balances

As a key element of ex-post accountability, the Department supports in principle greater disclosure of information relevant to assessing the performance of departments. We note, however, that some information may be of limited use, difficult to interpret and costly to produce. In the Department's view, there may be some merit in greater disclosure of SAU Account balances, but there is limited value in detailed disaggregation of transactions on the SAU fund or requiring re-appropriation of funds which Parliament has already appropriated.

Part 5

Use of the Treasurer's Advance

5.1 Given that State Budgets represent prospective estimates of revenue and expenditure based on expected conditions over future periods, it is not unreasonable for them to include some provision for unforeseen events. In the context of the annual appropriation arrangements, such provision is made through the Advance to the Treasurer (known as the Treasurer's Advance).

5.2 The Treasurer's Advance represents a specific appropriation given to the Treasurer each year as part of the Annual Appropriation Act, to meet any *"… urgent claims that may arise before Parliamentary sanction is obtained"*. Such approval is obtained through the subsequent financial year's annual Appropriation Act, which includes a schedule outlining all payments made against the Advance. The following is an extract from the 2002-03 annual Appropriation Act, outlining the use of part of the Treasurer's Advance in the previous year.

Sch. 3

Appropriation (2002/2003) Act 2002

Act No. 33/2002

SCHEDULE 3

Payments from Advance to Treasurer, 2000/2001

Department	*Purpose*	*Amount* $
Education, Employment and Training	Middle Years of Schooling initiative	7 790 000
	WorkCover - impact of government policy changes	5 007 000
	17.5 per cent recreation leave loading backpay	140 000
	Approved wage increases (including on-costs)	71 774 000
		84 711 000
Human Services	Completion of Commonwealth funded programs	1 596 000
	Drugs program expenses	6 000 000
	Legal costs for representation in the Metropolitan Ambulance Service Royal Commission	2 210 000
	Revenue shortfall - private patients in public hospitals	6 300 000
	Trauma System agreement	5 824 000
	Tobacco legislation expenses	3 158 000
	Reinstatement of embedded tax savings for charities	4 400 000
	International Year of Volunteers	200 000
	National Depression Initiative	2 625 000
	WorkCover - impact of government policy changes	14 947 000
	Mildura Hospital - expenses including closure costs of the former hospital	30 825 000
	Program Development Unit expenses	2 453 000
	Latrobe Hospital - allocated facilities charge	4 180 000
	Approved wage increases (including on-costs)	72 222 000
		153 940 000
Infrastructure	Resourcing of major rail infrastructure projects	14 200 000
	Recreational boat operator licensing expenses	1 300 000

Source: *Appropriation (2002/2003) Act* 2002.

5.3 Accountability for use of the Treasurer's Advance is also met through the presentation of a summary of each year's expenditure in the Government's Annual Financial Report which is tabled in the Parliament after the end of each financial year.

5.4 In addition to the Treasurer's Advance, various other budgetary mechanisms are available to the Government to manage the financial impact of unforeseen events, including increasing the parliamentary authority to cover increased salary and related costs arising from industrial awards and determinations, temporary advances, and the transfer of departmental appropriation sums between individual items of appropriation. These are discussed in earlier parts of this report.

Use of the Treasurer's Advance

5.5 Table 5A outlines the level of appropriation authority that has been available to the Government under the Treasurer's Advance, and its application, over the 4 years to 2001-02.

TABLE 5A
TREASURER'S ADVANCE

Financial year	*Total budgeted annual appropriations (a)*	*Treasurer's Advance authority*		*Treasurer's Advance applied (utilised)*
	($m)	*($m)*	*(%)*	*($m)*
1998-99	16 592	342	2.06	342
1999-00	16 845	360	2.14	360
2000-01	18 407	436	2.37	427
2001-02	19 696	470	2.39	464

(a) Represents the estimated gross annual appropriations, including annotated receipts and carried-forward appropriations from the previous year.

Source: Victorian Auditor-General's Office.

5.6 We used 2 broad criteria to inform our assessment of the administration of the Treasurer's Advance, namely, whether the size (value) of this discretionary provision was reasonable relative to need and whether appropriate conditions were attached to its use.

5.7 The level of the Treasurer's Advance, compared with the total budgeted expenditure, does not seem unreasonable, given that the value of the Advance has been equivalent to around 2 per cent of total budgeted annual appropriations for the above 4 years, with such authority fully applied by the Treasurer in 1998-99 and 1999-2000, and substantially applied in 2000-01 and 2001-02.

5.8 The full (or near full) utilisation of the Advance over this period suggests that the expenditure requirements that emerged in those years and classified as "urgent claims" have been at the upper limit of the available appropriation, therefore the full allocation has been required to meet such needs.

5.9 **Our examination highlighted that a clear definition of what could be deemed to constitute "urgent claims" has not been established in the Appropriation Acts or in other legislation. Clear criteria for determining what constitutes "urgent claims" had also not been established at an administrative level to guide assessments of departmental claims for the utilisation of the Advance. Accordingly, the type of expenditure that is able to be funded from the Advance has been open to wide interpretation - at the discretion of the Government.**

5.10 Certain other jurisdictions, such as the Commonwealth of Australia, have dealt with this issue through some greater prescription within legislation and supporting administrative guidelines of the conditions under which expenditures may be funded from such Advances.

5.11 We observed that, in recent times, governments within Victoria have not utilised the available mechanism of Supplementary Appropriations to seek parliamentary approval for expenditure needs that have arisen post the annual appropriation process. Instead, there has been a reliance on the utilisation of the Treasurer's Advance which, over the above 3-year period, has been utilised for a variety of purposes, including additional costs arising from:

- unanticipated developments, such as wage and salary award increases, contractual and legal settlements, natural disaster relief etc.;
- new output initiatives and other costs arising from government policy changes; and
- new or additional capital works.

5.12 The *Macquarie Concise Dictionary* defines "urgent" as "*pressing, compelling or requiring immediate attention or action*". In the context of this definition, our examination identified various examples where expenditure was funded from the Treasurer's Advance which could be subject to differences in interpretation regarding the urgency or otherwise of the expenditure. Table 5B outlines some examples for 2001-02.

TABLE 5B
EXAMPLES OF CLAIMS FUNDED FROM TREASURER'S ADVANCE, 2001-02 *(a)*

Description of funded item	*Amount*	*Reason for funding allocation*	*Audit comment*
Special power payment	$118.0m	To finance special power rebates to be provided to householders, small businesses and farmers in outer suburban, regional and rural areas aimed at mitigating the impact of electricity price rises, in respect of electricity consumed over the period April 2002 to March 2003. The amount (excluding a sum directly disbursed by the then Department of Natural Resources and the Environment) was paid into a trust account of which the Victorian Energy Networks Corporation is Trustee) - with the funds to be progressively applied towards the above purposes over the period 2001-02 to 2002-03.	This item represents a discretionary payment made in the year. As at 30 June 2002, an amount of $106 million remained in the trust account, to be paid in 2002-03.
Timber communities in partnership	$8.6m	To finance various projects in rural and regional communities which were adversely affected by the restructuring of the State's timber industry.	This item represents a discretionary payment made in the year.
Legal aid asset investment grant	$1.4m	To finance the development of a video conferencing network across Victoria involving Victoria Legal Aid and the Department of Human Services, the conduct of various capital improvements at community legal centres, and various other one-off legal aid initiatives.	This item represents a discretionary payment made in the year.

(a) A full listing of claims funded from Treasurer's Advance in 2001-02 is presented in note 32 of the Government's Annual Financial Report, 2001-02.

Source: Victorian Auditor-General's Office.

5.13 While we do not question the merit of these expenditures, **given their discretionary nature, it is open for debate whether it was appropriate to utilise the Treasurer's Advance for these purposes. Accordingly, consideration should be given to more clearly/explicitly defining the purposes to which the Treasurer's Advance might be applied in annual Appropriation Acts, supported with further guidelines at an administrative level, to assist in its future application. Such definition and associated guidelines will assist in articulating Parliament's intentions on the application of the Advance, and will avoid debate and speculation as to the appropriateness of its utilisation towards purposes such as the funding of new or additional outputs and capital works.**

RESPONSE *provided by Secretary Department of Treasury and Finance*

> *It is common practice in many jurisdictions for Parliaments to make available an Advance to the Treasurer to meet emerging priorities during the year. The concepts of “urgent claim” or “discretionary expense” will inevitably remain liable to interpretation. Given that the Advance to the Treasurer and its application are subject to scrutiny in appropriations and the Annual Financial Report, what matters is that the Advance is applied when immediate attention is required to avoid a situation developing with more serious ramifications. It is unlikely that a more precise circumscribing of the application of the Advance to Treasurer would significantly change this situation.*

Part 6

Role of the Trust Fund

6.1 The Trust Fund is established under the *Financial Management Act* 1994 as a separate and discrete component of the Public Account. It comprises:

- Accounts established to record the receipt of certain State funds and their disbursement for specified purposes. These include trust accounts established to record the receipt and disbursement of State revenues which are hypothecated (through special appropriations) to particular purposes, e.g. gaming revenue is hypothecated for the provision of health services;
- Accounts established to record the receipt and disbursement of specific purpose payments from the Commonwealth Government which are on-passed by the State to other organisations (such as non-government schools, local government bodies and TAFE institutes);
- Suspense accounts established for accounting purposes;
- Working accounts established for departmental commercial and service units; and
- Accounts established to facilitate the receipt and disbursement of private funds held by the State in trust.

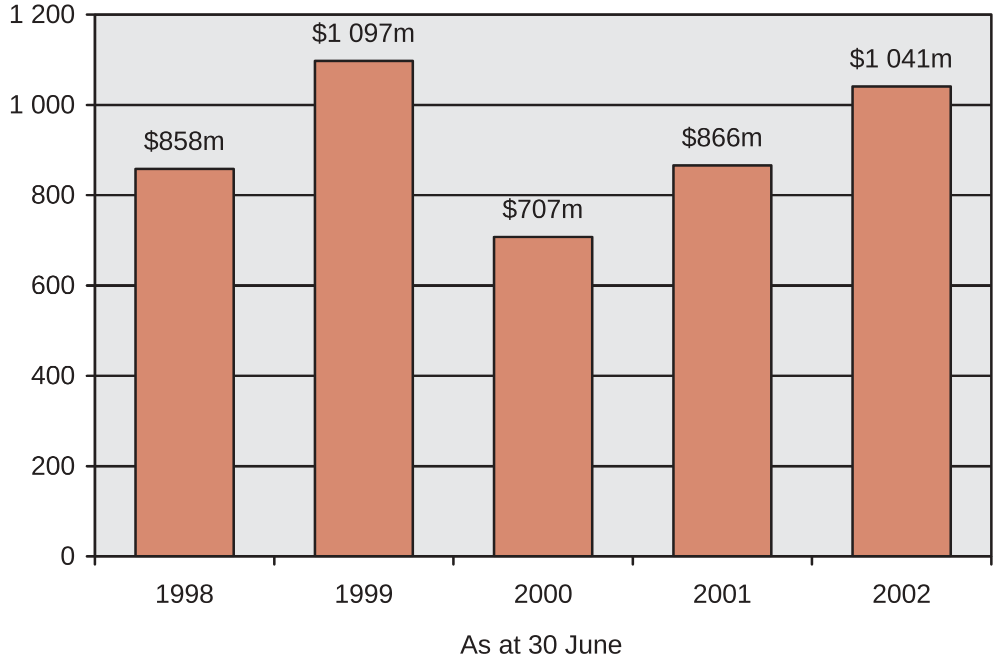
6.2 A number of these trust accounts are established under the authority of specific legislation. The *Financial Management Act* 1994 further provides that the Minister for Finance may establish accounts within the Trust Fund and define the purposes for which they are established. The Minister may also direct the closure of accounts, with any balances not required for the purposes of such accounts to be paid into the Consolidated Fund.

6.3 The financial transactions and balances of Trust Fund accounts are reported within the financial reports of the administering departments. A high level summary of these transactions and balances is also included in the Government's Annual Financial Report.

EXTENT OF TRUST FUND OPERATIONS

6.4 Chart 6A outlines the balances held within the Trust Fund over a 5 year period to 30 June 2002.

TABLE 6A
TRUST FUND BALANCES
($million)



6.5 The chart illustrates that the Trust Fund balance has been subject to considerable movement between financial periods, ranging from $858 million held as at 30 June 1998 to almost $1.1 billion held as at 30 June 1999 and $1 billion held as at 30 June 2002. This movement in balances largely reflects the nature of Trust Fund operations, which are influenced by factors such as changing Commonwealth Government funding arrangements and levels, the impact of transactions (such as asset sales) which may involve the temporary holding of moneys in trust - pending the finalisation of transactions, and any financing requirements associated with temporary funding shortfalls within the Consolidated Fund. For example, the substantial increase in the Trust Fund balance as at 30 June 1999 was mainly due to loan funds paid into the Fund on 30 June 1999 to finance a temporary shortfall in the Consolidated Fund, with this financing repaid the following day on 1 July 1999.

6.6 As at 30 June 2002, $1 billion was held in 77 trust accounts in the Trust Fund, with the majority of this balance ($867 million) relating to accounts established to administer funds which emanate from State sources. An outline of the major account groups comprising this part of the Trust Fund is presented in note 32 of the Government's Annual Financial Report, 2001-02. The remaining balance of the Trust Fund relates to:

- trust accounts established to administer funds received from the Commonwealth Government for specific purposes ($21 million);
- joint Commonwealth/State funds ($106 million), and
- prizes, scholarship and other private donations ($47 million).

6.7 Of the above trust accounts, 30 accounts have been established under the authority of specific legislation and account for $776 million (74.5 per cent) of the Trust Fund balance as at 30 June 2002, with the remaining accounts operating under administrative decisions made over many years by the Minister for Finance under the provisions of the *Financial Management Act* 1994.

6.8 Table 6B provides a summary of the operating activities of the Trust Fund within the Public Account over the 4 year period to 30 June 2002.

TABLE 6B
SUMMARY OF TRUST FUND OPERATING ACTIVITIES
($million)

Item	*1998-99*	*1999-00*	*2000-01*	*2001-02*
Major operating receipts -				
Net transfers from the Consolidated Fund *(a)*	3 441	4 367	5 208	5 622
Grants received	1 342	1 450	1 692	1 855
Sale of goods and services	112	163	136	116
Taxation	86	74	86	90
Interest	35	50	65	60
Other	64	110	190	244
Total operating receipts	**5 080**	**6 214**	**7 377**	**7 987**
Major operating payments -				
Grants paid	4 266	4 601	5 395	6 010
Supplies and consumables	719	1 372	1 729	1 708
Employee-related costs	192	75	80	67
Other	9	4	1	6
Total operating payments	**5 186**	**6 052**	**7 206**	**7 791**
Net operating cash flows	**(106)**	**162**	**171**	**196**

(a) Includes the hypothecation of Consolidated Fund revenues.
Source: Victorian Auditor-General's Office.

6.9 As the table highlights, the vast majority of Trust Fund receipts (around 94 per cent of operating receipts) are sourced from:

- Consolidated Fund appropriations that have been applied by the Treasurer and transferred into trust accounts established to facilitate the disbursement of these funds towards specified purposes, such as grants to hospitals (which are paid from the Hospitals and Charities Fund consistent with legislative requirements), contributions and other payments into departmental working accounts etc.; and
- Specific purpose grants received from the Commonwealth Government for on-passing to external organisations, such as non-government schools and local government bodies, which are required to be paid directly into the Trust Fund.

6.10 The remaining receipts are raised from miscellaneous sources, including interest earned on Trust Fund balances, various fees and charges collected by departmental service units (operating under working account arrangements) from the sale of goods and services - for example, the Information Victoria Bookshop, and certain levies and fees collected under the authority of legislation which are specifically required to be paid into trust accounts and applied towards specific purposes – such as estate agent licensing fees.

6.11 Table 6C outlines the major Trust Fund accounts, which jointly represented approximately 69 per cent of the Trust Fund balance at 30 June 2002.

TABLE 6C
MAJOR TRUST ACCOUNTS, BALANCES AT 30 JUNE 2002

Trust account	*Purpose for which established*	*Amount*
Public Transport Fund	Established under the *Transport Act* 1983 to record amounts received from private sector public transport operators under arrangements entered into between the State and the operators, relating to passenger transport or other transport services, and the disbursement of these amounts in accordance with such arrangements. These amounts mainly relate to fare revenue collections, which under the arrangements are mainly allocated between the individual operators/franchisees.	$155m
Estate Agents Guarantee Fund	Established under the *Estate Agents Act* 1980 to record moneys received mainly from interest earned on real estate agent trust accounts and estate agent licensing fees, and the disbursement of such funds for purposes set out in the Act, which include costs associated with the operation of the Estate Agents Council, compensation claims associated with estate agent misappropriations etc.	$146m
Community Support Fund	Established under the *Gaming Machine Control Act* 1991 to record the receipt (under special appropriations) of certain gambling revenues and the disbursement of these funds in accordance with the requirements of the Act, mainly including the funding of gambling research and various community programs.	$141m
Office of Training and Further Education Managed Funds	Established by the Minister for Finance under the Authority of the FMA to record the receipt and investment of moneys received by the State from the Commonwealth Government pursuant to agreements relating to the provision of tertiary and further training services, and their disbursement in accordance with such agreements to TAFE institutes and registered training organisations.	$99m

TABLE 6C
MAJOR TRUST ACCOUNTS, BALANCES AT 30 JUNE 2002 - *continued*

Trust account	*Purpose for which established*	*Amount*
Better Roads Trust Account	Established under the *Business Franchise (Petroleum Products) Act* 1993 to receive (under special appropriations) certain motor spirit fees and to apply these amounts towards the construction and maintenance of roads.	$99m
Treasury Trust Fund	Established originally under the *Audit Act* 1958, to record the receipt and disbursement of unclaimed and unidentified moneys such as unpresented cheques, surplus cash, unidentified remittances etc. These moneys are retained within the fund for a period of 6 years and, if unclaimed at the end of that period, are required to be paid into the Consolidated Fund. Since the repeal of the former *Audit Act* 1958, this trust fund now operates under the provisions of the *Financial Management Act* 1994.	$77m

Source: Victorian Auditor-General's Office.

TRANSPARENCY AND ACCOUNTABILITY

6.12 Other than trust accounts established under specific legislation, the *Financial Management Act* 1994 assigns discretion to the Minister for Finance for the establishment of trust accounts and the closure of existing accounts, thereby providing the Government with substantial managerial flexibility in the configuration and management of its finances. For example, new accounts may be established and closed within the Trust Fund to account for certain departmental activities previously funded directly through the Consolidated Fund, without informing the Parliament of such a change.

6.13 Within the Government's Annual Financial Report only a high level summary of Trust Fund receipts, payments and balances is annually presented to Parliament. Under the current reporting arrangements, departments are not required to specifically report within their annual financial reports on the operations and balances of individual trust accounts (some of which are governed by specific legislative provisions and involve substantial funds – for example, the Community Support Fund and the Hospitals and Charities Fund), thereby diminishing transparency over their operations.

6.14 **To facilitate adequate transparency and accountability over the activities of the Trust Fund, which has annual aggregate expenditure exceeding $7 billion, we recommend that the current annual reporting requirements at a whole-of-government and departmental level be enhanced to incorporate additional disclosures for trust accounts. Such disclosures could include information about the establishment of new accounts and their purpose, and the closure of existing accounts, together with some greater detail about the transactions and balances of trust accounts.**

SCOPE OF OPERATIONS

6.15 As previously mentioned, the purposes of trust accounts established under specific legislation are defined in such legislation and, in relation to the remaining accounts, their purpose and scope is defined by the Minister for Finance at the time of their establishment.

6.16 Given the wide-ranging changes that have occurred over recent years to the State's appropriation framework, the nature of Trust Fund operations has also changed. That is, while prior to these changes a number of trust accounts were operated to facilitate the carry-forward of appropriations between financial periods for certain "accrued" items such as salaries, wages and creditors, these accounts have now been discontinued and made redundant due to the operation of accrual appropriations.

6.17 However, we observed that a number of trust accounts that were established many years ago under the cash-based appropriation arrangements to facilitate improved accounting and financial flexibility, continue to operate under the new arrangements, for example:

- *Hospitals and Charities Fund* – This Fund is established under the *Health Services Act* 1988 mainly to record the receipt of certain gambling revenues under special appropriation arrangements and certain annual appropriations relating to the provision of health services, and the disbursement of these moneys towards the funding of hospitals and other health services. Around $4 billion is paid annually into this Fund, the vast majority of which is distributed within the same financial year to hospitals and other specified recipients;
- *Conservation, Forests and Lands Plant and Machinery Fund* – This Fund is established under the *Conservation, Forests and Lands Act* 1987 to provide a mechanism for the accumulation of plant and machinery costs (including provision for the replacement of these items) and the allocation of these costs though hire charges to the works on which these items are used. The Fund essentially facilitates cost allocation, and plant and machinery replacement, within the former Department of Natural Resources and Environment. During 2001-02, around $8 million was paid into the Fund, with a similar amount expended in the year; and
- *Conservation, Forests and Lands Stores Suspense Account* – This Account is established under the *Conservation, Forests and Lands Act* 1987 to provide a mechanism for the former Department Natural Resources and Environment to accumulate the cost incurred in relation to stores, fuel, materials, fittings etc. that may be used in future works, and to allocate these items and the associated costs towards works actually undertaken by the Department. Similar to the previous example, the trust account essentially facilitates cost allocation by the Department. During 2001-02, around $22 million was paid into the Account, with expenditure of around $20 million incurred in the year.

6.18 **It is important to note that the purposes served by these, and similar, trust accounts under previous appropriation arrangements may now be adequately managed within the appropriation and departmental accountability framework, without the need to operate separate trust accounts.**

6.19 In relation to the Hospitals and Charities Fund, the major sources of funding are hypothecated for specific purposes and are mainly expended in the year of receipt. Accordingly, one may question what substantive/residual purpose is served by processing these transactions through the Trust Fund, particularly given that output management now provides the mechanism for resource budgeting, management and reporting. In relation to the Conservation, Forests and Lands Plant and Machinery Fund and the Stores Suspense Account, the operation of accrual appropriations now provides the mechanism for asset replacement (through the funding of asset depreciation), and accrual-based accounting by departments now facilitates the full attribution of costs to capital works etc. Again, one may question the residual substantive purpose now served by these trust accounts.

6.20 **The above examples serve to highlight the need for ongoing assessment/review by individual departments, and the Department of Treasury and Finance in its central agency role, of the operations of individual trust accounts, to ensure that they remain relevant and appropriate in the context of any changes in the operating, accounting and accountability environment, including the associated resource management framework.**

Operations of the Treasury Trust Fund

6.21 The Treasury Trust Fund was originally established under the *Audit Act* 1958 to facilitate the recording and accounting for unclaimed and unidentified moneys held by departments. With the repeal of that Act in 1994, the *Financial Management Act* 1994 included provision for the continuation of all existing trust funds and, therefore, now provides the legislative authority for the continuing operation of the Treasury Trust Fund consistent with its previous purpose.

6.22 At 30 June 2002, the Treasury Trust Fund had a balance of $77 million. During 2001-02, the aggregate revenues of the Fund across all departments totalled around $138 million, while its expenditures totalled around $150 million.

6.23 Our examination of the operations of the Treasury Trust Fund identified that, while the initially established purpose for this account had not changed, the scope and nature of the transactions recorded within the account have expanded significantly over the years - beyond what was expressly envisaged when the account was first established. Accordingly, it is questionable whether all of the current operations of the account are consistent with the stated purpose for which the account has been established.

6.24 In practice, this account is now generally used as a "working account" by departments to record transactions such as:

- certain programs/projects delivered across multiple departments - whereby funds from appropriations and other trust accounts are paid to this account for the delivery of specified projects and programs (e.g. the Youth Employment Scheme which was partly delivered by the Department of Infrastructure on behalf of the Department of Victorian Communities);
- certain programs delivered by individual departments (such as the Notebook Computers For Teachers Program and the International Students Program within the Department of Education and Training) - which are funded from a combination of appropriated funds and external (i.e. teacher and student) contributions; and
- events organised by departments (e.g. conferences) – for processing user/attendance fees and other revenues, and the event costs.

6.25 As can be seen from the above examples, certain aspects of the operations of the Treasury Trust Fund (such as accounting for the receipts and payments associated with delivering certain events and programs) are not dissimilar to the types of activities that are typically funded from the Consolidated Fund through annotated appropriation arrangements.

6.26 **Additionally, one might question whether the payment of certain receipts associated with government programs directly in the Treasury Trust Fund (such as teacher contributions relating to the notebook computer program) is consistent with the requirements of section 9(2) of the *Financial Management Act* 1994, which requires that "… *There shall be credited to the Consolidated Fund - all money raised by or on behalf of or received by the State ... and which is not, by or under an Act, required or authorized to be paid to the Trust Fund, or an account in the Trust Fund, or to any other Fund*", and the similar requirements of the *Constitution Act* 1975**.

6.27 Our audit also identified a small number of instances where departmental appropriated funds had been paid into this trust account to facilitate the delivery of certain programs (such as the *Information and Communications Technologies Excellence Fellowship Program* administered by the Department of Education and Training on behalf of the former Department of State and Regional Development), yet remained unexpended and were not paid back into the Consolidated Fund at year-end.

6.28 While such examples did not involve substantial amounts compared with the value of total appropriations issued (an aggregate amount of $806 000 was identified by audit at 30 June 2001 and $4.8 million at 30 June 2002), this practice is considered inappropriate - given that under the current framework, unexpended appropriation funds held within the Trust Fund are required to be paid into the Consolidated Fund.

6.29 Given the restricted purpose for which the Treasury Trust Fund was established, the scope of the activities currently transacted through this account appear to go beyond the statutory purpose of the account. Accordingly, we recommend that the operations of the Treasury Trust Fund be subject to review to determine the full scope of its current activities and the consistency of such activities with the established statutory purpose of the account. Clear guidelines/rules should then be established to govern the future operations of the account.

6.30 We further recommend that any amounts standing to the credit of the Treasury Trust Fund at the end of a financial year, which represent unspent appropriations, should be transferred back to the originating department and repaid to the Consolidated Fund.

***RESPONSE** provided by Secretary, Department of Treasury and Finance*

> *The Department notes that it is some time since departmental trust accounts were reviewed. It may be timely to request departments to undertake a systematic review of all their current trust accounts and justify why they need to continue to exist on a case-by-case-basis.*

Appendix A

Other appropriation frameworks

APPROPRIATION FRAMEWORKS OF A NUMBER OF AUSTRALIAN AND OVERSEAS JURISDICTIONS – AN OVERVIEW *(a)*

	Victoria	*New South Wales*	*Queensland*	*South Australia*	*Commonwealth of Australia*	*New Zealand*	*United Kingdom*
Basis of Appropriations	Global accrual output-based departmental appropriations for output provision, additions to net assets, and payments on behalf of State.	Global cash input-based departmental appropriations, for recurrent and capital purposes. The State is currently working towards the introduction of output appropriations.	Global accrual output-based departmental appropriations, for controlled outputs, controlled equity adjustments, and administered items.	Global accrual output-based departmental appropriations, for the purchase of outputs, equity contributions, and appropriated borrowings.	Accrual-based output/outcome appropriations to departments and public sector agencies. All appropriations are global and made for outputs, equity injections, and loans. Administered appropriations for expenses are outcome-based, while one global appropriation is provided for administered capital purposes for each department and public sector agency.	Accrual output-based departmental appropriations for individual output classes, capital contributions, non-departmental operating costs, and loan and interest costs.	Global input-based departmental appropriations, with appropriations referenced to the key departmental aims and parliamentary authority provided on both an accruals and net-cash basis.
Authority to apply appropriations vested in:	The Treasurer	Portfolio Ministers	The Treasurer	The Treasurer - total appropriation limits applied at commencement of financial year.	The Finance Minister (however, the authority is generally delegated to Ministers or departmental senior officials)	Vote Ministers	Departments

APPROPRIATION FRAMEWORKS OF A NUMBER OF AUSTRALIAN AND OVERSEAS JURISDICTIONS – AN OVERVIEW - *continued*

	Victoria	*New South Wales*	*Queensland*	*South Australia*	*Commonwealth of Australia*	*New Zealand*	*United Kingdom*
Treasurer's Advance	✓ Specific "urgent claims" allocation included in the Annual Appropriation Act.	✓ Specific allocation for recurrent and capital purposes included in the Annual Appropriation Act.	✓ The Treasury Department's appropriations include provision for a "Treasurer's Advance" which may be paid to line departments where their appropriations are insufficient.	✓ Specific contingency allocation included in the Annual Appropriation Act. In addition, a "Governor's appropriation fund" provides a further allocation of up to 3 per cent of total annual appropriations for unforeseen events.	✓ Specific allocation to the Finance Minister for application under specified conditions, mainly relating to urgent and unforeseen need, and erroneous omission or understatement of other appropriations.	✗ Supplementary appropriations generally provide the means to fund unexpected/new expenditures.	✗ Supplementary appropriations generally provide the means to fund unexpected/new expenditures.
Other (temporary) advances (to meet urgent claims)	✓ Authority limit capped at 0.5 per cent of total annual appropriations - for "urgent claims".	✓ Authority limit not capped for "exigencies" of government, but requires approval by the Governor on the Treasurer's recommendation.	✓ Authority limit not capped for "unforeseen expenditure" incurred, but requires approval by the Governor-in-Council on the Treasurer's recommendation.	✗ No other advances.	✗ No other advances.	✓ For other than capital appropriations, the authority limit is capped at one per cent of each vote appropriation, and is uncapped in respect of emergency expenditure.	✓ Contingency Fund capped at 2 per cent of prior year cash appropriation.

APPROPRIATION FRAMEWORKS OF A NUMBER OF AUSTRALIAN AND OVERSEAS JURISDICTIONS – AN OVERVIEW - *continued*

	Victoria	*New South Wales*	*Queensland*	*South Australia*	*Commonwealth of Australia*	*New Zealand*	*United Kingdom*
Appropriation transfers	✓ Only within the same department.	✓ Only between departments	✓ Within the same department, and between departments in certain circumstances.	✓ Within the same department, and between departments.	✗ Not permitted.	✓ Only within the same vote - limited to 5 per cent of each output class.	✗ Not permitted.
Receipt annotation/retention	✓ Receipt annotation, with legislative authority limit uncapped.	✓ Receipt retention, with legislative authority limit uncapped.	✓ Receipt retention, with legislative authority limit uncapped.	✓ Receipt retention, with legislative authority limit uncapped.	✓ Receipt retention, with legislative authority limit uncapped.	✓ Receipt retention, with authority limit capped in legislation.	✓ Receipt annotation, with authority limit capped by Appropriation Act.
Carry-forward of unused appropriations	✓ Subject to Treasurer approval.	✗ Not permitted.	✓ Only available for 2 weeks post year-end.	✗ Not necessary, given that the total parliamentary appropriation limits are applied each year.	✓ Departmental appropriations remain available to the Government over future years until applied. Annual administered appropriations which are unapplied at year-end, may be carried-forward to future years unless the Minister for Finance reduces the amount that can be carried forward.	✗ Not permitted.	✗ Not permitted.

APPROPRIATION FRAMEWORKS OF A NUMBER OF AUSTRALIAN AND OVERSEAS JURISDICTIONS – AN OVERVIEW - *continued*

	Victoria	*New South Wales*	*Queensland*	*South Australia*	*Commonwealth of Australia*	*New Zealand*	*United Kingdom*
Borrowing against future year appropriations	✓ The Treasurer, with the approval of the Governor-in-Council, may approve additional expenditure which accrues benefits for future years, with the authority limit capped at 3 per cent of the relevant department's annual appropriation.	✗ Not permitted.	✗ Not permitted.	✗ Not permitted.	✗ Not permitted.	✗ Not permitted.	✗ Not permitted.

APPROPRIATION FRAMEWORKS OF A NUMBER OF AUSTRALIAN AND OVERSEAS JURISDICTIONS – AN OVERVIEW - *continued*

	Victoria	*New South Wales*	*Queensland*	*South Australia*	*Commonwealth of Australia*	*New Zealand*	*United Kingdom*
Other provisions facilitating increased parliamentary appropriation authority and management flexibility	✓ Relate to increased salary and associated costs resulting from industrial awards or determinations, <u>and</u> additional expenditure associated with Commonwealth grants received post-budget. Furthermore, unspent accrual appropriations are available for departmental working capital purposes, <u>and</u> departmental surpluses may be expended without the need for further parliamentary sanction.	✓ Relate to additional expenditure associated with Commonwealth grants received post-budget.	✓ Unspent accrual appropriations that have been previously applied are available for departmental working capital purposes, <u>and</u> departmental "controlled" surpluses may be expended by departments without the need for further parliamentary sanction.	✓ The total appropriation authority/limit is applied and provided to departments each year, with any unspent amount available for departmental purposes in the following financial year without the need for further parliamentary sanction.	✓ Unspent departmental appropriations remain available for departmental purposes, and may be expended by departments without the need for further parliamentary sanction.	✓ Unspent accrual appropriations are available for departmental working capital purposes. Departmental surpluses are required to be repaid to the Crown, except as otherwise agreed between the vote Minister and the Minister for Finance.	✗ Additional expenditure authority can only be obtained from supplementary parliamentary appropriations, sought during the course of each year. Unspent appropriations of both cash and accruals lapse at the end of each year. Working capital is part of cash appropriation, but constrained by a 'no payment in advance of need' Treasury rule.

(a) Represents the frameworks in operation at the various jurisdictions as at 30 June 2002.

✓ Represents availability of the relevant feature within the jurisdiction.

✗ Represents non-availability of the relevant feature within the jurisdiction

AN EXAMPLE

THE UNITED KINGDOM (UK) APPROPRIATION FRAMEWORK

Similar to other Westminster-based jurisdictions, the UK appropriation framework has traditionally been cash-based, with Parliament annually authorising only the cash to be spent by the Government/departments in the respective years. However, as part of recent wide-ranging reforms of resource accounting and management in this jurisdiction, as from 2001-02 the appropriation framework has been reformed to facilitate improved parliamentary control and transparency over government operations and spending.

THE UK MODEL - A SNAPSHOT

Global input-based departmental appropriations.

Appropriation limits set by Parliament on both accrual and cash basis.

Supplementary appropriations by Parliament provide the key budget flexibility mechanism.

Receipt retention/annotated appropriation arrangements are used, but their coverage and monetary limits are explicitly set in the annual Appropriation Act.

Application of temporary advances (the Contingency Fund) towards urgent claims is subject to strong conventions.

Overall, strong focus on parliamentary spending control.

Basis of appropriation

Under the new resource accounting regime in UK, parliamentary appropriations establish spending limits for the Government on 2 basis, namely:

- the consumption of resources (i.e. the accrual cost of service delivery); and
- the net cash requirement (i.e. the cash required to be drawn from the Consolidated Fund to meet the service delivery, including recurrent and capital costs).

As a result, the Government is required to observe both accrual-based and cash-based spending limits established by Parliament under the annual Appropriation Acts. As a corollary, the accrual costs of prior year service delivery which need to be funded in the current period are considered and voted by Parliament in the year that they emerge, therefore providing strong parliamentary control over both costs incurred and paid in any one year.

The appropriations to departments are generally "one line" global allocations, referenced to the key aims of the respective departments. Departments progressively apply the available appropriations towards their costs, and are administratively responsible for meeting performance targets established under service agreements between the Chancellor of the Exchequer (the Treasurer), and the relevant portfolio Minister and the Department.

Budget management and flexibility

The global appropriations arrangements, under which high level accrual and cash-based appropriations are provided to each department, provides flexibility to the Government/departments to respond to emerging cost pressures in the course of a year - through the administrative re-allocation of activity/output funding within the legislated global spending limits. Nevertheless, this is subject to constraints.

Although Parliament does not explicitly (by legislation) define the underlying Budget detail, there is an expectation that actual spending will generally conform with the underlying detail in the Budget Papers. If significant shifts are required during the course of the year, the Government needs to seek parliamentary approval through Supplementary Estimates. If after the year-end some budget lines prove to be overspent but there are offsetting savings elsewhere, Departments are required to seek Treasury approval for such offsets (called "virement"). This approval is seldom withheld, but Treasury may do so if it considers it necessary, forcing the respective department to seek an "Excess Vote" and thereby drawing such over-spending to Parliament's attention.

Reflecting a strong parliamentary control culture/environment, supplementary appropriations represent the key budget flexibility mechanism available to government (beyond the flexibility available through global appropriations) to meet further funding demands/needs. Such appropriations are routinely sought and approved by the Parliament at 3 times during the year (and exceptionally at other times), consistent with the principle that additional spending should be sanctioned by Parliament prior to its incurrence.

Revenue retention arrangements are also in place, under which departments are able to retain and spend revenues collected. However, the Parliament through the annual Appropriation Act, sets monetary limits for each of these annotated appropriations (which are called Appropriations in Aid). Descriptions of the revenue categories that qualify for such annotation arrangements are footnoted in the Appropriation Acts. These arrangements jointly establish clear boundaries for the operation of these arrangements and the available limits of parliamentary authority.

The established legislative arrangements do not include other budget management mechanisms, such as Treasurer's Advances, transfer provisions etc. However, where it is not practicable to first seek and obtain supplementary appropriation, a Contingency Fund (representing a temporary advance equivalent to 2 per cent of prior year's appropriation) is available to the Government to meet any urgent claims/needs that arise during the course of the year.

The availability of the Contingency Fund is administered by the Treasury, with any funds accessed by departments during a year required to be appropriated by Parliament in a subsequent Appropriation Act. The availability of this Fund is also subject to strong established conventions under which the Fund is not to finance new government services – defined as services which Parliament has not authorised either specifically by way of enabling legislation or, in cases where it is legitimate to base expenditure on the sole authority of the Appropriation Act, through the Estimates processes. It is generally considered that specific legislative authority should be available for the establishment of new services (or a Bill which is at least at the second reading speech stage) prior to public funds being made available towards their delivery.

The Contingencies Fund operates only in relation to cash requirements. There is no comparable "emergency approval" mechanism for additional resource requirements that do not also require cash (e.g. additional stock consumption). Such additional requirements are dealt with solely by Supplementary Appropriations in the course of the year, or if too late to do so after year-end, by an "Excess Vote".

There is a further, more general, parliamentary convention regarding the overall scope of the appropriation process. Although the annual Appropriation Act of itself is sufficient statutory authority for the expenditures it approves, there is a convention that, with a few exceptions, expenditure of a continuing nature must have "underlying" enabling legislation.

Appendix B

Glossary of terms

GLOSSARY OF TERMS

Accountability	The process by which individuals or organisations report on what actions they have taken in the context of given delegations and legislation, and accept responsibility for those actions and their foreseeable consequences.
Accrual accounting	An accounting method under which revenue, expenses, assets and liabilities are recognised when transactions occur, irrespective of the timing of the related cash flow. For example, expenses are recorded when goods or services are provided, rather then when payments are made.
Accrual-based appropriations	Arrangements under which, once appropriations are applied by the Treasurer (refer to "application of appropriations"), the cash can be drawn from the Consolidated Fund at any future time.
Accrual output-based management	A resource management model focused on the funding, reporting and monitoring of defined outputs, with linkages to government strategic priorities and outcomes. Under this model, the Government (as purchaser), decides which outputs it will purchase from departments (the providers) at specified levels of quantity, quality and price. As owner, the Government also decides the investment required in departments in order to enable them to maintain or build their capacity to meet output targets/expectations.
Advance to Treasurer	A specific appropriation to the Treasurer, included in the annual Appropriation Act, to meet urgent expenditure claims that were unforeseen at the time of the budget. Amounts applied under this authority are reported to Parliament at a later date and approved by Parliament in a subsequent Appropriation Act.
Annotated receipts	Under the provisions of the *Financial Management Act* 1994 and the annual Appropriation Act, the authority limit for certain departmental appropriation items can be increased by an amount equal to specified departmental receipts under the terms and conditions agreed between the responsible Minister and the Treasurer. These receipts are known as annotated receipts.
Annual Appropriation	The appropriation of moneys standing to the credit of the Consolidated Fund for various purposes contained in the annual Appropriation Act and the Appropriation (Parliament) Act.
Application (of appropriations)	The formal act of drawing-down/utilising available appropriation authority by the Treasurer, representing the point at which appropriation revenue is made available to/controlled by departments.
Appropriation	An authority given by the Parliament to make payments from the Consolidated Fund for the purposes stated, and up to the limit of the amount specified in the particular Act.
Appropriation items	The specific purposes and amounts (limits) appropriated by Parliament via the Appropriation Acts (i.e. the individual appropriation line items).
Budget Sector	Refer to the definition of the General Government Sector.
Consolidated Fund	The Government's primary account that receives all Consolidated Revenue under the *Constitution Act* 1975 and from which amounts are appropriated by Parliament for specific purposes. The Consolidated Fund, together with the Trust Fund, form the Public Account.

GLOSSARY OF TERMS *- continued*

Depreciation	The allocation of the cost of an asset over the years of its useful life.
GAAP	Generally accepted accounting principles (GAAP), embodying the requirements of accounting standards and other professional pronouncements.
General Government Sector	The part of the public sector that provides public services (outputs) which are mainly non-market in nature, for the collective consumption of the community, and which involve the transfer or redistribution of income and are financed mainly through taxes and other compulsory levies. Government departments are the major agencies within this sector. The definitions of the General Government Sector and the Budget Sector are identical in Victoria.
Government Finance Statistics (GFS)	A framework implemented by the Australian Bureau of Statistics (ABS) for the presentation of public sector financial statements. While these statements are based on accrual accounting principles, there are substantial underlying differences in concepts and disclosures between their presentation and the presentation of statements prepared using generally accepted accounting principles (GAAP).
Global Appropriations	Refers to high level/aggregated appropriations provided to departments for application towards generic purposes (such as the provision of outputs etc.), which provide substantial management flexibility to the Government and departments.
Net Appropriations	Base parliamentary appropriations, the authority limit of which is increased/decreased through the operation of other provisions contained in the *Financial Management Act* 1994 and the annual Appropriation Act - such as annotated receipts, the carry-forward of previously unused appropriations, etc.
Outcomes (Government)	The Government's desired or intended effects on the community as a result of its activities and other external factors.
Outputs	Products or services produced or delivered by departments/agencies.
Output Groups	For the purposes of budgeting and reporting, a grouping of individual outputs that contribute to a common outcome.
Performance indicators (of departmental objectives)	Measures that demonstrate achievement or progress towards achievement of entity objectives.
Performance measures	Quantity, quality, timeliness and cost measures used to describe how many, how well, when and how frequently outputs are delivered.
Performance targets	Intended output delivery levels expressed in terms of each of the performance measures.
Responsible Minister/s	One or more portfolio Minister/s that have specific and/or collective responsibility over a department's activities and performance.
Revenue certification	The formal acceptance by the Minister for Finance of departmental claims for appropriation revenue, based upon the provision of agreed outputs in terms of quantity, quality, timeliness and cost.
State Administrative Unit (SAU)	An account established within the Consolidated Fund to meet the accounting and accountability needs associated with the operation of the accrual-based output management arrangements. These include the recording of the Treasurer's application of appropriations and the departmental draw-down of these funds from the Consolidated Fund.

GLOSSARY OF TERMS *- continued*

Special Appropriation	A standing authority that remains in force until amended or repealed by Parliament, for specific once-off or ongoing payments.
Trust Fund	That part of the Public Account established to account for the receipt and disbursement of moneys not forming part of the Consolidated Fund and therefore not subject to parliamentary appropriation. The Trust Fund comprises various trust specific purpose accounts established under separate legislation or at the discretion of the Minister for Finance under the authority of the *Financial Management Act* 1994.
Warrant	A written authority provided under the *Constitution Act* 1975 and the *Financial Management Act* 1994 to spend specified sums from the Consolidated Fund during a financial year, which must be signed by the Treasurer, the Auditor-General and the Governor.

AUDITOR GENERAL
VICTORIA

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