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Performance Audit

Management of Net Appropriation Agreements

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Australian National
Audit Office

Canberra ACT
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Dear Mr President
Dear Mr Speaker

The Australian National Audit Office has undertaken a performance audit in across agencies in accordance with the authority contained in the *Auditor-General Act 1997*. Pursuant to Senate Standing Order 166 relating to the presentation of documents when the Senate is not sitting, I present the report of this audit and the accompanying brochure. The report is titled *Management of Net Appropriation Agreements.*

Following its presentation and receipt, the report will be placed on the Australian National Audit Office's Homepage—http://www.anao.gov.au.

Yours sincerely

Ian McPhee
Auditor-General

The Honourable the President of the Senate
The Honourable the Speaker of the House of Representatives
Parliament House
Canberra ACT

AUDITING FOR AUSTRALIA

The Auditor-General is head of the Australian National Audit Office. The ANAO assists the Auditor-General to carry out his duties under the *Auditor-General Act 1997* to undertake performance audits and financial statement audits of Commonwealth public sector bodies and to provide independent reports and advice for the Parliament, the Government and the community. The aim is to improve Commonwealth public sector administration and accountability.

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Abbreviations

ABS	Australian Bureau of Statistics
ABIS	Agency Banking Incentive Scheme
ACIAR	Australian Centre for International Agricultural Research
AFP	Australian Federal Police
ACM	Appropriation and Cash Management module
AFDA	Administrative Functions Disposal Authority
AGD	Attorney-General's Department
AGS	Australian Government Solicitor
ANAO	Australian National Audit Office
Archives Act	*Archives Act 1983*
ARPANSA	Australian Radiation Protection and Nuclear Safety Authority
ATO	Australian Taxation Office
Audit Act	*Audit Act 1901*
Auditor-General Act	*Auditor-General Act 1997*
AusAID	Australian Agency for International Development
BEFR	Budget Estimates and Framework Review
BA	Biosecurity Australia
BoM	Bureau of Meteorology
CAC Act	*Commonwealth Authorities and Companies Act 1997*
CAMM	Cash and Appropriations Management Module
CFO	Chief Financial Officer
CRF	Consolidated Revenue Fund
CRS	CRS Australia
DAFF	Department of Agriculture, Fisheries and Forestry
DCITA	Department of Communication, Information Technology and the Arts
DEH	Department of the Environment and Heritage

DEST	Department of Education, Science and Training
DFAT	Department of Foreign Affairs and Trade
Defence	Department of Defence
DIMIA	Department of Immigration and Multicultural and Indigenous Affairs
DITR	Department of Industry, Tourism and Resources
DoS	Department of the Senate
DPRS	Department of the Parliamentary Reporting Staff
FaCS	Department of Family and Community Services
Finance	Department of Finance and Administration
FMA Act	*Financial Management and Accountability Act 1997*
FMO	Finance Minister's Orders
FRLI	Federal Register of Legislative Instruments
GDA	General Disposal Authority
GST	Goods and Services Tax
Health	Department of Health and Ageing
IGT	Inspector-General of Taxation
LI Act	*Legislative Instruments Act 2003*
LI Regulations	*Legislative Instruments Regulations 2004*
NBA	National Blood Authority
NOO	National Oceans Office
OASITO	Office of Asset Sales and IT Outsourcing
OLDP	Office of Legislative Drafting and Publishing
OPA	Official Public Account
ORER	Office of the Renewable Energy Regulator
PAES	Portfolio Additional Estimates Statement
PBS	Portfolio Budget Statement
PM&C	Department of the Prime Minister and Cabinet
Treasury	Department of the Treasury

Glossary

Administered item	Items that the entity does not control. Rather, they are controlled by the Government and administered by agencies on behalf of Government.
Cancellation Instrument	*Financial Management and Accountability Net Appropriation Agreement Cancellation 2005*, an instrument made by the Finance Secretary on 24 June 2005 to cancel, as at 30 June 2005, all Section 31 agreements commencing on or before 30 June 2004.
Chief Executive	The person with the special responsibilities set out in Section 44 of the *Financial Management and Accountability Act 1997*, as defined by Section 5 of that Act.
Departmental item	Assets, liabilities, revenues and expenses controlled by agencies and used in producing their outputs.
Section 31 agreement	Agreements made under Section 31 of the *Financial Management and Accountability Act 1997*, for the purposes of items in Appropriation Acts that are marked "net appropriation".
Section 35 agreement	Net appropriation agreements made in accordance with the provisions of the annual Appropriation Acts for the purposes of Section 35 of the *Audit Act 1901*, which deemed certain amounts to be appropriated.
Variation Instrument	*Financial Management and Accountability Net Appropriation Agreement Variation 2005*, an instrument made by the Finance Secretary on 24 June 2005 to regularise receipts collected by agencies in periods covered by an ineffective Section 31 agreement or agreements.
Variation Instruments 2 & 3	*Financial Management and Accountability Net Appropriation Agreement Variation (No.2) 2005* and *Financial Management and Accountability Net Appropriation Agreement (Department of the Environment and Heritage) Variation 2005*, instruments made by the Finance Secretary on 28 October 2005 to regularise receipts collected by agencies in periods not covered by a Section 31 agreement.

Summary and Recommendations

Summary

Background

1. An appropriation is an authorisation by the Parliament to spend an amount from the Consolidated Revenue Fund (CRF) for a particular purpose. Section 83 of the Constitution provides that no money shall be drawn from the Treasury of the Commonwealth[1] except under an appropriation made by law.

2. In this context, net appropriation arrangements are a longstanding feature of the Commonwealth's financial framework. They provide a means by which an agency's appropriation item in the annual Appropriation Acts can be increased by amounts received from non-appropriation sources. This provides the agency with the appropriation authority to retain and spend those amounts.

3. During the course of the 1990s, the use of net appropriation arrangements became more widespread amongst agencies, in part reflecting public sector management reforms introduced at the time. This particularly related to an increasing focus on user charging and cost-recovery by agencies for some services, as a means of improving resource allocation and reducing the call on Budget funding for agency running costs.

4. Under the Commonwealth's current financial framework, Section 31 of the *Financial Management and Accountability Act 1997* (FMA Act) allows the Finance Minister to enter into net appropriation agreements (known as Section 31 agreements) for the purposes of appropriation items in Appropriation Acts that are marked "net appropriation". The FMA Act requires that an agreement be made with the Minister responsible for the appropriation item or, in the case of items for which the Finance Minister is responsible, with the Chief Executive of the agency for which the appropriation is made.

5. A Section 31 agreement specifies the types of departmental and/or administered receipts that will be eligible to be retained by the relevant agency, and the terms on which the relevant appropriation item will be increased for those receipts by operation of the agreement. For example, the agreement may require certain receipts to be shared with the Budget in nominated proportions. The annual Appropriation Acts provide that, if a Section 31 agreement applies to an appropriation item, the amount specified in the item is taken to be increased in accordance with the agreement, on the conditions set out in the agreement. The increase cannot be more than the relevant receipts covered by the agreement.

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[1] In this context, the Treasury of the Commonwealth refers to the CRF.

6. In this respect, the relevant provisions of the annual Appropriation Acts and FMA Act provide the Executive Government with the authority to increase the appropriations set out in the Schedules to the Appropriation Acts, providing certain specified steps are undertaken. The terms of Section 31 of the FMA Act must be complied with in order for an agency to obtain the authority to retain and spend amounts received from non-appropriation sources.

7. There has continued to be growth in the use of net appropriations since the commencement of the FMA Act. In 1996–97, the last full financial year prior to the Act commencing, agencies reported net appropriation receipts totalling $831 million. In 2003–04, 68 FMA Act agencies collectively reported receipts totalling $1.55 billion as having been added to their respective annual appropriations by operation of Section 31 agreements. In 2004–05, 67 agencies reported Section 31 receipts totalling $1.46 billion.[2]

Roles and responsibilities

8. In accordance with the framework created by the FMA Act, agencies are responsible for the control, management and reporting of their finances, including appropriations.

9. Quite specific obligations in relation to keeping proper accounts and records are placed on agency Chief Executives by the FMA Act and the Finance Minister's Orders (FMOs). These include an obligation to keep the records of the agency in a manner that, among other things, ensures that moneys are only expended for the purpose for which they were appropriated, and the limit (if any) on appropriations is not exceeded.

10. Agencies are expected to disclose estimated non-appropriation receipts as part of the Budget process. The actual Section 31 receipts added to an agency's annual appropriations are required to be disclosed in the agency's annual financial statements.

11. The responsibilities of the Department of Finance and Administration (Finance) relate to the maintenance of the financial framework established by the FMA Act, FMA Regulations and FMOs, and the provision of guidance on the operation of that framework.

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[2] The $99 million reduction in Section 31 receipts reported in 2004–05 compared to 2003–04 is consistent with increased actual Section 31 receipts, combined with corrections made by agencies in 2004–05, in response to issues raised in this performance audit, to exclude amounts previously incorrectly disclosed as Section 31 receipts. See Chapter 1 (footnote 40) and Chapter 4 (paragraphs 4.45 to 4.54) for more detail regarding those issues. In December 2005, Finance advised ANAO that overall departmental appropriations have also increased over the period and Section 31 appropriations have reduced as a proportion. Finance noted that, in 1996–97, Section 31 receipts comprised 6.1 per cent of agencies' departmental (running costs) appropriations, and that, by 2004–05, Section 31 receipts comprised only 4.4 per cent of agencies' departmental appropriations.

12. In its most recent Annual Report, Finance noted that a number of audit reports have identified scope for improvements in the financial framework, predominantly in agencies' application of the framework.[3] In this context, during the first seven months of 2004, as part of its rolling review of various aspects of the financial framework, Finance undertook an examination of Section 31 of the FMA Act. The examination reflected emerging concerns within the Department about the form of Section 31 agreements, and agencies' application of the agreements.[4] The culmination of this work was the issuing, on 11 August 2004, of Finance Circular No. 2004/09, *Net appropriation agreements (Section 31 Agreements)*.

13. The Finance Circular included a revised template for the preparation of Section 31 agreements. Associated with the Circular, Finance required all agencies to make a new agreement. By 30 June 2005, all agencies had executed a revised agreement using the new template.

14. The template was further revised on 30 June 2005, when Finance Circular No. 2004/09 was replaced by Finance Circular No. 2005/07, *Net appropriation agreements (Section 31 Agreements)*. Issued in response to matters raised during the course of this performance audit, the most recent Circular included enhanced guidance to agencies on the execution of Section 31 agreements.

Audit objective

15. The objective of this performance audit was to assess agencies' financial management of, and accountability for, the use of net appropriation agreements to increase available appropriations.

Overall audit conclusions

16. Overall, this audit has revealed quite widespread shortcomings in the administration of net appropriation arrangements. In particular, there has been inadequate attention by a number of agencies to their responsibility to have in place demonstrably effective Section 31 arrangements that support additions made to annual appropriations and the subsequent expenditure of those amounts. Given the fundamental importance of appropriations to Parliamentary control over expenditure, improvements are necessary to secure proper management of net appropriation arrangements. The two recent Finance Circulars should assist in this regard, as will changes to Finance's practices in negotiating and executing agreements on behalf of the Finance

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3 Department of Finance and Administration, *2004–05 Annual Report*, October 2005, pp. 22 and 34.

4 ibid.

Minister. Nevertheless, in terms of appropriation management, individual agencies are directly responsible for ensuring that an appropriation is available before spending funds from the CRF.

17. Accountability to the Parliament for the use of Section 31 arrangements to increase the annual appropriations provided through the annual Appropriation Acts is expected to occur through disclosure of estimated receipts in budget papers and actual receipts in agency financial statements. However, the current presentation of budget estimates does not assist in providing users of agency Portfolio Budget Statements (PBS) with a clear understanding of the extent to which the relevant agency expects to increase its annual appropriation for amounts collected under authority of its Section 31 agreement.[5] Further, the Australian National Audit Office (ANAO) found that agency financial statements have not accurately reflected the use of Section 31 arrangements.

18. While many of the issues raised by this audit are quite technical (in a legal sense), there are important considerations of appropriate accountability, including transparency, to the Parliament. In this respect, the Joint Committee of Public Accounts and Audit, in examining previous audit reports on aspects of the financial management framework, has emphasised the importance of managers understanding their responsibilities under the FMA Act. The Committee has also put on notice its intention to continue to investigate agency understanding of, and adherence to, the requirements of the financial framework.[6]

19. The measure being implemented by Finance to require agency Chief Executives to provide an annual statement of compliance with the legislative and policy elements of the financial management framework, with effect from 2005–06, should assist in ensuring a stronger agency focus on compliance issues of this kind, which are important from both a government and Parliamentary perspective.

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5 The Portfolio Budget Statements are targeted towards providing the Parliament with information regarding the proposed allocation of resources to Government outcomes. Information is provided to Parliament regarding 'Other receipts available to be used', which is the estimated amount of receipts that are available to the agency for expenditure to contribute to the relevant outcome.

6 Report 404, *Review of Auditor-General's Reports 2003–04 Third & Fourth Quarters; and First and Second Quarters of 2004–05*, Joint Committee of Public Accounts and Audit, October 2005, p. 191.

Key Findings

Establishing effective Section 31 arrangements (Chapters 2 and 3)

20. Significant Constitutional consequences result from the operation of Section 31 agreements. Specifically, an effectively executed agreement provides an agency with an appropriation authority to spend the receipts to which it applies. It is in this context that the issue of who can execute an agreement, and in what capacity, must be considered.

21. In order to comply with the provisions of the FMA Act, a net appropriation agreement must be made between the Finance Minister (as the whole-of-government representative) and the Minister responsible for the relevant agency or, for most Finance portfolio agencies, the agency Chief Executive. Accordingly, there are two signatories to a Section 31 agreement. Both signatories must have the necessary authority in order for an agreement to be effectively executed in accordance with the legislative requirements.

22. In almost all instances, a Finance official has signed the whole-of-government side of Section 31 agreements, as delegate of the Finance Minister. Finance officials must hold a written delegation from the Finance Minister in order to enter into these agreements.[7]

23. Similarly, the significant majority of agreements made to 30 June 2005 were signed by an official of the relevant agency, rather than the responsible Minister or, for Finance portfolio agencies, Chief Executive. Chief Executives of Finance portfolio agencies have an express power to delegate to agency officials, by written instrument, their power under subsection 31(2) of the FMA Act to make net appropriation agreements with the Finance Minister.[8] The Treasurer and Attorney-General are also able to delegate their power under that subsection, as the responsible Minister.[9]

24. However, other Ministers are not able to delegate their power to enter into Section 31 agreements with the Finance Minister. Nor is there any express power for Ministers to authorise a person to exercise that power for and on the

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7 In accordance with the requirements of Sections 62 and 53 of the FMA Act.

8 This power is provided by Section 53 of the FMA Act.

9 Section 62A of the FMA Act provides the Treasurer with an express power to delegate, by written instrument, his or her powers under the FMA Act. The *Law Officers Act 1964* provides the Attorney-General with an express power to delegate, in writing, his powers under all or any of the laws of the Commonwealth or a Territory to the Secretary to the Attorney-General's Department or to the person for the time being holding or performing the duties of the office specified in the instrument of delegation. AGS has advised that other Ministers administering the same relevant legislation as the Treasurer and Attorney-General also have a power of delegation.

Minister's behalf, or the required form any such authorisation should take. Relying on the *Carltona* principle[10], the Australian Government Solicitor (AGS) has advised agencies that, on balance, a Minister has an implied power to authorise officials to enter into Section 31 agreements for and on behalf of the Minister.

25. Where the *Carltona* principle applies in relation to a particular function or power, an important qualification to its operation is that the Minister's surrogate must be appropriately qualified to act on the Minister's behalf. Authority to so act may arise through an express authorisation from the Minister, or impliedly from the nature of the power or function. Based on legal advice, Chief Executives[11] in agencies for which the Finance Minister is not responsible are considered to have an implied authority to enter into Section 31 agreements on their Minister's behalf. This is based upon the Chief Executive's responsibilities, under the FMA Act, for the financial management of the agency.[12]

26. Legal advice provided to both Finance and ANAO in June and July 2005 respectively was that officials who are not agency Chief Executives are not impliedly authorised to enter into Section 31 agreements on the Minister's behalf. Consequently, such officials require an express authorisation from the relevant Minister in order to be empowered to sign a Section 31 agreement.[13] AGS has advised that the Minister may give such an express authorisation either in writing or orally.

27. Legal advice provided to Finance by AGS in June 2005 was that the question as to whether a written or oral express authorisation existed at the time the official signed the agreement is one of fact. However, AGS further advised that the 'presumption of regularity' principle may apply in certain circumstances where an agency is not able to verify that an official had been expressly authorised by the Minister.

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[10] That principle, established in *Carltona Ltd v Commissioners of Works* [1943 2 ALL ER 560], applies, in certain circumstances, to infer to a Minister a power to authorise officials to exercise, on the Minister's behalf, a power vested in the Minister, despite the absence of an express power to delegate or authorise.

[11] Being the person with the special responsibilities set out in Section 44 of the FMA Act, as defined in Section 5 of the Act.

[12] Section 44 of the FMA Act requires a Chief Executive to manage the affairs of the agency in a way that promotes efficient, effective and ethical use of the Commonwealth resources for which the Chief Executive is responsible.

[13] The Treasurer and Attorney-General may elect to exercise their express power of delegation, or their implied power to authorise. In both cases, this must be expressly done in order to empower an official below the level of Chief Executive to sign Section 31 agreements.

28. AGS advised that:

> In this respect, it may be that an agreement signed by an official other than the Chief Executive is presumptively valid in circumstances where:
>
> - the officer signed the agreement 'for and on behalf of the Minister' or in some other way which indicated that the officer understood himself or herself to be acting under an authorisation from the Minister; and
> - there is no evidence to support the view that the officer was not expressly authorised to enter into Section 31 agreements on behalf of the Minister.

Summary of assessment outcomes

29. ANAO examined 231 Section 31 agreements made between the commencement of the FMA Act on 1 January 1998 and 30 June 2005. Agreements were assessed in order to form a conclusion as to whether they had been effectively executed by both signatories. The assessment process was based on the evidence provided by agencies and Finance substantiating the authority of their respective signatories. The assessment was conducted using a decision tree that reflected a series of legal advices provided to Finance and ANAO by AGS regarding assessing the effectiveness of Section 31 agreements, including the application of a 'presumption of regularity'.[14]

30. Of the agreements examined, 157 (68 per cent) were assessed as having been effectively executed. Of the remaining agreements, 42 (18 per cent) were assessed as 'ineffective'. A number of agencies were unable to provide evidence to demonstrate the effectiveness of a further 32 agreements (14 per cent). On the basis of the AGS legal advice, those agreements were assessed as 'in doubt'.

31. ANAO also identified 16 agencies that had increased the reported available balance of their annual appropriations by amounts that were at no time captured by a Section 31 agreement, or that spent receipts prior to having an agreement in place. Collectively, these agencies were assessed as having 'no agreement' in place in relevant periods.

32. The 2004–05 financial statements of each affected agency included disclosures relating to the period(s) in which a demonstrably effective agreement was not in place. Each agency was expected to identify the affected receipts and, where relevant, disclose the necessary adjustments to its reported available appropriation.

33. To the extent that amounts were identified as having been spent without appropriation, Section 83 of the Constitution was contravened. This

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[14] See Figure 3.1 in Chapter 3.

was disclosed by the relevant agencies in their financial statements. Where the Section 83 breach was a result of the agency signatory to an agreement not being authorised or the agency not having an agreement, a corresponding breach of Section 48 of the FMA Act was also required to be reported, given the specific obligations placed on agency Chief Executives under that Section to keep proper accounts and records.[15] Pursuant to the provisions of the *Auditor-General Act 1997* (Auditor-General Act) and the ANAO Auditing Standards (which incorporate the Australian Auditing and Assurance Standards), these breaches were reported as 'Other Statutory Matters' in the audit opinions of the affected agencies' 2004–05 financial statements.[16]

34. Table 1 summarises the receipts reported by agencies as having been received and, where relevant, spent during periods up to 30 June 2005 where the agency operated with an 'ineffective' or 'in doubt' agreement. Many of the relevant agencies had relied upon the affected agreement(s) since 1998 or 1999. The agreements were only replaced during 2004–05. Table 1 also includes the same information for those agencies that are in the 'no agreement' category.

Table 1

Amounts collected and spent by agencies without having a demonstrably effective Section 31 agreement in place: 1997 to 2005

Category	Agencies affected	Affected receipts ($)	Amount spent ($)
'In doubt' agreements	18	4 970 554 155	2 988 690 984[A]
'Ineffective' agreements	23	1 756 443 655	1 162 778 759[B]
'No agreement'	16	1 692 274 912	1 649 423 530[B]
Total	**52**[C]	**8 419 272 722**	**5 800 893 273**

Notes:

[A] In August 2005, AGS advised ANAO and Finance that, where the two requirements identified in its advice regarding the application of a 'presumption of regularity' were satisfied (resulting in an agreement being categorised as 'in doubt' – see paragraph 28), it was unlikely that a court would declare that expenditure in accordance with the agreement was invalid because of a breach of Section 83 of the Constitution.

[B] The relevant agencies' 2004–05 annual financial statements disclosed these amounts as having been spent in prior years and/or during 2004–05 without appropriation, in contravention of Section 83 of the Constitution.

[C] Total does not add as some agencies had an agreement(s) in more than one category.

Source: ANAO analysis based on examination of Section 31 agreements, agencies' financial reporting, evidence and advice provided by agencies to substantiate the authority of signatories to agreements, and the decision tree of AGS advices on assessing the effectiveness of agreements.

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[15] Under Section 48, a Chief Executive must ensure that accounts and records of the agency are kept as required by the FMOs. In particular, clause 2.3 of the FMOs provides that Chief Executives must ensure that the accounts and records are kept in a way that ensures the limit on any appropriation is not exceeded. Where the deficiency in relation to an agency's Section 31 agreement related to the Finance signatory, the affected agency did not breach Section 48 of the FMA Act.

[16] Subsection 57(4) of the FMA Act requires that, if the Auditor-General is of the opinion that the Chief Executive has contravened Section 48, the Auditor-General must state particulars of the contravention in the financial statement audit opinion.

Effective agreements

35. All 125 agreements that were signed by the responsible Minister or the relevant agency's Chief Executive (or an official acting in that capacity) were, consistent with legal advice provided to Finance, relevant agencies and ANAO, assessed as having been effectively executed by the agency. This was based on Chief Executives signing agreements under either an express or implied authorisation from the responsible Minister. However, seven of these agreements were assessed as being 'ineffective', due to the Finance official who signed on the whole-of-government side not holding the necessary delegation from the Finance Minister, leaving 118 effective agreements.

36. Officials at levels below the Chief Executive had signed the agency side of the remaining 39 agreements that were assessed as effective. In each case, the relevant agency was able to provide evidence confirming that the official had been expressly authorised or delegated by the responsible Minister or Chief Executive. Finance was also able to demonstrate that the official who signed each of those agreements held the necessary delegation from the Finance Minister.

'In doubt' agreements

37. Based on the AGS advice, a number of agencies relied upon a 'presumption of regularity' for agreements in respect of which they were unable to substantiate the authority of the relevant signatory – 11 agencies in respect to the agency signatory to 23 agreements[17], and Finance in respect to the Finance signatory to four agreements relating to four agencies.[18] In accordance with the AGS decision tree for assessing effectiveness, these agreements were assessed as 'in doubt'.

38. The agreements for three other agencies were assessed as 'in doubt' because, although they were unable to provide ANAO with evidence of an express Ministerial authorisation, there was sufficient and appropriate evidence available to provide an indication that the official may have been authorised.[19]

39. The 18 agencies with 'in doubt' agreements disclosed this issue, and the affected receipts (including amounts that had been spent) in their 2004–05 financial statements. Many of the affected agreements were relied upon by the relevant agency as the authority to appropriate money over a number of financial years, including for part or all of the 2004–05 financial year.

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17 For details of the relevant agencies, see Figure 3.2 in Chapter 3.

18 For details of the relevant agencies, see Figure 3.3 in Chapter 3.

19 For details of the relevant agencies, see paragraph 3.84 in Chapter 3.

to 30 June 2005, those agencies' annual appropriations had been increased by amounts totalling $4.97 billion under the authority of 'in doubt' agreements, with $2.99 billion of those receipts having been spent.

40. In August 2005, AGS advised ANAO and Finance that, where the two requirements identified in its advice regarding the application of a 'presumption of regularity' were satisfied (see paragraph 28), it was unlikely that a court would declare that expenditure in accordance with the agreement was invalid because of a breach of Section 83 of the Constitution. Reference to this legal advice was included in the affected agencies' appropriations disclosure note to their 2004–05 financial statements.

41. The agencies that have sought to rely on a 'presumption of regularity' depended upon the absence of any relevant records relating to them obtaining an express authorisation to exercise a statutory power on their Minister's behalf as the basis for claiming that there is no evidence the official was not authorised. In December 2005, Finance advised ANAO as follows:

> Finance notes that these decisions were made by Chief Executives of the affected agencies and assessments made against the decision criteria (based on AGS legal advice).

42. ANAO's understanding, from separate legal advice received, is that the 'presumption of regularity' is for the protection of those who are entitled to assume, because they cannot know, that the person with whom they deal has the authority that is claimed. For example, 'the person in the street' who cannot know whether a government official with whom he or she deals has the authority to undertake a particular function.

43. The application of a 'presumption of regularity' in relation to Australian Government agencies substantiating whether officials within the agency concerned complied with legislative requirements in executing a Section 31 agreement, where it is the agency that has relied on the agreement, is not desirable. Relying upon a 'presumption of regularity' in this context inevitably leaves doubt as to the effectiveness of the agreement and, therefore, the amount of the appropriation that was legally available to the relevant agency. This does not reflect sound administrative practice, in the ANAO's view.

44. To put matters beyond doubt, ANAO and Finance agree that agencies should obtain a written authorisation from the responsible Minister before entering into Section 31 agreements on the Minister's behalf. The Circulars issued by Finance in August 2004 and June 2005 advocated this approach as best practice.

45. In the interests of an effective and accountable financial framework, ANAO has recommended that Finance examine possible further

administrative and/or legislative changes that could limit the opportunity for agencies to rely upon a 'presumption of regularity' when increasing their annual appropriations. This might involve clearer legislative requirements covering Ministers delegating or authorising officials to exercise the statutory power of entering into Section 31 agreements. It might also involve stronger recordkeeping requirements that are specific to the signing of Section 31 agreements. ANAO has also recommended that agencies' recordkeeping practices be improved.

'Ineffective' agreements

46. In total, 42 agreements (18 per cent) across 23 agencies were assessed as being 'ineffective'.[20] This assessment was based on the evidence and advice provided by agencies and Finance in relation to the authority of their respective signatories, considered against the decision tree of AGS advices.

47. To address the issue of 'ineffective' agreements, on 24 June 2005, the Finance Secretary made two instruments under subsection 31(4) of the FMA Act.[21] They were:

- an instrument to cancel all agreements made on or before 30 June 2004. This step was taken to ensure each agency was operating on the basis of an effective agreement made under the new template[22] and to provide certainty regarding which agreements were in operation; and
- an instrument (the Variation Instrument) to vary all agencies' current agreements as at 30 June 2005 to include, as eligible receipts, amounts retained by the agency in reliance on prior, 'ineffective' agreements.

48. The Variation Instrument provided a basis for agencies to capture retrospectively all receipts that were subject to an 'ineffective' agreement. An appropriation for the affected receipts was made available to agencies as at 30 June 2005, which would allow any unspent amounts to be lawfully spent. This action could not, however, remove past breaches of Section 83 of the Constitution that occurred due to agencies spending receipts collected under an 'ineffective' Section 31 agreement.

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20 For details of the relevant agencies, see Figure 3.4 in Chapter 3.

21 Subsection 31(4) provides that the Finance Minister may at any time cancel or vary an agreement, without the consent of the other party. This power has been delegated to the Finance Secretary.

22 As noted, Finance had required all agencies to make a new agreement using the revised template issued in August 2004. By 30 June 2005, all agencies had executed a revised agreement using the new template.

49. The Variation Instrument applied in respect to receipts totalling $1.76 billion across 19 agencies.[23] Of those receipts, a total of $1.16 billion was disclosed by the relevant agencies as having been spent without appropriation between 1997–98 and 2004–05, in contravention of Section 83.

'No agreement'

50. ANAO identified 14 agencies[24] that had, for various reasons, reported their respective annual appropriations as having been increased by receipts totalling $105.31 million that had at no time been captured by a Section 31 agreement.[25] Three of those agencies disclosed $62.76 million of those receipts as having been spent without appropriation between 1997–98 and 2004–05, in contravention of Section 83 of the Constitution.

51. In October 2005, the Government agreed to forgo recovery from the relevant agencies of the amounts collected during the periods not covered by a Section 31 agreement. In order to give effect to this position, it was necessary to provide for those receipts to be captured by an effective agreement. This would also provide the relevant agencies with appropriation authority in respect of any unspent amounts still held. As with the Variation Instrument, this would not remove past breaches of Section 83 of the Constitution that occurred due to agencies spending receipts not covered by a Section 31 agreement.

52. On 28 October 2005, the Finance Secretary executed two further variation instruments under subsection 31(4) of the FMA Act (Variation Instruments 2 & 3). Those instruments varied the current agreements for 11 agencies, such that the amounts collected in the 'no agreement' period are eligible receipts for the purposes of the current agreement. Both instruments came into effect upon registration on the Federal Register of Legislative Instruments (FRLI) on 8 November 2005. Disclosure of the period not covered by an agreement, the affected receipts and, where relevant, amounts spent without appropriation and the associated breaches of Section 83 of the Constitution and Section 48 of the FMA Act was included in the affected agencies' 2004–05 financial statements.

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[23] Excluding cases where the ineffective agreement was not relied upon by the relevant agency to increase its annual appropriation, or the receipts collected under the agreement were not regularised by the Variation Instrument.

[24] For details of the relevant agencies, see Figures 2.1 and 2.2 in Chapter 2.

[25] In respect of five agencies, this situation arose due to the change in terminology used in annual Appropriation Acts, from "running costs" to "departmental items", which meant that some existing agreements were unable to operate from the start of the 1999–2000 financial year. The inability of these agreements to continue to operate was not identified until mid-2005.

53. A further two agencies, the Bureau of Meteorology (BoM) and Centrelink, were identified as having spent amounts totalling $1.59 billion prior to having a Section 31 agreement (and, for BoM, other necessary arrangements relating to appropriations) in place to provide them with appropriation authority.[26] Consequently, each contravened Section 83 of the Constitution and Section 48 of the FMA Act. The agreements subsequently executed for both agencies provided for the retrospective capture of all receipts collected during the period each did not have an agreement. Accordingly, neither agency was included in Variation Instruments 2 & 3 relating to 'no agreement' periods. Both agencies disclosed this issue in their 2004–05 financial statements.

Eligible receipts (Chapter 2)

54. The FMA Act does not provide guidance as to the type of receipts that may be included in Section 31 agreements. Legal advice to agencies has been that the only express restrictions on the terms and operation of an agreement in relation to the amounts that may be applied to increase an appropriation item are:

- that the agreement must specify the receipts that are eligible receipts for the purposes of the agreement; and
- the increase in the appropriation item cannot be greater than the amount of those specified receipts that is received.

55. However, the extent to which agencies' adherence to these limited requirements could be monitored was not promoted by the broad and inclusive manner in which eligible receipts have been defined in individual agreements, using a category based approach. The template included with Finance Circular No. 2004/09 improved the clarity and precision with which the receipts that an agency is entitled to retain can be identified.

56. Difficulties have also been encountered over time in the use of Section 31 agreements to increase an agency's annual appropriation for amounts debited from internally managed Special Accounts. Specifically, there has been an absence of clarity about if and how this can occur. Often, the relevant agreement did not clearly cover notional intra-agency transactions of this type. There is also ongoing uncertainty as to whether these internal transactions are relevant receipts for the purposes of the net appropriation provisions of the annual Appropriation Acts. The uncertainty in respect to these transactions does not contribute to the orderly management and governance of appropriations. ANAO has recommended that Finance take the necessary steps to remove such uncertainty.

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[26] The bulk of the funds spent without appropriation relates to $1.56 billion received by Centrelink in 1998–99 from other Commonwealth agencies for the delivery of services.

57. A third area where difficulties have arisen has involved the transfer of appropriation following a change of agency functions. Section 32 of the FMA Act enables the Finance Minister to issue a direction transferring appropriated amounts relating to a transferred function from the old agency to the new agency. The appropriation transferred can include any amounts added to an annual appropriation under the authority of Section 31 agreements. ANAO noted an instance where cash exceeding $25 million was passed from the Department of the Environment and Heritage to BoM, following BoM's prescription as a separate FMA Act agency in September 2002. A Section 32 direction transferring the appropriation authority to spend that cash was not executed. As a consequence, BoM spent those funds without appropriation authority, in contravention of Section 83 of the Constitution.

Accountability to the Government and the Parliament (Chapter 4)

58. The financial framework requires accountability for agency use of net appropriation arrangements in three primary ways, as follows:

- Since 1 January 2005, Section 31 agreements have been registered on the publicly available register, FRLI, enabling the Parliament to be aware of what agreements have been made since that date and their terms and conditions;
- Disclosure in PBS and Portfolio Additional Estimates Statements (PAES) of receipts estimated to be collected by the relevant agency under authority of a Section 31 agreement; and
- Disclosure in annual financial statements of the actual increase in the agency's annual appropriation under authority of Section 31.

59. ANAO found that improvements could be made in respect of each of these accountability mechanisms to assist in providing the Parliament with a complete and accurate record of the use of Section 31 arrangements. These are discussed below.

Registration of legislative instruments

60. Finance advised ANAO that it has consistently operated on the basis that, in the interests of accountability and disclosure to the Parliament, Section 31 agreements are properly regarded as legislative instruments and, therefore, should be registered on FRLI. Parliament has recently shown an interest in obtaining additional information to that already publicly available regarding the operation of Section 31 agreements. This includes information on the types of receipts covered by agreements. The registration of Section 31 agreements on FRLI will assist in this regard.

61. The *Legislative Instruments Act 2003* (LI Act), under which FRLI was established, requires instruments made on or after 1 January 2005 to be lodged in electronic form with the Attorney-General's Department for registration as soon as practicable after being made. However, ANAO found that there have often been delays of some months between the signing of Section 31 agreements and their registration. To improve the benefits obtained from the registration of Section 31 agreements on FRLI, such registration should be timely.

62. Irrespective of other provisions of the LI Act, Section 31 agreements are taken to be legislative instruments for the purposes of the Act once registered on FRLI.[27] The Act further provides that Section 31 agreements are not subject to the Act's disallowance or sunsetting provisions. However, there is ongoing uncertainty regarding the extent to which the LI Act was intended to apply to Section 31 agreements. In particular, Schedule 1 to the *Legislative Instruments Regulations 2004*, which prescribes certain instruments that are declared not to be legislative instruments for the purposes of the LI Act, appears to specifically remove agreements of this nature from the concept of legislative instruments. In November 2005, AGS advised Finance that all doubt in this respect should be removed. Finance advised ANAO that it was considering options proposed by AGS in relation to addressing this issue.

Reporting on the use of Section 31 agreements

63. As part of their annual PBS prepared in conjunction with the Budget, agencies are required to disclose estimates of the receipts from non-appropriation sources that will be available to be used in delivering their approved departmental and administered Outcomes. The current presentation of those estimates does not assist in providing users of the PBS with a clear understanding of the extent to which the relevant agency expects to increase its annual appropriation for amounts collected under authority of their Section 31 agreement. Enhanced guidance in this area may assist in improving the utility of the information provided in this respect. ANAO's examination also identified that the accuracy and consistency of the Section 31 receipt estimates that are disclosed in agency PBSs could be improved.

64. In addition, ANAO identified a number of agencies that had overstated or misstated the Section 31 receipts disclosed in their financial statements and/or PBS by including items such as:

- accrual based revenue amounts and other non-cash transactions, rather than cash received;

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[27] Subsection 5(3) of the LI Act provides that an instrument that is registered is taken, by virtue of that registration and despite anything else in the Act, to be a legislative instrument.

- amounts that were not eligible items under the terms of the relevant Section 31 agreement;
- amounts that related to other legislative provisions of the FMA Act relating to appropriations management, rather than Section 31; and
- amounts credited to Special Accounts, which stand to the credit of the special appropriation provided by the FMA Act in relation to those Accounts, as also being added to the agency's annual appropriation as Section 31 receipts.

65. ANAO concluded that improvements are required to agencies' reporting and disclosure of appropriations, including in their PBS and PAES. A number of agencies moved to address reporting issues identified in this performance audit in their 2004–05 financial statements.

66. In this context, there will also be an increased focus on legislative compliance as part of ANAO's future financial statement audit coverage, as a supplement to the conventional financial statement audit.[28] This will involve confirming the presence of key documents or authorities, and sample testing of relevant transactions directed at obtaining assurance about entities' compliance with key aspects of legislative compliance in relation to annual appropriations, special appropriations, annotated appropriations (through Section 31 arrangements) and special accounts. This will not provide a guarantee that all legislative breaches will be identified, but will give reasonable assurance as to the state of legislative compliance in key areas.

Financial framework enhancement opportunities (Chapter 5)

67. Many of the findings of this performance audit relate to agencies' understanding of, and compliance with, the financial framework. The audit also identified scope for enhancing certain aspects of the financial framework as it operates in respect to net appropriations.

Retrospective application of Section 31 agreements

68. It has been a common practice for agencies to enter into Section 31 agreements some time after the commencement of the period to which the agreement is then purported to apply. Indeed, nearly half of the agreements made to 30 June 2005 had been applied retrospectively to amounts received by the agency prior to the agreement being executed.

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[28] In this respect, the objective of an audit of a financial report is to enable the auditor to express an opinion whether the financial report is prepared, in all material respects, in accordance with the Finance Minister's Orders, which include the application of the Australian Accounting Standards.

69. The basis on which legal advice provided to agencies has concluded that agreements made under Section 31 of the FMA Act can be expressed so as to apply to amounts previously received has been the broad nature of the language of that Section, and the absence of any provision requiring that such agreements may only operate prospectively. In this context, greater specificity in the FMA Act as to the conditions under which an agreement can be applied retrospectively to amounts previously received would assist in enhancing the rigour of the financial framework and promoting orderly governance of appropriations.

70. Irrespective of any legislative changes, retaining cash receipts for significant periods in anticipation of subsequently obtaining the necessary appropriation authority to spend those amounts, or operating for a period of time as if that authority existed when it did not, can put an agency at risk of spending in excess of its legally available appropriation. This risk would be reduced by changes to administrative practices that meant that, wherever possible, Section 31 agreements are in place prior to agencies receiving eligible amounts.

Role of Section 31 agreements

71. One of the more significant changes under the FMA Act from the net appropriation arrangements that previously existed was the change in the role played by the agreement itself.

72. Previously, the annual Appropriation Acts specified the sources from which net appropriations could be received. The agreements made under those arrangements identified, in a Schedule, the types of receipts an agency would be able to collect under the broad sources specified in the Appropriation Acts, and the quantum of such receipts expected to be collected in the relevant financial year. Under the FMA Act, the receipts each agency may use to increase its annual appropriation are established by the terms of its particular Section 31 agreement.

73. As discussed, difficulties have been encountered by a number of agencies in terms of ensuring an agreement that is relied upon has been effectively executed and/or is capable of operating in the manner intended. In this context, there may be merit in examining the on-going role of individual agency agreements in the management of net appropriations. Areas that could be examined include:

- The nature of the instrument that is used to provide an agency with access to net appropriations. Changes to the instrument could provide greater certainty over the effectiveness of net appropriation arrangements by reducing the potential for officials to act without Ministerial authorisation. One option may be to revise the relevant

legislative provisions so that the Finance Minister (or his or her delegate) may, following consultation with the relevant Minister, issue a direction regarding the conditions under which specified receipts may be retained by an agency; and

- Whether instruments relating to individual agencies should be retained as the means of specifying eligible receipts. Specifically, returning the central role in net appropriations from individual agency agreements to the annual Appropriation Acts so as to provide certainty and transparency in relation to the majority of net appropriations that will be available to agencies, without the need for separate agency agreements in all cases.

74. In December 2005, Finance advised ANAO that:

> Finance is currently examining possible policy, administrative and legal changes that could be effected to improve the operation and effectiveness of section 31 agreements, as part of a broader project to simplify the management of the financial framework.

Recommendations and agency responses

75. ANAO has made five recommendations. The first three are aimed at improving administration of net appropriation arrangements within the current financial framework. Specifically, they address the interaction of Section 31 agreements with the operation of Special Accounts (Recommendation No. 1) and establishing demonstrably effective Section 31 agreements (Recommendation Nos. 2 and 3). The final two recommendations identify opportunities for Finance to examine possible improvements to the framework (Recommendation Nos. 4 and 5).

76. Finance largely agreed to the recommendations (it agreed with qualification to Recommendation No. 1 and agreed to the remainder). Where they responded to recommendations, all other agencies agreed (one agency agreed with qualification to one recommendation). Detailed agency comments on the proposed audit report are included at Appendix 1, and a summary of agency responses to each recommendation is included at Appendix 2.

Recommendations

Set out below are ANAO's recommendations and agencies' abbreviated responses. More detailed responses are shown in the body of the report immediately after each recommendation. A summary of agency responses to the recommendations is included at Appendix 2.

Recommendation No.1
Para. 2.89

In order to provide certainty as to the capacity of amounts debited from internally managed Special Accounts to be captured by agencies' Section 31 agreements, ANAO *recommends* that the Department of Finance and Administration take the necessary steps to align the provisions relating to notional transactions in the annual Appropriation Acts with those set out in Section 6 of the *Financial Management and Accountability Act 1997*.

Finance agreed with qualification. All other agencies that responded to this recommendation agreed.

Recommendation No.2
Para. 3.35

ANAO *recommends* that, before entering into future Section 31 agreements:

(a) all signatories establish the capacity in which they may legitimately sign the agreement, and correctly identify that capacity in the agreement;

(b) where it is intended that an official will be entering into the agreement, rather than the holder of the statutory power, agencies take steps to obtain written authorisations or delegations (where available) from the responsible Minister (or, for Finance portfolio agencies, Chief Executive); and

(c) delegates of the Finance Minister satisfy themselves that the agreement has been signed by the responsible Minister or an agency official who holds a current authorisation or delegation, as appropriate, from the responsible Minister (or, for Finance portfolio agencies, Chief Executive.).

All agencies that responded to this recommendation agreed to relevant parts.

Recommendation No.3 Para. 3.97

In the interests of an effective and accountable financial framework for the management of appropriations, ANAO *recommends* that:

(a) as part of their financial controls and in accordance with Commonwealth recordkeeping requirements, all agencies maintain adequate records of Section 31 authorisations and delegations provided by Ministers (and, where relevant, Chief Executives), together with records of which official(s) held the power when Section 31 agreements were signed; and

(b) the Department of Finance and Administration examine possible administrative and/or legislative changes that could limit the opportunity for agencies to rely upon a 'presumption of regularity' when increasing their appropriations through Section 31 arrangements.

All agencies that responded to this recommendation agreed to relevant parts.

Recommendation No.4 Para. 5.24

ANAO *recommends* that, as part of its responsibilities for developing and maintaining the Commonwealth financial framework, the Department of Finance and Administration consider the merits of including greater specificity in the relevant legislative provisions regarding the conditions under which net appropriation agreements may be applied retrospectively to amounts previously received by an agency.

BoM agreed with qualification. All other agencies that responded to this recommendation agreed.

Recommendation No.5 Para. 5.38

ANAO *recommends* that, as part of its current work examining opportunities to simplify the financial framework, the Department of Finance and Administration examine options to improve the framework for net appropriation arrangements, including the merits of specifying the relevant terms and conditions (including common eligible receipts) in the annual Appropriation Acts, rather than through delegated legislation (Section 31 agreements).

All agencies that responded to this recommendation agreed.

Audit Findings and Conclusions

1. Introduction

This chapter discusses the appropriation framework in which net appropriations are an element; the legislative history of such arrangements; the respective roles of agencies and Finance; and the audit approach.

Appropriation framework

1.1 The Australian Constitution states that all revenue or moneys raised or received by the Executive Government shall form one Consolidated Revenue Fund (CRF) (Section 81). Section 83 of the Constitution provides that no money shall be drawn from the Treasury of the Commonwealth[29] except under an appropriation made by law. An appropriation is an authorisation by Parliament to spend an amount from the CRF for a particular purpose.[30]

1.2 Taken together, the requirements of Section 81, Section 83 and Section 97 of the Constitution (governing accounting and audit) create a regime for Parliament to exercise control over, and require accountability for, the Executive Government's spending.

1.3 Australian Government agencies that are subject to the *Financial Management and Accountability Act 1997* (FMA Act) receive funding to deliver their approved Outcomes through departmental[31] and administered[32] appropriations provided by annual Appropriation Acts passed by the Parliament.[33] They also receive funding through special appropriations provided in Acts of Parliament that deal with particular purposes of spending.

1.4 Agencies may also receive payments from the public, employees, private sector entities, other agencies or other governments in the course of undertaking their respective functions. This may, for example, relate to user charging fees for goods or services provided. Those amounts automatically form part of the CRF upon being received. This is because the Commonwealth views the CRF as being 'self-executing'.[34] Accordingly, by virtue of section 83 of

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29 In this context, the Treasury of the Commonwealth refers to the CRF.

30 Department of Finance and Administration, Estimates Memorandum 2003/27, *Refresher on Appropriation Framework – Rules*, 28 August 2003, p. 1.

31 Departmental items are assets, liabilities, revenues and expenses controlled by agencies and used in producing their outputs.

32 Administered items are items that the entity does not control. Rather, they are controlled by the Government and managed or overseen (or 'administered') by agencies on behalf of Government.

33 Annual appropriations are generally made in six Acts each year. Of these six Acts, three are prepared at the time of each Federal Budget and a further three are prepared, as necessary, at Additional Estimates.

34 Refer to Finance Circular No. 2004/06, *Appropriations and the Consolidated Revenue Fund*, Department of Finance and Administration, 10 June 2004, p. 1.

the Constitution, the receiving agency requires an appropriation authority before it is able to spend those receipts.

1.5 A mechanism for providing that authority is the use of net appropriation arrangements. Under such arrangements, legislative deeming provisions operate to cause the receiving agency's appropriation item in the annual Appropriation Acts to be increased by the amount of certain eligible receipts received from non-appropriation sources.

1.6 As amounts held in agency bank accounts form part of the CRF, the Constitution does not distinguish between amounts held in the agency's bank account and the Commonwealth's central bank account, the Official Public Account (OPA). Accordingly, the Constitution does not require agencies to have an appropriation authority to retain receipts. However, recognising the risk involved in holding receipts that are not supported by an appropriation in an agency's bank account, the *Agency Banking Framework – Guidance Manual* requires agencies to not retain these receipts and return them to the OPA.[35] (This is discussed further at paragraphs 2.106 to 2.113.)

Net appropriation agreements

1.7 Under Section 31 of the FMA Act, the Finance Minister may enter into agreements, commonly referred to as Section 31 agreements, for the purposes of items in Appropriation Acts that are marked "net appropriation". Each agreement identifies those types of receipts that will be eligible to be added to a particular agency's annual departmental or administered appropriation item. The FMA Act requires that an agreement be made with the Minister responsible for the appropriation item or, in the case of items for which the Finance Minister is responsible, with the Chief Executive of the agency for which the appropriation is made.[36]

1.8 A Section 31 agreement operates to cause relevant provisions in the annual Appropriation Acts to take effect such that the specified appropriation item is automatically increased by the amount of eligible receipts received. In this respect, the net appropriation provisions of the annual Appropriation Acts and FMA Act provide the Executive Government with the authority to increase the appropriations set out in the Schedules to the Appropriation Acts, providing certain specified steps are undertaken. Figure 1.1 sets out the terms of Section 31 of the FMA Act, which must be complied with in order for an agency to obtain appropriation authority to spend amounts received from non-appropriation sources.

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[35] See section 4.2 of the Manual.

[36] Except for agreements relating to the ANAO. Section 52 of the *Auditor-General Act 1997* (Auditor-General Act) provides that any net appropriation agreement made by the Finance Minister in relation to the Audit Office must be made with the Auditor-General.

Figure 1.1

Section 31 of the FMA Act

31 Agreements for "net appropriations"

(1) The Finance Minister may enter into agreements for the purposes of items in Appropriation Acts that are marked "net appropriation".

(2) In the case of items for which the Finance Minister is responsible, the agreement is to be made with the Chief Executive of the Agency for which the appropriation is made. In all other cases, the agreement is to be made with the Minister who is responsible for the item.

(3) An agreement need not relate to a particular Appropriation Act or Acts and may be made for any period, including a period longer than a financial year.

(4) The Finance Minister may at any time cancel or vary an agreement, without the consent of the other party.

(5) In this section:

Appropriation Act includes a Supply Act.

Source: *Financial Management and Accountability Act 1997*.

1.9 In each financial year since the FMA Act commenced on 1 January 1998, the annual Appropriation Acts, including the Parliamentary Departments Appropriation Acts, have marked the departmental items for all budget-funded agencies, and specific administered items for some agencies, as "net appropriation".[37] The Acts have further provided that, if a Section 31 agreement applies to a departmental or administered item, the amount specified in the item is taken to be increased in accordance with the agreement, on the conditions set out in the agreement.[38]

Use of net appropriations

1.10 Net appropriations are a longstanding feature of the Commonwealth's financial framework. Similar arrangements existed under Section 35 of the *Audit Act 1901* (Audit Act), (which was added to the Act in 1969) and, prior to that, in the annual Appropriation Acts (through deduction lines and notations in the schedules to an Act).

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[37] In 1997–98 and 1998–99, each item that was so marked was individually identified in the Schedule to the Appropriation Acts. From 1999–2000, all departmental items have been collectively marked "net appropriation" in a Section of the Act itself, and a further Section has marked certain specified administered appropriation items.

[38] See, for example, Section 10 of *Appropriation Act (No. 1) 2005–2006.*

1.11 However, the extent to which agencies have used such arrangements to increase their available appropriation has grown considerably over time. During the course of the 1990s, net appropriation agreements became more widespread amongst agencies, in part reflecting public sector management reforms introduced at the time.[39] This particularly related to an increasing focus on user charging and cost-recovery by agencies for services provided, as a means of improving resource allocation and reducing the call on Budget funding for agency running costs.

1.12 There has continued to be growth in the use of net appropriations since the commencement of the FMA Act. In 1996–97, the last full financial year prior to the Act commencing, agencies reported net appropriation receipts totalling $831 million. In 2003–04, 68 FMA Act agencies collectively reported receipts totalling $1.55 billion as having been added to their respective annual appropriations by operation of Section 31, a growth of some 86 per cent. In 2004–05, 67 agencies reported Section 31 receipts totalling $1.46 billion.[40]

1.13 The bulk of reported Section 31 receipts relate to agencies' departmental appropriation items. These receipts include cost-recovery fees charged by agencies for goods and services provided to the public, agencies in other jurisdictions, and other Commonwealth agencies; proceeds from the sale of departmental assets; and other amounts received by an agency in the course of its departmental activities.

1.14 As noted, administered items are marked "net appropriation" on an exception basis. However, there has, in recent years, also been a growth in the number of agencies seeking to have net appropriation arrangements established in respect to one or more of their administered appropriation items. In 1999–2000, the administered items for three Outcomes in three agencies were marked "net appropriation". This had grown to 14 Outcomes in eight agencies in *Appropriation Act (No.1) 2005–06*.

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[39] Department of Finance and Administration Submission to ANAO, *Management of Net Appropriation agreements*, 10 February 2005.

[40] The $99 million reduction in Section 31 receipts reported in 2004–05 compared to 2003–04 is consistent with increased actual Section 31 receipts, combined with corrections made by agencies in 2004–05, in response to issues raised in this performance audit, to exclude amounts previously incorrectly disclosed as Section 31 receipts. For example, three agencies (the Department of Industry, Tourism and Resources (DITR), the Department of Health and Ageing (Health) and the Australian Radiation Protection and Nuclear Safety Agency (ARPANSA)) had included Special Account receipts totalling $103 million in the Section 31 receipts reported in 2003–04. Each agency excluded Special Account receipts from the Section 31 receipts reported in 2004–05. In December 2005, Finance advised ANAO that overall departmental appropriations have also increased over the period and Section 31 appropriations have reduced as a proportion. Finance noted that, in 1996–97, Section 31 receipts comprised 6.1 per cent of agencies' departmental (running costs) appropriations, and that, by 2004–05, Section 31 receipts comprised only 4.4 per cent of agencies' departmental appropriations.

1.15 The eligible receipts included in Section 31 agreements made in respect to an administered appropriation item are normally much more restricted than those included in departmental agreements, and will reflect the particular purpose of the relevant administered Outcome. For example, the administered agreement for the Department of Foreign Affairs and Trade (DFAT) for its Outcome 3, "Public understanding in Australia and overseas of Australia's foreign and trade policy and a positive image of Australia internationally", only includes one type of eligible receipt – 'receipts for the sponsorship for the administered item, the 2005 World Expo in Aichi Japan, for outcome 3.'

Changes in legislative arrangements under the FMA Act

1.16 The evolution of requirements relating to net appropriations provides useful background to some of the observations made in this report.

1.17 Section 35 of the Audit Act provided for certain amounts to be deemed to have been appropriated for the purposes and services referred to in the relevant item, subdivision or division in a Schedule to an Appropriation Act. The Audit Act did not, however, provide for the making of net appropriation agreements, despite such agreements commonly being referred to as 'Section 35 agreements.'

1.18 Prior to the FMA Act, the annual Appropriation Acts specified the types of receipts to which net appropriation arrangements could apply. The Appropriation Acts further provided that, for the purposes of the Audit Act, any money of those types received by the relevant agency could be credited to an appropriation item marked "net appropriation", to the extent and on the conditions agreed between the Minister for Finance and the Minister responsible for the relevant agency.

1.19 The extent and conditions agreed for each agency were set out in net appropriation agreements. As it was the annual Appropriation Acts that specified the types of receipts that agencies were able to retain, as well as being the source of the power for Ministers to make such agreements, they had to be renewed or extended to apply to each successive Supply Act and Appropriation Act.

1.20 On 1 January 1998, the Audit Act was replaced with the FMA Act and associated legislation. Under the revised arrangements, it is Section 31 of the FMA Act that provides the power for Ministers to enter into net appropriation agreements. Further, the annual Appropriation Acts no longer specify the types of receipts that can be retained as net appropriations. Instead, as noted, the relevant sections of the annual Appropriation Acts provide that the amount specified in an appropriation item is taken to be increased in accordance with, and on the conditions set out in, the Section 31 agreement applying to that item.

1.21 A further significant change is that an agreement made under Section 31 need not relate to a particular Appropriation Act and may be made for any period, including a period longer than a financial year.

1.22 Figure 1.2 sets out the main differences in the net appropriation arrangements that apply under the FMA Act compared to the previous arrangements.

Figure 1.2

Comparison of net appropriation arrangements pre- and post-FMA Act

Arrangements under Audit Act	Arrangements under FMA Act
Sources from which net appropriation receipts could be received were specified in the annual Appropriation Acts.	Sources from which net appropriation receipts can be received are specified in individual agency agreements.
The annual Appropriation Acts provided that money received from the sources specified in the Act may be credited to an item, subdivision or division that was marked "net appropriation", to the extent and on the conditions agreed between the Finance Minister and the Minister responsible for the relevant agency.	The Finance Minister may enter into agreements for the purposes of items in Appropriation Acts that are marked "net appropriation" (subsection 31(1)). In the case of items for which the Finance Minister is responsible, the agreement is to be made with the Chief Executive of the agency for which the appropriation is made. In all other cases, the agreement is to be made with the Minister who is responsible for the item (subsection 31(2)).
Section 35 of the Audit Act provided that, where amounts specified in a Schedule to an Appropriation Act were expressed to be less an amount provided by another source, an amount equal to those amounts was deemed to be appropriated for the purposes referred to in the item.	The annual Appropriation Acts provide that, if a Section 31 agreement applies to a departmental or administered item, then the amount specified in the item is taken to be increased in accordance with the agreement, and on the conditions set out in the agreement.
Net appropriation agreements applied to specific Appropriation Acts, and had to be renewed or extended to apply to each Supply Act and Appropriation Act, with appropriations lapsing each year.	An agreement need not relate to a particular Appropriation Act or Acts and may be made for any period, including a period longer than a financial year (subsection 31(3)). The Finance Minister may at any time cancel or vary an agreement, without the consent of the other party (subsection 31(4)).[A] Since 1999–2000, departmental appropriations, including deemed appropriations from Section 31 receipts, do not lapse at the end of a financial year.

Note A: With the exception of agreements for the Australian National Audit Office. Section 52 of the *Auditor-General Act 1997* provides that the Finance Minister must not cancel or vary a net appropriation agreement made with the Auditor-General unless the Auditor-General consents.

Source: ANAO analysis.

Roles and responsibilities

1.23 In accordance with the framework created by the FMA Act, agencies are responsible for the control, management and reporting of their finances, including appropriations. The responsibilities of the Department of Finance and Administration (Finance) relate to the maintenance of the financial framework established by the FMA Act, FMA Regulations and the Finance Minster's Orders (FMOs) and the provision of guidance on the operation of that framework.

Agency responsibilities

1.24 Agencies are individually responsible for managing and disclosing their use of appropriations in accordance with the Commonwealth's financial framework. Quite specific obligations in relation to keeping proper accounts and records are placed on agency Chief Executives by the FMA Act and FMOs. These include a requirement to keep the records of the agency in a manner that, among other things, ensures that moneys are only expended for the purpose for which they were appropriated, and the limit (if any) on appropriations is not exceeded.

1.25 Prior to 1999–2000, all amounts received by agencies were held in the OPA. To expend those amounts, agencies had to request their drawdown through the Cash and Appropriations Management Module (CAMM), a centralised system managed by Finance. Finance controlled agencies' access to net appropriations through the issuance of Agency Appropriation Advices.

1.26 With the introduction of agency transactional banking on 1 July 1999, control over access to net appropriations passed to individual agencies. Accordingly, each agency is responsible for ensuring that each of the elements required in order for an annual appropriation to be increased by operation of Section 31 are in place before any relevant amounts are spent.

1.27 Agencies are expected to disclose estimated non-appropriation receipts as part of the Budget process. The actual Section 31 receipts added to an agency's annual appropriations are required to be disclosed in the agency's annual financial statements, which are to be prepared in accordance with the applicable FMOs. This involves disclosing those amounts as part of revenue received from independent sources, and in the agency's acquittal of its authority to draw cash from the CRF under the annual Appropriation Acts. The latter is required to be disclosed as a Note to the financial statements. In addition, agencies are required to provide information to Finance for the preparation of whole-of-government financial reporting.

Finance responsibilities

1.28 For its part, Finance remains responsible for developing and maintaining the financial framework for agencies that are subject to the FMA Act. In terms of Section 31 of the FMA Act, Finance advised the Australian National Audit Office (ANAO) in February 2005 that its role comprises:

- negotiating all agreements with the relevant agency;
- signing each agreement as the delegate of the Finance Minister. Finance advised ANAO that, as a signatory to Section 31 agreements, it is responsible for assessing the types of receipts identified by agencies in the proposed agreement, to ensure that they are appropriate; and
- providing a range of guidance and advice to agencies on appropriation management generally and more specifically on Section 31 agreements.

1.29 In advance of this performance audit commencing, Finance issued Finance Circular No. 2004/09, *Net appropriation agreements (Section 31 agreements)*, in August 2004. This Circular was the culmination of an examination by Finance of Section 31 of the FMA Act during the first seven months of 2004.[41] Finance has reported that the review was undertaken as part of its rolling review of various aspects of the financial framework and reflected emerging concerns within the Department about the form of net appropriation agreements, and agencies' application of the agreements.[42] The stated purpose of the Circular was as follows:

> This Finance Circular provides guidance for agencies subject to the FMA Act on net appropriation agreements, made under section 31 of the FMA Act (Section 31 agreements). In particular, this Finance Circular sets out the arrangements for the establishment and management of section 31 agreements. It builds on the experience gained since the introduction of net appropriation agreements.[43]

1.30 A revised template for use in the preparation of Section 31 agreements was also issued as an attachment to the Circular. Estimates Memorandum–2004/22, issued by Finance on 10 September 2004, required all agencies to negotiate new Section 31 agreements using the new template as soon as practicable, but no later than 29 October 2004.[44] The first agreement made using

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41 Department of Finance and Administration, *2004–05 Annual Report*, op. cit., 2005, p. 28.

42 ibid.

43 Finance Circular No. 2004/09, *Net appropriation agreements (Section 31 agreements)*, Department of Finance and Administration, 11 August 2004, p.1.

44 Estimates Memorandum – 2004/22, *Financial Management and Accountability Act 1997 Section 31 agreements*, Department of Finance and Administration, 10 September 2004.

the new template was executed on 1 November 2004.[45] The process of executing new template agreements for all agencies was completed on 30 June 2005, with the execution of an agreement for the Department of Defence (Defence).

1.31 In response to matters raised in this performance audit, in June 2005 Finance replaced Finance Circular No. 2004/09 with Finance Circular No. 2005/07, *Net appropriation agreements (Section 31 Agreements)*. A further revised template was issued with that Circular. The updated Finance Circular provided similar guidance as to who should, as matter of best practice, sign Section 31 agreements. The main amendments to the Finance Circular related to Attachment B to the Circular, which provides guidance for completing the template. In December 2005, Finance advised ANAO that:

> This guidance, which relates to process, was enhanced to ensure that agencies correctly reflect the capacity in which agreements are executed in the execution clause.

Audit approach

1.32 The objective of this performance audit was to assess agencies' financial management of, and accountability for, the use of net appropriation agreements to increase available appropriations.

1.33 The audit commenced in October 2004. Six FMA Act agencies were selected for detailed examination, as follows:

- Australian Agency for International Development (AusAID);
- Bureau of Meteorology (BoM);
- Defence;
- Department of Industry, Tourism and Resources (DITR);
- Department of Immigration and Multicultural and Indigenous Affairs (DIMIA); and
- Finance.

1.34 Finance was also included in the audit in its capacity as the central agency with broad responsibility for the management of the Commonwealth financial framework, and the co-signatory to all agreements. Fieldwork was undertaken in these six agencies between October 2004 and April 2005.

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[45] This was the agreement for the Department of the Senate. The agency signatory to that agreement signed on 26 October 2004, with the Finance signatory signing on 1 November 2004.

1.35 ANAO also examined 231 agreements made in respect of FMA Act agencies between 1 January 1998 and 30 June 2005[46], and agencies' financial reporting of the use of Section 31 to increase their appropriations. ANAO engaged Professor Dennis Pearce, Senior Counsel at Phillips Fox, to provide legal advice in respect to certain aspects of the matters examined in the audit. In response to issues raised during the course of the audit, the Australian Government Solicitor (AGS) also provided various advices to Finance, agencies and/or the ANAO.

1.36 Issues Papers discussing various aspects of the audit were provided to agencies on 3 June 2005 and 25 July 2005. Given the nature of the issues raised in this audit, including those relating to Constitutional matters, and the consequential implications for agency financial statements, substantial delays arose from the need for agencies to achieve resolution of the issues. Consequently, a proposed audit report was issued to agencies for comment in November 2005.[47]

1.37 The audit was conducted in accordance with ANAO Auditing Standards at a cost to the ANAO of $535 000.

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[46] These agreements had been made in respect to 79 agencies. The least number of agreements made in respect to an individual agency in that period was one (including five agencies that had been created since 1 July 2003) and the most was eight (for Finance).

[47] Finance provided comments on the June 2005 Issues Papers on 9 September 2005 and on the July 2005 Issues Papers on 14 October 2005.

2. Prerequisites for Increasing Annual Appropriations Under Section 31

This chapter discusses the conditions that must be satisfied before an agency's appropriation item will be increased to enable it to spend amounts received from non-appropriation sources, and various instances where agencies purported to increase their appropriation for amounts received in the absence of all necessary arrangements. It also discusses issues relating to identifying amounts that are eligible to be retained and spent by an agency.

Conditions that must be satisfied

2.1 In order for an agency to receive an appropriation authorising it to retain and spend amounts received from non-appropriation sources, each of the following arrangements must be in place:

- there must be a relevant appropriation item for the agency in an annual Appropriation Act that has been marked "net appropriation";
- there must be an effectively executed Section 31 agreement in place that applies to that appropriation item; and
- the amount received must be of a kind that is specified as being an eligible receipt for the purposes of the agreement and, therefore, a relevant receipt for the purposes of the annual Appropriation Acts.

2.2 Purporting to increase an appropriation in advance of all requirements being in place will result in an agency misstating its available appropriation. It also places the agency at risk of spending money from the CRF that has not been appropriated, in contravention of Section 83 of the Constitution.

Purporting to increase an appropriation without an agreement

2.3 ANAO identified 14 agencies that had, for various reasons, purported to increase their respective annual appropriations for amounts that had at no time been captured by a Section 31 agreement.[48]

[48] These instances are to be distinguished from agencies that increased their appropriation for amounts collected under an agreement subsequently found through this audit to have been ineffective, which are discussed in Chapter 3.

No executed agreement

2.4 Nine agencies increased their reported available appropriations for amounts totalling $95.45 million that were received in periods to which their respective Section 31 agreements had never purported to apply. Each agency disclosed this issue in its 2004–05 financial statements or, in the case of the National Oceans Office, its closing accounts following its de-prescription as an FMA Act agency on 3 November 2004.

2.5 Two agencies disclosed the spending of amounts totalling $61.45 million that had not been appropriated, in contravention of Section 83 of the Constitution.[49] In both cases, a breach of Section 48 of the FMA Act was also required to be reported, given the specific obligations placed on agency Chief Executives under that Section to keep proper accounts and records.[50] Pursuant to the provisions of the Auditor-General Act and the ANAO Auditing Standards (which incorporate the Australian Auditing and Assurance Standards), these breaches were reported as 'Other Statutory Matters' in the audit opinions of the affected agencies' 2004–05 financial statements.[51]

2.6 Figure 2.1 identifies the relevant agencies, and the affected periods, receipts and, where applicable, amounts spent without appropriation disclosed by each agency.

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[49] The 2004–05 financial statements of one affected agency, the Australian Bureau of Statistics (ABS) categorised 1998–99 as a period in which its agreement was ineffective, resulting in a breach of Section 83 of the Constitution (as was the case for 1997–98 and 1 July 1999 to 6 March 2005 – see Figure 3.4). ABS's financial statements were completed prior to the assessment of the status of this period being finalised.

[50] Under Section 48, a Chief Executive must ensure that accounts and records of the agency are kept as required by the FMOs. In particular, clause 2.3 of the FMOs provides that Chief Executives must ensure that the accounts and records are kept in a way that ensures the limit on any appropriation is not exceeded.

[51] Subsection 57(4) of the FMA Act requires that, if the Auditor-General is of the opinion that the Chief Executive has contravened Section 48, the Auditor-General must state particulars of the contravention in the financial statement audit opinion.

Figure 2.1

Amounts collected in periods not covered by a Section 31 agreement

Agency	Period affected	Receipts not captured ($)	Receipts spent ($)
Australia-Japan Foundation	1 July 97 to 21 June 98	1 390	Nil
Australian Bureau of Statistics	1 July 98 to 30 June 99[A]	24 265 909	13 015 624
Department of Education, Science & Training	1 July 97 to 28 June 98	11 416 000	Nil
Department of Foreign Affairs & Trade	1 July 97 to 17 May 98	54 001 750	48 438 210
Department of the Parliamentary Library	1 July 97 to 30 April 98	33 964	Nil
Federal Court of Australia	1 July 98 to 30 June 00	1 973 700	Nil
Joint House Department	1 July 97 to 23 June 98	3 497 387	Nil
National Oceans Office	1 July 03 to 3 Nov 04	239 073[B]	Nil
Office of the Renewable Energy Regulator	1 July 03 to 25 May 05	19 000[C]	Nil
	Total	**95 448 173**	**61 453 834**

Notes:

[A] In December 2005, ABS advised ANAO as follows: 'The ABS's 2004–05 financial statements disclosed that on balance an 'ineffective' Section 31 agreement existed for 1998–99. Subsequent to the issuing of its audit opinion, the ANAO received further legal advice that classified a 'no agreement' for this period. While the ABS disagrees with this opinion, as it has documentation which points to an agreement although a signed copy has not been able to be found, it accepted the ruling given that appropriation of 'no agreement' receipts could occur through a similar process as receipts classified as 'ineffective'.' (See footnote 49).

[B] These receipts were included in appropriation transferred to the Department of the Environment and Heritage under a direction made under Section 32 of the FMA Act.

[C] The 'no agreement' period for the Office of the Renewable Energy Regulator (ORER) was 1 July 2003 to 25 May 2005. The disclosure of this issue included in ORER's 2004–05 financial statements referred to the $19 000 reported in 2003–04, but did not identify whether any relevant amounts had been received in the period 1 July 2004 to 25 May 2005, prior to its agreement being executed on 26 May 2005..

Source: ANAO analysis.

2.7 Five of the nine instances identified in Figure 2.1 related to 1997–98.[52] This was a transitional year, with the FMA Act commencing on 1 January 1998. A number of agencies did not enter into a net appropriation agreement that related to amounts received in 1997–98 until after the FMA Act had commenced.

[52] They are the 'no agreement' periods for the Australia-Japan Foundation, the Department of Education, Science and Training, the Department of Foreign Affairs and Trade, the Department of the Parliamentary Library and the Joint House Department.

2.8 As noted in Chapter 1, a significant change under the FMA Act was the introduction of the capacity for agreements to be perpetual in their terms. Previously, because they had to be renewed annually, it was normal for an agreement to state that it would apply in respect to a particular financial year. With the removal of that requirement, it is apparent that there was some confusion among agencies as to how their initial agreement made under Section 31 should be expressed so as to ensure it captured all relevant amounts received in 1997–98.

2.9 While some agencies' agreements were expressed so as to capture all amounts received from 1 July 1997, each of the agreements executed late in the 1997–98 financial year by the five agencies identified in Figure 2.1 simply stated that it would commence upon signature. As a result, those agencies did not have an agreement that captured amounts received prior to that date. In this respect, DFAT advised ANAO in August 2005 that:

> from the documentation available, both Finance and DFAT appeared to have believed that the legal requirement related to expending receipts and not the collection of receipts. It would seem, as this was the first year of the FMA Act, there was considerable confusion as to the legal intent of Section 31 of the Act.

Agreements unable to operate

2.10 From 1 July 1999, there was a fundamental change in the way appropriation legislation was drafted and operated. Prior to 1999–2000, the Schedule to the annual Appropriation Acts, which identified the services for which money was appropriated to an agency, made appropriations by reference to 'running costs' items (which were usually marked "net appropriation") and 'other services' items (which were not marked).

2.11 The 1999–2000 annual Appropriation Acts ceased to refer to running costs and other services. Instead, appropriations were made by reference to the new concepts of 'departmental items' and 'administered items', as defined in the Appropriation Acts. These changes occurred in the context of the introduction of accrual budgeting for Australian Government agencies, based on an outcomes/output framework.[53] As discussed in Chapter 1, the introduction of agency transactional banking on 1 July 1999 also had implications for the management of Section 31 receipts.

2.12 Internal advice provided to officials in Finance's Budget Group in June 1999 highlighted the importance of ensuring all agencies established a revised Section 31 agreement by 1 July 1999, as follows:

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[53] A departmental item was defined to mean the total amount set out in the Schedule to the Appropriation Act in relation to an agency under 'Departmental Outputs'. An administered item was defined to mean an amount set out in the Schedule opposite an outcome of an agency under the heading 'Administered Expenses.'

> Due to changes in the FMA Act, the introduction of accrual accounting and devolved banking arrangements a new Section 31 agreement has been developed to account for these changes…Agencies are responsible for signing and returning to DOFA two copies of the signed Section 31 agreement by 1 July 1999. However, Budget officers should ensure that they have accounted for those FMA agencies for whom they are responsible.[54]

2.13 In June 1999, Finance advised all agencies covered by the FMA Act that:

> It is important that a new Section 31 agreement is in place between DOFA and the agency before 1 July 1999. This new agreement enables an agency to deposit Section 31 departmental receipts into its agency departmental bank account and to make payments from Section 31 departmental receipts for the purposes of the delivery of Departmental outputs.[55]

2.14 Finance also advised agencies that a further driver for establishing a new Section 31 agreement was to provide for the retention, and legal appropriation, of interest earnings received under the Agency Banking Incentive Scheme (ABIS), which was to operate in conjunction with agency transactional banking.[56]

2.15 In July 2005, Finance sought advice from AGS regarding how its departmental agreement executed in March 1999, to operate from 1 July 1998, might have operated if it had continued in operation beyond 30 June 1999.[57] AGS advised Finance that there were substantial doubts about whether such agreements could have operated at all beyond 1 July 1999 because they were not drafted so as to apply to the new concepts (such as 'departmental items'), which were incorporated into the Appropriation Acts after that date.[58]

2.16 AGS advised Finance that, while the 1998 agreement could continue to operate on its terms:

> We have given considerable thought to whether, and how, the 1998 agreement could be given continuing operation in the absence of some transitional

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[54] Budget Circular, *New Section 31 Arrangements for 1999–2000 and beyond*, Department of Finance and Administration, June 1999.

[55] Estimates Memorandum 1999/26, *New Section 31 Arrangements for 1999–2000 and beyond*, Department of Finance and Administration, 2 June 1999, p. 2.

[56] See Estimates Memorandum 1999/17, *Agency Banking Arrangements*, Department of Finance and Administration, 23 March 1999, p. 1.

[57] This issue had arisen because ANAO had found that a subsequent agreement for Finance, signed on 30 June 1999 to operate from 1 July 1999, was ineffective as the Finance official who signed that agreement did not hold the necessary delegation from the Finance Secretary to do so (see further discussion in Chapter 3). The June 1999 agreement had purported to replace the earlier agreement, but, if ineffective, would not have validly done so.

[58] In December 2005, Finance advised ANAO as follows: 'It was widely believed that "running costs" were conceptually equivalent to "departmental items" and, therefore, that earlier agreements could continue to operate after 1 July 1999. Discovery that this was an erroneous premise only occurred when AGS was consulted in July 2005 on another issue.'

> provisions that align the terms of that agreement with the new appropriations concepts that were introduced in 1999. However, it seems to us that to do so requires not merely a process of interpretation of the 1998 agreement but instead requires a process of rewriting the terms of that agreement, which is impermissible…Your question assumes that it was possible for the 1998 agreement to operate in the years following 1998–99. We have concluded that it could not have done so…

2.17 Based on this advice, Finance prepared its 2004–05 financial statements on the basis that its departmental agreement signed in March 1999 under the running costs arrangements could not operate past 30 June 1999.

2.18 Five agencies did not execute a revised agreement to operate from 1 July 1999, and continued for one or more financial years to rely on agreements that had been prepared in 1998–99 in terms that reflected the running costs arrangements.[59] Three of those agencies did not execute a further agreement until late 2004. The other two executed new agreements that operated from 30 April 2000 and 1 July 2000 respectively.

2.19 As advised by AGS, to the extent the running costs agreements were not replaced, they were able to continue to operate, but only on their terms. Based on the AGS advice to Finance, those agreements were not capable of causing the relevant sections of the annual Appropriation Acts to take effect for amounts received after 30 June 1999.

2.20 In summary, the five agencies purported to increase their respective annual appropriations by receipts totalling $9.86 million that had not been captured by an operative agreement. Each agency disclosed this issue in its 2004–05 financial statements. This circumstance resulted in one agency, AUSTRAC, spending $1.31 million without appropriation authority. Accordingly, that agency also disclosed breaches of Section 83 of the Constitution and Section 48 of the FMA Act. Figure 2.2 identifies the agencies, relevant periods, affected receipts and, where applicable, amounts spent without appropriation, as disclosed in their respective financial statements.

[59] Four of the five affected agencies were within the Attorney-General's portfolio, which were the responsibility of the same Agency Advice Unit within Finance's Budget Group.

Figure 2.2

Agencies with agreements unable to operate from 1 July 1999

Agency	Period with no operating agreement	Receipts not captured ($)	Receipts spent ($)
Administrative Appeals Tribunal	1 July 99 to 1 Dec 04	5 008 678	Nil
AUSTRAC	1 July 99 to 1 Dec 04	3 010 000	1 312 000
National Native Title Tribunal	1 July 99 to 30 April 00[A]	244 844	Nil
Office of Parliamentary Counsel	1 July 99 to 1 Dec 04	652 127	Nil
Office of the Commonwealth Director of Public Prosecutions	1 July 99 to 30 June 00	940 094	Nil
	Total	**9 855 743**	**1 312 000**

Note A: In July 2005, the National Native Title Tribunal advised ANAO that it had submitted an agreement intended to operate from 1 July 1999 to Finance on 22 June 1999 for execution by the Finance Minister's delegate, but did not receive a signed copy in return. There was no record of a signed version of that agreement in the documentation held by Finance.

Source: ANAO analysis.

Variation Instruments for 'no agreement' periods

2.21 In October 2005, the Minister for Finance and Administration sought the Prime Minister's agreement to a proposal to forgo recovery from the agencies identified in Figures 2.1 and 2.2 of the amounts collected during the periods not covered by a Section 31 agreement. The Minister advised the Prime Minister that, while these funds should technically be repaid to the OPA:

> If agencies were required to repay this money to the OPA, they would require additional funding, as their original appropriations were reduced by the amount of Section 31 revenue expected to be generated. I consider that, in this particular instance, agencies should not be required to repay the amounts in question. This approach obviates the circular process of funding agencies in order for them to repay the OPA. This proposal has been agreed with the Auditor-General subject to agreement from the Government not to recover the money collected.

2.22 On 9 October 2005, the Prime Minister agreed to the Minister's proposal, noting that:

> I agree with your proposal that agencies that mistakenly believed they had s31 agreements in place should not be required to repay monies collected. This is a sensible approach given that agencies would otherwise require further funding in order to repay the amounts in question to the OPA. I note the Auditor-General has agreed to this approach.

2.23 In order to give effect to the proposal not to recover the relevant amounts, it was necessary to provide for those receipts to be captured by an effective Section 31 agreement. This would also provide the relevant agencies with appropriation authority in respect of any unspent amounts still held, but would not remove past breaches of Section 83 of the Constitution that occurred due to agencies spending receipts not covered by a Section 31 agreement.

2.24 Accordingly, on 28 October 2005, the Finance Secretary executed two variation instruments (Variation Instruments 2 & 3) made under subsection 31(4) of the FMA Act.[60] Those instruments varied the current Section 31 agreements for 11 agencies, such that the amounts collected in the 'no agreement' period are eligible receipts for the purposes of the current agreement.[61] Both instruments came into effect on 8 November 2005, upon registration on the Federal Register of Legislative Instruments (which is discussed further in Chapter 4).

Purported use of Section 31 prior to having an agreement

2.25 Two further agencies, BoM and Centrelink, were identified as having spent Section 31 receipts prior to having an agreement in place (see Figure 2.3). The agreements executed for BoM on 8 June 2004 and Centrelink on 21 April 1999 provided for the retrospective capture of all receipts collected during the period each did not have an agreement. Accordingly, neither agency was included in Variation Instruments 2 & 3 relating to 'no agreement' periods.

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60 The *Financial Management and Accountability Net Appropriation Agreement Variation (No.2) 2005* (Variation Instrument 2*)* and the *Financial Management and Accountability Net Appropriation Agreement (Department of the Environment and Heritage) Variation 2005* (Variation Instrument 3). Two further instruments executed by the Finance Secretary in relation to amounts collected under ineffective agreements are discussed in Chapter 3.

61 The Department of the Environment and Heritage (DEH) absorbed the functions of the National Oceans Office (NOO) from 4 November 2004. Variation Instrument 3 varied DEH's current agreement to capture receipts retained by NOO from 1 July 2003 to 3 November 2004 in reliance on an expired agreement.

Figure 2.3

Agencies identified as spending receipts prior to executing an agreement

Agency	Period Affected	Receipts retrospectively captured ($)	Receipts spent without appropriation ($)
Bureau of Meteorology	12 Sep 02 to 7 June 04	28 614 611[A]	A total of $28 301 311 was spent without appropriation in 2002–03, including Section 31 receipts (see para 2.27 to 2.36).
Centrelink	1 July 98 to 20 April 99	1 558 356 385	1 558 356 385
	Total	**1 586 970 996**	**1 586 657 696**

Note A: Includes $701 093 and $442 842 incorrectly disclosed in 2002–03 and 2003–04 respectively as receipts credited to a non-existent Special Account.

Source: ANAO analysis.

2.26 Centrelink's 1997–98 agreement expired on 30 June 1998. A further agreement was not executed until 21 April 1999. Centrelink spent $1.56 billion in Section 31 receipts in the period 1 July 1998 to 20 April 1999, prior to an annotated appropriation becoming available in respect to those receipts.

Bureau of Meteorology

2.27 BoM was prescribed as an FMA Act agency on 12 September 2002. It took a considerable period of time to finalise the separation of BoM's financial affairs from those of the Department of the Environment and Heritage (DEH). This contributed to delays in finalising a Section 31 agreement. There were also periods in which progressing the agreement fell into abeyance.[62]

2.28 Although two earlier drafts had been signed on the agency side and submitted to Finance, a delegate of the Finance Minister did not execute an

[62] In this respect, BoM advised ANAO in April 2005 as follows: 'Although an agreed Section 31 agreement was not in place in 2002–03, work towards a S31 agreement commenced with Finance in the two months following Prescription. However, a version acceptable to Finance was not countersigned by Finance until June 2004. Issues contributing to the delay in finalising the S31 agreement were: Finance's reluctance to progress the S31 agreement until S31 issues relating to the Section 32 direction were resolved; debates about the inclusion of Bureau S31 receipts from 1 July 2002 to 11 September 2002; the date from which the S31 agreement should apply, 1 July 2002 or 12 September 2002; the pro-forma for the agreement and the handling of standard clauses which were modified several times by Finance in the process, and in particular, which resulted in the Bureau's S31 receipts for 2002–03 prior to Prescription being excluded in the very last draft, when the pressure for signing was intense, the authority of the Director of Meteorology (vis a vis the Minister) to sign the Bureau's S31 agreement.' Refer to paragraph 2.34 for further discussion in relation to this issue.

agreement for BoM until 8 June 2004.[63] Despite this, BoM reported the retention and spending of Section 31 receipts in its 2002–03 financial statements.

2.29 The agreement executed on 8 June 2004 included a clause that stated:

> This agreement allows the crediting of relevant receipts from 12 September 2002. However, expenditure of the receipts deemed to be appropriated cannot occur prior to the date this agreement has been signed by all parties.

2.30 In February 2004, Finance had requested that BoM confirm that it had not yet expended any of the amounts the agreement was intended to cover. On 11 March 2004, BoM advised Finance that:

> We can confirm that, at this stage, the Bureau has not spent public money since 12 September 2002 using unauthorised appropriations; i.e. we have enough unused appropriation and cash to cover our notional Section 31 expenditure for this, and the previous financial year. In relation to the previous financial year it should be recognised that for most of the period 12 September 2002 to 30 June 2003 the Bureau was in transition mode to operating as a Prescribed Agency and clearly worked within the existing arrangements and authorisations set up for DEH when it included the Bureau.

2.31 The advice appears to have been based upon a mistaken belief that, for some period after becoming a separately prescribed agency, BoM could continue to receive, and spend, independent receipts in reliance upon the Section 31 agreement in existence for DEH. That is not the case.

2.32 It was clearly identifiable from BoM's 2002–03 financial statements that it had already spent receipts to which the agreement executed in June 2004 was to be retrospectively applied. In that circumstance, ANAO considers that BoM could have applied greater scrutiny to its circumstances prior to the agreement being executed in its final form. In addition, it would have been appropriate for Finance and/or BoM to have obtained legal advice in relation to the retrospective application of an agreement to amounts already spent (as was also the case in relation to Centrelink in 1998–99). Both BoM and Finance could also have pursued completion of the agreement more vigorously.

2.33 In August 2005, BoM advised ANAO that:

> The absence of a properly signed agreement is not to say that there was not a meeting of minds in DoFA and the Bureau about a S31 agreement in 2002–03. The draft agreement signed by the Director of Meteorology in June 2003…had been verbally agreed within the Bureau and the [*Finance Agency Advice Unit*], and to our knowledge it was only the late recognition that the Director of Meteorology had not been delegated to sign the agreement that prevented

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[63] An agreement signed by the BoM Chief Executive in June 2003 was rejected due to the absence of evidence that the Chief Executive had been authorised by the relevant Minister. An Agreement signed by the Minister for the Environment and Heritage in November 2003 was rejected as it purported to commence on 1 July 2002, instead of the date of BoM's prescription as an agency, 12 September 2002.

DoFA signing it at that time. The substance of the agreement was not at issue. Given this consensus on the "substance" one wonders if the Bureau should be considered as having operated with a doubtful S31 agreement in 2002–03 and hence subject to the disclosures in financial statements agreed between ANAO and DoFA for such agreements.'

2.34 In this respect, ANAO notes that a Section 31 agreement must be properly executed in order to cause the relevant provisions of the annual Appropriation Acts to take effect. Irrespective of the reasons, an agreement for BoM was not properly executed until 8 June 2004 and, therefore, the requirements of Section 31 of the FMA Act were not satisfied until that time. BoM was aware that an agreement had not been executed and was not in a position to conduct its affairs as if it had been. The consequence of doing so was that it contravened Section 83 of the Constitution.

2.35 ANAO further identified that cash exceeding $25 million was transferred to BoM from DEH upon its prescription in September 2002 without the transfer of appropriation, via a direction made under Section 32 of the FMA Act, needed to enable BoM to spend that money.[64] As a result, both BoM and DEH misstated their available appropriation as at 30 June 2003 and 30 June 2004. BoM also reported payments totalling $417 128 in 2002–03 as having been made from a non-existent Special Account. As a result of these issues, together with the absence of a Section 31 agreement, BoM spent at least $28.3 million without appropriation in 2002–03.

2.36 Disclosures relating to these issues were included in the 2004–05 financial statements of BoM, DEH and Centrelink. In the case of BoM and Centrelink, breaches of Section 83 of the Constitution and Section 48 of the FMA Act were also reported.

Other agencies' use of retrospective agreements

2.37 ANAO noted many other examples of agencies retaining amounts received from non-appropriation sources prior to having a Section 31 agreement in place. However, no other instances of such amounts being spent without appropriation were identified within the scope of this performance audit. In most cases, the relevant agencies subsequently executed agreements that were expressed so as to apply retrospectively to amounts already received. The retrospective application of agreements is discussed further in Chapter 5.

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[64] Section 32 of the FMA Act provides the authority for the adjustment of appropriations on a change of agency function. That section applies if, for any reason, a function of an agency becomes a function of another agency. Under Section 32, the Finance Minister may issue one or more directions to transfer to the new agency some or all of an amount that has been appropriated for the performance of that function by the old agency. The authority to issue Section 32 directions has been delegated to Finance officials.

Transfer of Section 31 receipts received prior to a split of functions

2.38 Advice provided to Finance by AGS on 6 November 2002 was that:

> the section 32 transfer can include not only some or all of the amount originally appropriated (so far as it remains unspent) but also some or all of the amount or receipts added to an appropriation by means of a section 31 agreement and the net appropriation provisions (again, so far as that amount remains unspent).[65]

2.39 Included in the cash transferred to BoM from DEH were Section 31 receipts totalling $1.619 million that had been received between 1 July 2002 and 11 September 2002. Those receipts were specifically excluded from the amounts intended to be transferred to BoM via a Section 32 direction.

2.40 The alternative approach that was intended to be adopted in BoM's case was to provide for the transfer of the receipts by specifying those amounts as eligible receipts under BoM's Section 31 agreement. The transfer of appropriations upon a change in function does not appear to be an intended purpose of Section 31 agreements. Regardless, the eligible receipts identified in the agreement ultimately executed in respect of BoM did not include amounts received prior to 12 September 2002.

2.41 Finance's October 2005 response to Issues Papers provided by ANAO advised that:

> Historically, section 31 receipts have not been transferred as part of section 32 directions as such amounts are not necessarily recorded in Finance's cash and appropriation management systems. However, the issue of whether such receipts could, or should, be transferred is being considered as part of an internal review which is currently underway…Once this review is finalised, Finance will clarify its advice to agencies on this issue.

Section 31 arrangements for administered items

2.42 Since 1999–2000, the annual Appropriation Acts have marked all departmental appropriation items "net appropriation", but Section 31 arrangements have been applied to administered items on an exception basis. ANAO noted two areas in which that process might be improved.

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[65] That advice was provided in response to a request for comments on a draft Finance Circular dealing with the implementation of machinery of government changes. AGS recommended that Finance include a reference to this effect in the Finance Circular, such as: 'The unspent appropriation amount includes amounts of receipts relating to the performance of the function that have been added to an appropriation by means of a section 31 agreement and the net appropriation mechanism.' The *Guidelines for Implementation of Administrative Arrangements Orders and other Machinery of Government changes* issued by Finance in September 2003 included advice in relation to the adjustment of agency appropriations via Section 32 directions on a change of agency functions, but did not include reference to Section 31 receipts received prior to the change in function. In December 2005, Finance advised ANAO that it intends to detail appropriate procedures in the next version of the guidance, with new guidelines expected to be released in 2006.

Marking appropriation items "net appropriation"

2.43 In each year since 1999–2000, the Appropriation Acts have marked a small number of administered items as "net appropriation". In general, this occurred following consideration by Finance of advice from the relevant agency of particular circumstances which indicated that program administration and resource allocation may be improved through the establishment of Section 31 arrangements in relation to their administered item for a particular Outcome.

2.44 In that context, it is reasonable to expect that the items that are so marked provide the Parliament with an accurate reflection of the agencies that:

- expect to have administered receipts available for expenditure for the purposes of the nominated Outcome in that financial year; and
- will have the necessary arrangements in place to enable them to apply those receipts to the relevant Outcome.

2.45 ANAO's examination of the annual Appropriation Acts and agencies' administered Section 31 agreements identified that this has not been the case. Agencies have, in various years, had administered items marked "net appropriation" in the annual Appropriation Acts without also having an agreement in place that would allow them to increase those appropriation items for amounts received from non-appropriation sources. These are:

- Outcome 2 for DITR, "Enhanced economic and social benefits through a strengthened national system of innovation", in each financial year 1999–2000 to 2004–05;
- Outcome 1 for the Department of the Prime Minister and Cabinet (PM&C), "Sound and well coordinated government policies, programmes and decision making processes", in 1999–2000;
- Outcome 2 for Finance, "Improved and more efficient government operations". In the only year that the administered item for Finance's Outcome 2 was marked "net appropriation" (2000–01), the department did not have a relevant agreement in place. In June 2002, Finance entered into a Section 31 agreement purporting to cover administered receipts in respect of Outcome 2 from 6 June 2002, but the appropriation item was no longer marked "net appropriation"; and
- Outcome 2 for the Attorney-General's Department (AGD), "Coordinated federal criminal justice, security and emergency management activity, for a safer Australia". The administered item for AGD's Outcome 2 was marked "net appropriation" in *Appropriation Act (No.3) 2004–05*. AGD did not have an administered agreement in place in 2004–05. AGD advised ANAO that it had not executed an

administered agreement because Finance had arranged for the wrong administered outcome to be marked "net appropriation", with a similar error occurring in *Appropriation Act (No. 1) 2005–06*.

2.46 Those agencies did not report any administered Section 31 receipts in any of the relevant years. For Finance, this included its Outcome 3, "Efficiently functioning Parliament", in respect of which it did have both a marked administered item and an administered agreement. Issues relating to Finance's disclosure of administered Section 31 receipts in respect of Outcome 3 are discussed in Chapter 4.

2.47 ANAO considers that there is scope for the processes surrounding the identification of administered appropriation items that are to be marked "net appropriation" to be improved. In this context, ANAO notes that Outcome 2 for DITR was removed from the administered appropriation items marked "net appropriation" in *Appropriation Act (No.1) 2005–06*. Also, a revised administered Section 31 agreement executed for Finance on 30 June 2005 excluded its Outcome 2.[66] In December 2005, Finance advised ANAO that:

> It has been Finance's practice to restrict application of section 31 agreements specifying administered items and…where the retention of specific receipts is justified, Finance will take measures to ensure more care is taken to correctly identify items in the Appropriation Acts and the agreements.[67]

Appropriation not available until Act receives Royal Assent

2.48 Administered appropriation items in respect of four agencies were marked net for the first time in *Appropriation Act (No.3) 2004–05*. That Act received Royal Assent on 1 April 2005. Three of those agencies have executed a Section 31 agreement relating to administered receipts, as follows:

- the Department of Family and Community Services (FaCS) entered into a revised agreement on 13 December 2004 that encompassed administered receipts. That agreement stated that it commenced on 1 October 2004;
- DFAT executed an administered agreement on 21 December 2004, to apply to amounts received from 25 February 2004; and
- DIMIA executed a revised agreement on 4 November 2004 encompassing administered receipts received from 1 July 2004.

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66 The capacity for that agreement to operate is discussed further in Chapter 4.

67 Finance further advised that all agencies are asked to provide detail on their administered section 31 agreements prior to finalisation of each appropriation Bill for ordinary annual services. This is done at least twice each year by means of the regular Estimates Memoranda (for example, Estimates Memorandum 2005/47, *2005–06 Additional Estimates – Appropriation Documents*).

2.49 An agreement may stipulate a commencement date and may also provide that it applies to amounts received from an earlier date. However, until the Appropriation Act in which the relevant item is marked "net appropriation" has received Royal Assent, agencies are not able to legally increase that appropriation item for amounts received, or spend those amounts.

2.50 At least one agency, FaCS, did not establish appropriate receipting and appropriations management procedures so as to ensure it did not purport to credit amounts to its administered appropriation item prior to having the legal authority to do so. In the context of the 2004–05 annual financial statement audit process, ANAO identified that FaCS had incorrectly retained administered receipts received from other agencies, and applied them to reduce its administered expenses, prior to having the necessary arrangements in place to enable it to do so.[68]

2.51 The administered agreements executed by each of the three agencies included a note advising that:

> This agreement is given effect by specific provisions within the annual appropriation Acts. Therefore, the agreement only has effect while the relevant specific provisions exist in the annual appropriation Acts.

2.52 However, the agreements did not include specific reference to the need for the relevant Appropriation Act to gain Royal Assent before the agreement could cause the agency's appropriation to be increased for amounts received.[69] Given the significance of agencies ensuring that no receipts are added to their appropriation, or spent, prior to all necessary arrangements being in place, there would be benefit in future agreements incorporating more explicit reference to this requirement in the clause specifying when the agreement will commence operation.

2.53 In December 2005, Finance advised ANAO that it has acknowledged the importance that agencies do not add receipts to their appropriations, or

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[68] See ANAO Audit Report No.56 2004–05, *Interim Phase of the Audit of Financial Statements of General Government Sector Entities for the Year Ending 30 June 2005*, Canberra, 24 June 2005, p. 153. That report noted that: 'FaCS has commenced a thorough review of administered receipts to detect and take corrective action where receipts have been incorrectly recorded against expenses.'

[69] The receipts to be captured by the DFAT administered agreement had been held in a Special Account pending the establishment of Section 31 arrangements. In August 2005, DFAT advised ANAO that, once an administered Section 31 agreement was executed, the moneys were transferred to its administered appropriation. The agreement stated that it commenced upon signature, which occurred on 21 December 2004. However, any transfer of funds would not have had legal effect in relation to increasing DFAT's administered appropriation item until the Appropriation Act received Royal Assent on 1 April 2005. In December 2005, DFAT confirmed to ANAO that the department did not receipt any moneys against the agreement until Royal Assent was granted. DFAT advised ANAO that the first receipt against the agreement did not occur until 20 April 2005, and that the moneys that were held in the Special Account were transferred on 26 May 2005.

spend those receipts, prior to all necessary arrangements being in place. Finance further advised that it agreed with ANAO's findings in this respect, and that it had taken steps to ensure that future agreements will incorporate a more explicit clause stating that the agreement (or applicable part of it) will commence from the date that the relevant Appropriation Act gains Royal Assent.

Identifying eligible receipts

2.54 The FMA Act does not provide guidance as to the type of receipts that may be included in Section 31 agreements. In this regard, legal advice provided by AGS in June 2005 was as follows:

> The language of section 31, and that of the provisions of the annual Appropriation Acts, is extremely broad and non-prescriptive. The only express restrictions on the terms and operation of a section 31 agreement in relation to the amounts that may be credited to an appropriation item are (i) that the agreement must specify the receipts that may be credited; and (ii) the increase in the appropriation item cannot be greater than those specified receipts.[70]

Change to inclusive approach to specifying eligible receipts

2.55 As was discussed in Chapter 1, prior to the FMA Act, the annual Appropriation Acts specified the types of receipts to which net appropriation arrangements could apply. *Appropriation Act (No.1) 1997–98*, which was the last time this occurred, defined five sources from which eligible receipts could be received.[71] The Act listed the eligible receipts in exclusive terms. The Ministers could not agree to the retention, as net appropriations, of amounts received from any other sources. Similar provisions had been included in the Appropriation Acts in previous financial years.

2.56 In 1998, Finance developed a template for use by agencies in making net appropriation agreements under Section 31 of the FMA Act. Figure 2.4 sets out the eligible receipts clause of the template. Although the template was amended to accommodate changes in the appropriations framework introduced on 1 July 1999, the same basic approach to specifying eligible receipts was used in all Section 31 agreements made until late 2004.

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[70] In respect to the latter, ANAO notes that the increase in appropriation cannot be greater than the amounts actually received by the agency in respect of the receipts specified in the agreement.

[71] They were: (a) the sale, leasing or hiring out of, or other dealing with, goods or other personal property; (b) the sale of real property used for the purpose of providing staff residential accommodation or from the leasing of real property for that purpose; (c) the provision of services; (d) a person (*employee*) appointed or employed by, or performing services for, the Commonwealth as payment for any benefit provided (whether to the employee or another person) in respect of the appointment or employment of, or the services performed by, the employee; or (e) from the sub-leasing of real property, or the resale of goods used in fitting out premises, under a property resource agreement between the Minister and the Minister responsible for the relevant agency (Section 8).

Figure 2.4

Eligible receipts clause included in the template used for Section 31 agreements from 1998 until August 2004

4. Nature of Eligible Receipts

4.1 The nature of the receipts which may be made available to the agency include, but are not limited to the following:

4.1.1 **Category A** subsidy and grant monies received from approved employment subsidy schemes or programs, eg, such as Job Network service providers

4.1.2 **Category B** net receipts from "user charging" activities (as defined in Estimates Memorandum 1995/21 at page 4 and 5), eg:

4.1.2.1 from the sale, leasing, hiring out of, or other dealing with, goods or personal property;

4.1.2.2 from the provision of services;

4.1.2.3 from a person ("employee") appointed or employed by, or performing services for, the Commonwealth as payment for any benefit provided (whether to the employee or another person) in respect of the appointment or employment of, or the services performed by, the employee; and

4.1.2.4 from the sub-leasing of real property, or the resale of goods used in fitting out premises, under a property resource agreement between the Department of Finance and Administration and the agency.

4.1.3 **Category C** other net receipts of an administrative nature, eg:

4.1.3.1 from the sale of departmental assets[A];

4.1.3.2 from insurance recoveries; and

4.1.3.3 from net interest on the balances of "Departmental" bank accounts and term deposits.[B]

Notes:

[A] This item was added from 1 July 1999, replacing 'receipts from the sale of real property used for the purpose of providing staff residential accommodation or from the leasing of real property for that purpose', which had previously been one of the receipts specified in the annual Appropriation Acts.

[B] This item was added from 1 July 1999 to accommodate the receipt of interest under ABIS.

Source: Template for net appropriation agreements made under Section 31 of the FMA Act provided to agencies by the Department of Finance and Administration.

2.57 A significant change included in the template was the introduction of an inclusive, rather than exclusive, approach to identifying the receipts that were eligible to be added to an agency's appropriation. Three broad categories of eligible receipts were identified, with examples of the types of receipts that would fall under each category. The examples shown included the five sources previously identified in the Appropriation Acts.

2.58 Net appropriation agreements made under the previous arrangements had also grouped eligible receipts into similar categories, but each category was expressed in exclusive terms. In comparison, the receipts that would be considered to be eligible under each category in the template developed for Section 31 agreements were not limited to the examples listed. Further, the

receipts that could be made available to the agency were not restricted to the identified categories.

2.59 Accordingly, agreements could be interpreted to cover a very broad range of receipts. This was most evident with the use of the phrase 'other net receipts of an administrative nature' to describe a group of eligible receipts (identified as Category C in the template). The term 'receipts of an administrative nature' was not defined for the purposes of Section 31 agreements. This approach significantly reduced the precision with which eligible and ineligible receipts could be identified.

2.60 Uncertainty in this regard was further increased by the different approaches taken over time to the need for a particular type of receipt to be identified as an example under the relevant category in order to be considered eligible. Finance and/or the relevant agency have, from time to time, sought to amend or replace existing agreements so as to specifically list an additional type of receipt under the relevant category.[72] However, in other cases, agencies have obtained legal advice confirming that the broad and non-exhaustive nature of the categories shown in agreements allowed them to retain receipts that were not specifically listed. For example, in November 2001, one agency received legal advice that:

> In our view, categories B and C are defined in inclusive terms. It is not necessary for a receipt to match one of the given examples, provided it satisfied the overall description given to the category of receipts that are intended to be covered. Thus, all amounts which satisfy the description of being receipts for 'user charging' activities would be covered by category B, and all amounts which satisfy the description of being 'other' receipts of 'an administrative nature' would be covered by category C…When read in context with category B, which deals with receipts from 'user charging' activities, in our view category C is intended to cover amounts which are received by [*the agency*] in respect of all other departmental (ie. not administered) activities other than 'user-charging' activities.

2.61 In that context, the category-based approach did not assist in providing a robust framework in relation to agencies' use of Section 31 to increase their annual appropriations. An agency could potentially add any type of receipt to its appropriation, provided it could be shown to fit within one of the broadly

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[72] For example, in March 1999, Finance advised all agencies that their agreement would need to be updated to provide for the retention of, and legal appropriation of, interest earned on departmental bank accounts following the introduction of agency transactional banking and ABIS (see Estimates Memorandum 1999/17, *Agency Banking Arrangements*, 23 March 1999). As noted in Figure 2.4, the revised template issued by Finance for the making of agreements commencing 1 July 1999 specifically identified interest earned on departmental bank accounts as an example of an eligible receipt.

expressed categories, without the retention of such receipts having been considered by the Finance Minister or his delegate.[73]

2004 revised template

2.62 In 2004, Finance reviewed the template used for the preparation of Section 31 agreements. In February 2005, Finance advised ANAO that:

> The review was considered timely, as most of the existing Section 31 agreements were five years old. Since these agreements were executed, there have been a number of changes to the Administrative Arrangements Orders and the nature of the activities conducted by some agencies. Following the passage of the *Legislative Instruments Act 2003* and its commencement on 1 January 2005 these agreements have been classified as 'instruments' for the purposes of the Act. In practical terms, this means that all Section 31 agreements will be publicly available on the Federal Register of Legislative Instruments. The requirement to register documents such as Section 31 agreements prompted Finance to devise a more easily understood format.

2.63 The revised template, issued in August 2004, removed the concept of non-exhaustive categories. Agencies are now expected to specify the types of receipts that they will be able to add to their appropriations through their Section 31 agreement. By 30 June 2005, all agencies had executed a revised agreement using the new template.

Commonly required receipt types

2.64 The new template initially provided to agencies contained a list of seven suggested eligible receipts, which have been included in most agencies' current agreements.[74] As agencies negotiated new agreements, additional types of common receipts were identified. They were:

- receipts from the transfer of annual leave entitlements between agencies (the original template only identified long-service leave);

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[73] For example, in 2003–04, BoM retained $119 793 in interest earned on money held in a contractor's trust account for civil and property works to be undertaken. Payments into this fund are treated by BoM as advances, with the interest received from this account being treated as a Section 31 receipt under a 'Miscellaneous' clause included in its previous Section 31 agreement. However, following the abolition of ABIS from 1 July 2003, it is the Budget, not agencies, that are exposed to an interest loss from payments made in advance of requirements. Regardless of the validity or otherwise of retaining these amounts, the Bureau's revised agreement executed on 24 June 2005 makes no provision for amounts of this nature to be retained by BoM.

[74] Receipts from the sale, leasing, hiring out of, or other dealing with goods; Receipts from the provision of staff and other services; Receipts from a person (whether employed, appointed, or performing services for, the Commonwealth) as payment for any associated benefit provided (whether to that person or another person); Receipts from the sale of minor assets that are departmental in nature such as furniture and fittings; Receipts from the transfer of long–service leave entitlements between agencies; Subsidy and grant moneys received as a result of participation in employment subsidy schemes or programs; and Court awarded costs to the extent to which they reflect legal costs incurred in litigating the matter.

- amounts received from the Australian Taxation Office (ATO) as interest on a late repayment of Goods and Services Tax (GST);
- sponsorships, grants, subsidies and contributions received to fund departmental activities;
- donations received, expressed to be for the performance of specific departmental activities;
- financial incentives to enter into leasing arrangements; and
- amounts received in relation to the ADF Reserves Employer Support Payment Scheme.

2.65 Agencies that had completed their new agreement prior to these additional receipt types being identified will not be able to retain such amounts, unless their agreement is amended. Agencies that retained similar receipts under the broad terms of their previous agreement will need to revise their receipting procedures to ensure they no longer include those amounts in their reported Section 31 receipts.[75]

2.66 Finance issued a revised template, incorporating the additional receipts, on 30 June 2005 under Finance Circular No. 2005/07. ANAO noted three agencies that have subsequently executed revised agreements to include additional receipts from the revised template.[76] In October 2005, Finance advised ANAO that most of the agreements that were executed prior to December 2004 had been reviewed, and that a minority were in the process of being reviewed by the Budget Group of Finance in conjunction with individual agencies.[77]

Improved clarity and precision

2.67 The revised approach has provided an improvement in the clarity and precision with which the receipts that an agency is entitled to retain can be identified. It will be important that agencies ensure that receipts that were

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[75] For example, the Section 31 receipts reported by DIMIA in 2003–04 included $10 798 relating to interest received from the ATO on late GST refunds. The revised agreement executed for DIMIA in November 2004 does not identify interest on late GST refunds as an eligible receipt.

[76] The ATO, the Department of the Treasury (Treasury) and PM&C. In PM&C's case, the agreement was also varied to include specific reference to receipts from various Special Accounts. That issue is discussed further later in this Chapter.

[77] As noted, the original template referred to the transfer of long service leave entitlements, but Finance subsequently identified a requirement for agencies to also include the transfer of annual leave entitlements. ANAO noted two agreements that did not include annual leave entitlements as an eligible receipt. ANAO further noted that Finance Circular No. 2005/07 and the revised template issued on 30 June 2005 both included only the transfer of long service leave entitlements. In October 2005, Finance advised ANAO that it has now made the necessary change to the template to include annual leave entitlements, and that it has, with the concurrence of the two affected agencies, subsequently varied their agreements to include this clause.

arguably covered by the broad nature of their earlier agreements, but which are no longer specifically identified as eligible receipts, do not continue to be included in their reported Section 31 receipts. In this respect, Finance advised ANAO in February 2005 as follows:

> While the previous template adopted a category-based approach to comprehensively cover receipts, the revised template is more explicit in the types of receipts that are included. This approach provides enhanced clarity around the receipts covered by the agreements. Finance has made it clear that agencies negotiating a Section 31 agreement need to have a thorough understanding of the receipts which might be considered for inclusion, to ensure that amounts are not expended without an appropriation.

2.68 Alternative options for the future role of Section 31 agreements, including in respect to the specification of eligible receipts, are discussed in Chapter 5.

Eligibility of notional amounts debited from Special Accounts

2.69 An area in which there has been continuing uncertainty in identifying eligible Section 31 receipts has been in relation to amounts debited from Special Accounts managed by the relevant agency. These notional intra-agency transactions usually relate to the agency charging a fee for services provided to the Special Account, or being reimbursed for amounts initially paid out of its departmental appropriation for activities relating to the purposes of the Account.

2.70 In order for an agency's annual appropriation to be increased for such amounts, the notional 'payment' received from the Special Account must be able to be treated as both:

- an 'eligible receipt' for the purposes of its Section 31 agreement; and
- a 'relevant receipt' for purposes of the net appropriation provisions of the annual Appropriation Acts.[78]

2.71 A number of agencies have had a practice of including amounts debited from internally managed Special Accounts in the Section 31 receipts added to their annual appropriations.[79] Despite this, there is ongoing uncertainty as to whether both of those conditions have been satisfied.

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[78] Those provisions provide that the amount by which an appropriation item can be increased by operation of a Section 31 agreement 'cannot be more than the relevant receipts covered by the agreement'. The purpose for which the amount is debited from the Special Account must also be within the purposes of the Account as specified in the determination, or Act, establishing the Account.

[79] For some agencies, the amounts involved appear to be significant. For example, advice provided to Finance by DEH in June 1999 indicated that the majority of its Section 31 receipts (estimated at that point to be $11.7 million for 1998–99) related to payments from the Natural Heritage Trust. Transactions of this nature have occurred in subsequent financial years.

DCITA October 2003 legal advice

2.72 This issue was first raised in the course of an ANAO performance audit of the management of Special Accounts.[80] One agency, the Department of Communication, Information Technology and the Arts (DCITA), sought legal advice in response to issues identified in the course of that audit. The October 2003 advice to DCITA from AGS was that given the broad terms in the department's then Section 31 agreement, it was arguable that transactions of this nature could be regarded as an eligible receipt for the purposes of the agreement. However, AGS further advised that:

> A more debatable point is whether the crediting of the [*Special Accounts*] involved any 'receipt' for the purposes of the Section 31 Agreement and the related provisions of the FMA Act and the annual Appropriation Acts. In this respect, the debiting of the Special Accounts and the crediting of the departmental appropriation amounted to an intra-agency transaction.
>
> It is unclear whether the relevant provisions of the annual Appropriation Acts and FMA Act governing Section 31 Agreements contemplate or recognise intra-Agency payments and receipts. Section 6 of the FMA Act can be read as recognising intra-Agency transactions and requiring such transactions to be treated in the same way as real transactions. Specifically, section 6(1) provides that the Act applies to a notional payment by an Agency, *or part of an Agency*, as if it were a real payment by the Commonwealth.[81]
>
> In contrast, the annual Appropriation Acts do not expressly recognise transactions within an Agency as a relevant transaction (cf. a provision such as section 5 of the *Appropriation Act (No. 1) 2001–2002* which provides that '[*F*]or the purposes of this Act, notional transactions between Agencies are to be treated as if they were real transactions). Accordingly, it is doubtful whether a crediting to a departmental appropriation involves a relevant 'receipt'.

2.73 The January 2004 report of the Special Accounts performance audit included DCITA's response to ANAO on this issue, which in part advised:

> The Department considers that Finance should consider amending the relevant provisions of the annual Appropriation Acts and the FMA Act governing Section 31 Agreements to enable a Special Account to be debited and an annual appropriation credited where the debit and credit are for a purpose within the purposes of the Special Account.[82]

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[80] See ANAO Audit Report No.24 2003–04, *Agency Management of Special Accounts*, Canberra, 30 January 2004, pp. 74–75.

[81] ANAO notes that section 6(2) of the FMA Act further provides, relevantly, that the Act applies to a notional receipt by an Agency (or part of an Agency) of such a notional payment as if it were a real receipt by the Commonwealth.

[82] ANAO Audit Report No.24 2003–04, op cit., p.75.

2.74 Two other agencies, Finance and PM&C, sought further legal advice from AGS on this issue in 2005, in response to issues identified in this respect in this performance audit.

Finance April 2005 legal advice

2.75 The Section 31 receipts disclosed by Finance in 2003–04 included a number of transactions relating to amounts debited from internally managed Special Accounts. Finance's Section 31 agreement did not identify such amounts as eligible receipts. In response to ANAO queries regarding this practice, and given the earlier legal advice provided to DCITA, Finance sought clarification of this issue from AGS. In April 2005, Finance was advised as follows:

> having considered the matter closely, we think the better view is that the agreement under section 31 can extend to notional intra-Agency payments and receipts, and that the reference to 'relevant receipts covered by the agreement' in the annual Appropriation Acts extends to all receipts covered by the agreement including intra-agency receipts. …the expression 'relevant receipts covered by the agreement', as used in section 10 of the annual Appropriation Act, directs attention to the section 31 agreement itself and the proper interpretation of its terms. Where the particular section 31 agreement clearly extends to notional intra-agency receipts (as, in light of section 6 of the FMA Act, it can) there is no compelling basis, as a matter of ordinary language, to read 'relevant receipts covered by the agreement' as excluding those receipts.

2.76 The circumstances in which AGS advised that the reference to 'relevant receipts' in the annual Appropriation Acts would extend to amounts debited from Special Accounts was where the particular Section 31 agreement clearly extends to notional intra-agency receipts (emphasis added). No such clear provision was included in any agency's agreement until after issuance of Finance Circular No. 2004/09.

2.77 Until September 2005, none of Finance's Section 31 agreements, including revised agreements executed in April and June 2005, had identified amounts received from Special Accounts as an eligible receipt.

PM&C 2005 legal advice

2.78 In the course of this audit, ANAO noted that the PM&C Secretary had advised the Prime Minister in November 2004 that the department retains revenues from other sources of around $2 million annually, including $1.2 million from the Campaign Advertising Special Account (which varies from year to year depending upon the volume of campaign advertising).

2.79 In July 2005, ANAO queried with PM&C the basis on which amounts of this nature had been included in the Section 31 receipts added to its annual appropriation.

2.80 In October 2005, PM&C advised ANAO that its advice from AGS was:

> The AGS legal advice supports the view that the previous Section 31 agreement is broad enough to allow the Department to acknowledge the [*intra agency*] transfer from the [*Campaign Account Special Account (CASA)*] into the Departmental account…AGS advised that it was arguable that clause 5.1.2 of the [*Department's*] Section 31 agreement [*that applied for the period February 2005 to September 2005*] ("Receipts for the provision of staff and other services") would extend to include these transactions in relation to salary expenses in providing "services" for the purposes of the CASA…
>
> However, the AGS also suggest that there still remains considerable ambiguity about whether these [*intra-agency*] transactions are actually a "receipt" for Section 31 purposes. The legal advice suggests the FMA Act and the Appropriation Act provide conflicting opinions. To quote:
>
> > "…section 6 of the FMA Act recognises [*intra-agency*] transactions and requires such transactions to be treated in the same way as real transactions. However, the standard provisions in the annual Appropriation [*Acts*] dealing with section 31 agreements (e.g. section 10 of the Appropriation Act (No.1) 2004–05), do not expressly recognise transactions within an Agency as a relevant transaction."[83]
>
> It appears that while this level of ambiguity exists, it is difficult to determine whether the Department actually has a "receipt" for section 31 purposes, and more importantly, whether a section 31 breach has actually occurred.

2.81 Another agency, the Department of Agriculture, Fisheries and Forestry (DAFF), similarly advised ANAO that it considered, given the broad terms of its Section 31 agreement signed in 1999, transactions of this nature that it undertakes in respect to the Natural Resources Management Account were within the scope of eligible receipts covered by the Section 31 agreement.

Special Account transactions included in agreements

2.82 In August 2004, Finance Circular No. 2004/09 advised agencies to be aware that where they receive notional payments, including from a Special Account, these receipts should be identified in the agreement if they are to be spent, including cases where the Special Account and the appropriation are managed by the same agency.[84] This advice was reiterated in Finance Circular No. 2005/07 issued on 30 June 2005.

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[83] In December 2005, PM&C provided ANAO with a copy of this legal advice. It is relevant to note that the legal advice concluded that the better view is that: 'a section 31 agreement can extend to notional intra-agency payments and receipts. First, the expression 'relevant receipts covered by the agreement' as used in provisions such as section 10 of the annual Appropriation Acts directs attention to the section 31 agreement itself and the proper interpretation of its terms. Where the particular section 31 agreement extends to notional intra agency receipts (as, in light of section 6 of the FMA Act, it can) there is no compelling basis, as a matter of ordinary language, to read the reference in the annual Appropriation Acts to 'relevant receipts covered by the agreement' as excluding those receipts.'

[84] Finance Circular No. 2004/09, op. cit., paragraph 12.

2.83 Revised agreements executed with seven agencies since August 2004 have specifically identified, as eligible receipts, amounts debited from a nominated Special Account(s) managed by that agency. The agencies are:

- Australia-Japan Foundation (Australia-Japan Account);
- DAFF (Natural Resources Management Account)[85];
- DEH (Natural Heritage Trust of Australia Account, Ozone Protection and Synthetic Greenhouse Gas Account, and Water Efficiency Labelling and Standards Account);
- DCITA (Untimed Local Call Access Account, Television Fund Account and Other Trust Moneys Account). DCITA's agreement was varied on 30 November 2005 to include receipts from the Art Rental Special Account for the provision of services[86];
- Department of Transport and Regional Services (Rural Transactions Centre Account);
- Department of the Treasury (Australian Government Actuary Special Account);
- PM&C (Campaign Advertising Special Account, Services for Other Governments and Non Agency Bodies Account and Other Trust Moneys Account). A revised agreement for PM&C, which identified amounts received from three Special Accounts as eligible receipts, was executed on 27 September 2005; and
- Finance. A further revised departmental agreement for Finance was made on 26 September 2005 to specifically include amounts debited from Special Accounts as eligible receipts.

2.84 Of the affected agencies, only DCITA's agreement included a provision such that it applied to amounts previously received from the nominated Special Accounts.

2.85 In 2003–04, Finance increased its departmental appropriation by at least $1.853 million for amounts debited from Special Accounts. This amount was excluded from the Section 31 receipts re-credited to Finance's annual

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[85] DAFF advised ANAO that: 'While we are of the view that the Natural Resources Management Account transactions were within the scope of eligible receipts detailed in the 1999 agreement, they were nevertheless specifically requested to be included as eligible receipts in the new 2005 agreement by the Department of Finance and Administration.'

[86] See *Financial Management and Accountability Net Appropriation Agreement (Department of Communications, Information Technology and the Arts) Variation (No.2) 2005*. As a transitional provision, the agreement was also varied to provide that, before the commencement of a Determination establishing the Art Rental Special Account, this eligible receipt clause would be taken to refer to the Artbank Account.

appropriation on 30 June 2005 under operation of a Variation Instrument executed by the Finance Secretary in relation to 'ineffective' agreements (see Chapter 3). No adjustment was made to exclude any amounts received from Special Accounts in any earlier years, despite such amounts having been previously included in Section 31 receipts.

2.86 In October 2005, Finance advised ANAO that, while it agreed transactions of this nature should be avoided where there is no provision in the Section 31 agreement, it did not agree that previous transactions should be reversed. In December 2005, Finance advised that:

> This was on the basis of legal advice initially provided to DCITA in October 2003, which stated that receipts from Special Accounts can be covered in Section 31 agreements, even where no clause specifically mentioned the Special Account (as long as they met the definition of "eligible receipt" under another clause). Finance has subsequently adopted a specific clause as an example of best practice for the purposes of avoidance of doubt.

2.87 The specification of Special Account transactions as an eligible receipt for the purposes of an agency's Section 31 agreement does not overcome the continuing uncertainty as to whether such internal transactions can be 'relevant receipts' for the purposes of the net appropriation provisions of the annual Appropriation Acts.

2.88 The uncertainty in respect to these transactions does not contribute to the orderly management and governance of appropriations. This is particularly the case in light of the significant amounts that are involved in some agencies. ANAO considers that there would be considerable benefit in Finance taking the necessary steps to remove such uncertainty. If it is the intention that the provisions of the annual Appropriation Acts should recognise payments within an agency as real transactions, then amending the relevant provision of the Acts to make this clear would resolve the current uncertainty.

Recommendation No. 1

2.89 In order to provide certainty as to the capacity of amounts debited from internally managed Special Accounts to be captured by agencies' Section 31 agreements, ANAO *recommends* that the Department of Finance and Administration take the necessary steps to align the provisions relating to notional transactions in the annual Appropriation Acts with those set out in Section 6 of the *Financial Management and Accountability Act 1997*.

Agency responses

2.90 Finance agreed with qualification, advising that it will give policy consideration to this recommendation and to whether such transactions should be included in Section 31 agreements. All other agencies that responded to this

recommendation agreed (see Appendix 2). In agreeing to the recommendation, agencies commented as follows:

- Australian Centre for International Agricultural Research (ACIAR):

  ACIAR would welcome the clarification in relation to Special Accounts and Section 31 Agreements to ensure our current reporting continues to be accurate.

- DEH:

  The effective operation of specific DEH programmes relies on the ability to have eligible and relevant receipts from the Natural Heritage Trust of Australia Account, Ozone Protection and Synthetic Greenhouse Gas Account, the Water Efficiency Labelling and Standards Account and other special accounts that may exist from time to time.

- Department of the Senate (DoS):

  Such a review should also include the Appropriation (Parliamentary Departments) Acts.

Consistency with Government decisions

2.91 On a number of occasions, various agencies have received legal advice that, in general terms, where an agency receives an amount to which its Section 31 agreement applies, the relevant annual appropriation item is automatically increased by the amount received. For example, in November 2001, AGS advised one agency as follows:

> The effect of the [*agency's*] s.31 agreement is that in respect of any amount received by [*the agency*] which falls within the kinds of amounts (or receipts) covered by the agreement, and in accordance with any conditions set out of the agreement, the departmental item appropriation for [*the agency*] is increased. An amount equal to the amount of money received by [*the agency*], necessarily part of the CRF when it is received, is automatically and immediately appropriated to [*the agency*]. To that extent, [*the agency*] 'retains' the money.

2.92 On that basis, the terms of the annual Appropriation Acts make the deeming of an appropriation in respect of relevant receipts, and the commensurate increase in the relevant appropriation item, automatic at the time eligible amounts are received.[87] In that context, it is important that the

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[87] See for example, the *Agency Banking Framework – Guidance Manual*, Fourth Edition, issued by Finance in October 2003, which states: 'Departmental receipts relating to departmental items are deposited into official departmental bank accounts where covered by a net appropriation agreement (established under Section 31 of the FMA Act) with Finance. Items that are covered by such an agreement are deemed to be appropriated at the time of receipt…Where a section 31 agreement applies to an administered item, the relevant receipts are deposited into official administered receipts bank accounts. Items that are covered by such an agreement are deemed to be appropriated at the time of receipt.' (pp. 7 and 8).

provisions specifying which types of receipts are relevant receipts for the purposes of the Appropriation Acts are framed in terms that are consistent with relevant Government decisions regarding the funding that is to be made available to the relevant agency. Where that is not the case, a disconnect will arise between those decisions and the appropriation that is legally available to an agency.

Defence property sale program

2.93 For example, from 2000–01, annual targets for proceeds from the Defence property sale program have been set in the Budget context. The Budget target figure was required to be returned to the CRF. Defence could retain any amount generated above the target figure. However, Defence's Section 31 agreements that operated between 1 July 1999 and 29 June 2005 identified receipts from the sale of departmental assets as an eligible receipt. Those agreements included no limit on the amount of those receipts that would be added to Defence's appropriation by operation of the agreement and the relevant annual Appropriation Acts.

2.94 Consequently, all property sale proceeds were automatically appropriated to Defence upon receipt. As a result, the deemed appropriation provided to Defence by operation of its Section 31 agreement was greater than the amount the Government had decided should be available to it, by $473.5 million in 2002–03 and $82.4 million in 2003–04. Those amounts were included in the Section 31 receipts disclosed by Defence as being added to its annual appropriation in those financial years.

2.95 Defence advised ANAO that the amounts required to be returned to the Budget in each year had been transferred to the OPA, with those transfers being included in the amounts disclosed as payments made from its departmental appropriation. This treatment effectively overstated the extent of Defence's expenditure from its available appropriation in each financial year.

2.96 Legal advice provided to ANAO by AGS in 2002 was that a transfer of money into the OPA would probably not be a transfer 'between Agencies' for the purposes of section 5 of the Appropriation Acts.[88] In the view of AGS, the transfer of the proceeds of asset sales to the OPA was probably not required to be debited to an agency appropriation. AGS advised that:

> If this produces an unsatisfactory result for accounting purposes, it would be open to vary the section 31 agreement so that there is no extant appropriation to the value of the money which has been returned to the OPA.

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[88] Section 5 of the Annual Appropriation Act (No. 1) provides that, for the purposes of the Act, notional transactions between agencies are to be treated as if they were real transactions. One of the effects of this section is that a payment from one agency to another will be debited from an appropriation of the payment agency, even though no payment is actually made from the CRF.

2.97 The revised Section 31 agreement executed for Defence on 30 June 2005 included provisions that addressed this issue in regard to the proceeds from the property sales program. The agreement specifically provides that the amount or percentage of receipts from the sale of land and buildings by which Defence's appropriation item will be taken to be increased is subject to a determination made by Government as part of the property sales program.[89]

Foreign exchange risk management policy

2.98 Another example identified involved $16.5 million relating to net foreign exchange gains that was included in the Section 31 receipts reported by Defence in 2003–04. It could be argued that receipts of that nature were eligible under Defence's previous broadly expressed agreement as receipts of 'an administrative nature'. However, as part of the annual Budget process, Defence's appropriation is adjusted to account for losses or gains that result from movements in the foreign exchange parameters.[90] This arrangement was continued under the Revised Government Foreign Exchange Risk Management Policy that commenced on 1 July 2002.[91]

2.99 Under the Budget supplementation arrangements applying to Defence, a net gain arising from movements in foreign exchange parameters is required to be returned to the Budget. A net loss will result in supplementation of Defence's appropriation in the following financial year. For Defence to separately increase its appropriation for net foreign exchange gains through the Section 31 process is inconsistent with the existing Government policy on foreign exchange risk management. This view is supported by the absence of any reference to foreign exchange gains in the eligible receipts identified in the revised Section 31 Agreement for Defence executed on 29 June 2005.

2.100 In December 2005, Finance advised ANAO that this is an area that agencies should pay close attention to in the administration of Section 31 agreements to ensure they remain consistent with Government decisions.

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89 The revised agreement also identified receipts from the sale of specialist military equipment as an eligible receipt. The agreement provides that Defence is entitled to retain such receipts (net of sales costs) up to a threshold of $1 million per item (and for Grouped items $5 million), with proceeds above this threshold to be returned to the CRF 'unless otherwise determined by Government'. Unlike for proceeds from property sales, this caveat was not included in the clause stipulating the percentage of eligible receipts by which Defence's appropriation item will be taken to be increased. Accordingly, there is less clarity as to whether a formal variation of the agreement would be required before any such Government decision would take effect to change the amount of deemed appropriation for these receipts.

90 The Commonwealth Budget and constituent agency budgets are prepared on the basis of economic parameters developed by Treasury, including exchange rate parameters.

91 See Finance Circular No. 2002/01, *Foreign Exchange (FOREX) Risk Management*, 26 June 2002 and *Guidelines for the Management of Foreign Exchange Risk*, Department of Finance and Administration, November 2002, p. 7.

Cash management processes for Section 31 receipts

2.101 Prior to 1 July 1999, agency Section 31 receipts were centrally held in the OPA. To access those funds, agencies had to request Finance to issue an additional Agency Appropriation Advice to the relevant annotated appropriation item, and submit payment instructions to the Finance Information on Resource Management (FIRM) system, recording the expenditure against the relevant appropriation item. The Agency Appropriation Advices issued by Finance detailed the Section 31 receipts deemed to have been appropriated to each agency.[92]

Changes under agency transactional banking

2.102 Changes to those processes arose in July 1999, when agencies became responsible for establishing and maintaining their own bank accounts and processing their payments and receipts. From that time, departmental appropriations as set out in the annual Appropriation Acts were drawn from the OPA through CAMM. However, the annotated appropriation available to agencies through Section 31 receipts was not recorded through CAMM. Departmental receipts were deposited directly into agency bank accounts and could be retained until spent. As a result, the central appropriation management system no longer provided agencies with a complete record of their available appropriation at a given point in time. In this respect, Finance advised agencies that:

> From 1 July 1999, agencies will need to account for and monitor expenditure of their Section 31 receipts to ensure that appropriation does not exceed aggregated net receipts.[93]

2.103 In that context, the cash management processes applied following the introduction of agency transactional banking increased the scope for agencies to retain, and potentially spend, Section 31 receipts prior to having the necessary arrangements in place.

2.104 Minor changes were made to these arrangements on 1 July 2003, following the recommendations of the Budget Estimates and Framework Review (BEFR). BEFR resulted in agency departmental drawdowns occurring on an 'as needed' basis, with agencies maintaining a working cash balance. Finance advised agencies that:

> Section 31 receipts will not be reported in CAMM. Material Section 31 receipts will be accounted for by agencies advising Finance through monthly

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92 In the case of DFAT, ABS (see Figure 2.1) and Centrelink (see Figure 2.3), this process did not operate effectively to prevent the spending of Section 31 receipts in the absence of an agreement.

93 Department of Finance and Administration, Estimates Memorandum 1999/26, *New Section 31 Arrangements for 1999–2000 and beyond*, June 1999.

statements. Agency issues relating to Section 31 receipts will be considered as part of the process to agree working cash balances. However, CAMM will provide agencies with an option of transferring Section 31 receipts into the OPA (therefore recording the receipts in CAMM against a specific nominal account) for cash management purposes and drawing on these funds on an as needed basis.[94]

2.105 Finance advised ANAO in February 2005 that an optional separate ledger account was also available in CAMM for recording receipts relating to administered Section 31 agreements. Finance further advised that, during 2003–04, only one agency (the then Aboriginal and Torres Strait Islander Services) used this facility.

2.106 The *Agency Banking Framework Guidance Manual* issued in October 2003, following BEFR, advised agencies that, where they were covered by a Section 31 agreement, receipts relating to departmental items were to be deposited into official departmental bank accounts. The Manual further advised that if agencies were unable to immediately identify receipts, then they must deposit the funds into an administered receipts account until clearly identified.[95] In October 2005, Finance advised ANAO that this requirement meant that, where receipts could not be identified as Section 31 receipts (as would be the case where an agreement has not been executed), agencies were to deposit those receipts into an administered receipts account.[96]

2.107 ANAO noted examples where this requirement was not followed. For example, in addition to relevant agencies identified in Figures 2.1 and 2.3:

- The Inspector-General of Taxation (IGT) was prescribed in the FMA Regulations of 1 July 2003, and established on 7 August 2003. A Section 31 agreement for IGT was not executed until 17 February 2005. IGT's 2003–04 financial statements reported $246 682 in non-appropriation receipts as having been retained as at 30 June 2004, none of which had been spent as at 30 June 2004. In December 2005, IGT advised ANAO that 90 per cent of those receipts related to the transfer of long service and other entitlements of staff engaged to establish the new agency.
- The National Blood Authority (NBA) became a prescribed agency on 1 July 2003, but a Section 31 agreement was not executed until

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94 Department of Finance and Administration, Estimates Memorandum 2003/22, *Budget Estimates and Framework Review – Cash Management Arrangements for 2003–04*, 6 June 2003.

95 *Agency Banking Framework — Guidance Manual*, Fourth Edition, Department of Finance and Administration, October 2003, p. 7.

96 In December 2005, Finance further advised ANAO that earlier editions of the Agency Banking Framework Guidance Manual, issued in July 1999 and January 2002, also provided advice about Section 31 agreements.

7 March 2005. NBA's 2003–04 financial statements disclosed cash of $1 006 861 as being held in excess of its available appropriation, none of which had been spent as at 30 June 2004. The financial statements noted that the funds had been recognised as a payable to the Commonwealth, pending a final review and decision on the agency's Section 31 agreement. NBA advised ANAO that, pending receipt of a duly authorised agreement, it had held the funds in the NBA bank account.[97]

2.108 Both IGT and NBA subsequently executed agreements that were expressed to apply retrospectively to the amounts already received. In recognising the amounts received during the period in which it did not have an agreement as a liability to government, NBA adopted a better practice in terms of its disclosure of the relevant amounts. However, the long-term retention of funds in excess of an agency's legal appropriation is not a sound practice.

Revised cash management systems

2.109 In February 2005, Finance advised ANAO that:

> A project is currently underway to develop a system to replace AIMS [*the Accrual Information Management System*] and CAMM. The treatment of both departmental and administered Section 31 receipts is being addressed as part of the design and implementation phases of the project, with a view to increasing Finance's monitoring capability. Agencies will continue to be responsible for:
>
> - the correct recording and reporting on Section 31 receipts;
> - their spending from the resulting appropriation; and
> - ensuring that amounts spent are in accordance with their Section 31 agreement (eg. with regard to revenue sharing with the budget).

2.110 From 1 July 2005, Finance commenced the introduction of the replacement for CAMM, the Appropriation and Cash Management module (ACM) of the Central Budget Management System. CAMM and ACM were initially operated in parallel.

2.111 In October 2005, Finance advised ANAO that agencies are responsible for ensuring that expenses are met from their appropriations and that it is not Finance's responsibility to monitor these transactions. However, Finance also advised ANAO that the ACM module provides it with the ability to only allow processing of Section 31 receipts in ACM once the existence of a valid agreement has been verified. Finance advised ANAO that:

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[97] A further example noted by ANAO related to amounts included in the Section 31 receipts reported by Defence in 2003–04. These were receipts totalling $318 000 for which the relevant details identifying the nature of the receipt were not available.

> Agencies without a section 31 agreement will be unable to record receipts as section 31 receipts for funds transferred to the Official Public Account, and will, therefore, be unable to draw on those receipts.

2.112 In June 2005, Finance advised agencies that, while they could initially continue to retain Section 31 receipts in departmental bank accounts, they would be required to provide monthly advice to Finance regarding the amount of receipts processed through their account.[98] Finance further advised that:

> From 1 August 2005, ACM will provide the functionality to automatically increase the appropriation limit for all Administered and Departmental s31 receipts recorded in ACM according to the conditions in the s31 agreement. It is ultimately intended that all Departmental s31 receipts will be deposited into the OPA upon receipt and be drawn out again via Departmental draw downs processed in ACM. Consultation with agencies about the processes surrounding this will commence during early July 2005.[99]

2.113 Once fully implemented, this process should provide for improved control over agencies retaining and/or spending amounts received from non-appropriation sources prior to having relevant Section 31 arrangements in place.

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[98] Estimates Memorandum 2005/30, *Central Budget Management System (CBMS): Phased Implementation and Cutover Arrangements*, Department of Finance and Administration, 28 June 2005, p. 3.

[99] ibid.

3. Establishing Effective Section 31 Agreements

This chapter discusses the authority under which agency and Finance officials may be signatories to Section 31 agreements, and the outcomes of an assessment of the effectiveness with which the Section 31 agreements examined in this audit were executed.

Legislative requirements

3.1 Significant Constitutional consequences result from the operation of Section 31 agreements. Specifically, Section 31 of the FMA Act provides a mechanism by which an agency may obtain an appropriation authorising it to retain and spend amounts received from independent sources. It is in this context that the issue of who can execute a Section 31 agreement, and in what capacity, must be considered.

3.2 The FMA Act specifies who may enter into net appropriation agreements, as follows:

> 31(1) The Finance Minister may enter into agreements for the purposes of items in Appropriation Acts that are marked "net appropriation".
>
> 31(2) In the case of items for which the Finance Minister is responsible, the agreement is to be made with the Chief Executive of the Agency for which the appropriation is made. In all other cases, the agreement is to be made with the Minister who is responsible for the item.[100]

3.3 That is, there are two signatories to a Section 31 agreement – one on the whole-of-government (Finance Minister) side and one on the agency (responsible Minister or, for Finance portfolio agencies, Chief Executive) side. Both signatories must have the necessary authority in order for an agreement to be effectively executed in accordance with the legislative requirements.

Who has signed Section 31 agreements?

3.4 Delegations and authorisations play a key role in the Westminster system of public administration. They are the mechanism by which, in certain circumstances, officials may be provided with the authority to exercise a statutory power that the Parliament has vested in another individual or office-holder. Just how well departments and other agencies administer their

[100] For the purposes of the FMA Act, 'Minister' includes Presiding Officers (Section 5, FMA Act).

delegations and authorisations is crucial to how efficiently government operates.[101]

3.5 There are three main ways in which the devolution of authority can be achieved:

- An express power to delegate: Legislation may expressly provide a statutory procedure for the devolution of a power. This most commonly takes the form of an express power to delegate the power to another person in writing;
- An express power to appoint an authorised officer: Some legislation expressly provides for the appointment of 'authorised officers', or the authorisation of persons, to exercise specified statutory powers; and
- An implied power to authorise: Where legislation does not expressly provide a person in whom a statutory power is vested with the power to delegate or to authorise others to exercise the statutory power for, and on behalf of, that person, they may, in some circumstances, be able to rely on an implied power to authorise. Such a power is commonly referred to as the '*Carltona*' principle.[102]

3.6 The manner in which a delegate[103] of an office-holder exercises the power in question is fundamentally different from that of someone who is authorised by an office-holder to exercise a power on his or her behalf. A delegate exercises a delegated power by applying their own discretion and acts in their own capacity, not that of the person who delegated the power to them. In contrast, the act of an authorised person is, at law, an act of the person in whom the power is vested. A person exercising a power for, and on behalf of, another does so as the 'alter ego' of the person in whom the power is vested.[104]

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[101] Legal Briefing Number 74, *Delegations, authorisations and the Carltona principle,* Australian Government Solicitor, 14 December 2004, p.1.

[102] That principle, established in *Carltona Ltd v Commissioners of Works* [1943 2 ALL ER 560], applies, in certain circumstances, to infer to a Minister a power to authorise officials to exercise, on the Minister's behalf, a power vested in the Minister, despite the absence of an express power to delegate or authorise. AGS has advised that, in *Carltona*, the court's reasoning indicates that there are two grounds which justify inferring such a power to a Minister, as follows:

- the Minister is ultimately responsible to the Parliament for the decision of an authorised official; and
- in modern government, Ministers have so many functions and powers, administrative necessity dictates that they act through duly authorised officials (Source: Legal Briefing Number 74, op. cit., p.7.)

[103] Or statutory authorised officer.

[104] Legal Briefing Number 74, op. cit., pp. 2 and 6.

Finance Minister's side of Section 31 agreements

3.7 Reflecting the key role the Finance Minister and Finance play in the Commonwealth's financial framework, the FMA Act requires that the Finance Minister be a party to all Section 31 agreements. In addition, the Finance Minister may, at any time, cancel or vary an agreement without the consent of the other party.

Agreements signed by the Finance Minister

3.8 The Finance Minister signed two of the 231 agreements examined by ANAO, being:

- one agreement relating to Finance's departmental appropriation item; and
- another agreement relating to Finance's administered appropriation item for its Outcome 3 ("Efficiently functioning Parliament").

3.9 The Minister signed these agreements on 29 June 2005. The Finance Secretary signed them on the agency side on 24 June 2005.[105] On this occasion, Finance considered it prudent to have the Minister and Secretary sign the agreements because of doubts about the effectiveness of earlier Finance agreements signed by officials. In December 2005, Finance advised ANAO that this was because ANAO had questioned the effectiveness of earlier agreements and resolution of the broader issue, that officials could sign the agreements, was not reached prior to the execution of the new agreements.[106]

Agreements signed by Finance officials

3.10 Finance officials sign the whole of government side of almost all Section 31 agreements. Section 62 of the FMA Act provides the Finance Minister with an express power to delegate to an official, by written instrument, any of the Minister's powers or functions under the Act, except the power to make Orders. Successive Finance Ministers have, in accordance with Section 62, delegated their powers and functions under the FMA Act to the Finance Secretary, including the powers in relation to Section 31.

3.11 Under Section 53 of the FMA Act, the Finance Secretary may delegate to an official in any agency any of his or her powers and functions under the Act, including powers or functions that have been delegated to the Secretary by the Finance Minister. Successive Finance Secretaries have, in accordance

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[105] Each agreement commenced on 29 June 2005.

[106] Finance relied on the 29 June 2005 departmental agreement for annotating its departmental item until it was replaced to specifically include amounts debited from certain Special Accounts as an eligible receipt. Finance officials signed the revised agreement on 26 September 2005. See Chapter 4 for further discussion regarding Finance's administered agreement.

with Section 53, sub-delegated the Finance Minister's powers under Section 31 to Finance officials in specified positions.

3.12 Section 53 requires that the delegation of powers to officials by the Finance Secretary be by way of written instrument. In the absence of a written instrument identifying the power being delegated and the persons or positions to whom that power is delegated, there is no lawful basis on which a person other than the Finance Minister or Finance Secretary may execute the whole-of-government side of Section 31 agreements.

Agency side of Section 31 agreements

3.13 On the agency side, the significant majority of agreements made to 30 June 2005 were signed by an official of the relevant agency, rather than the responsible Minister or, for Finance portfolio agencies, Chief Executive.

3.14 Of the 209 agreements examined by ANAO for agencies with appropriation items for which the Finance Minister was not responsible:

- the responsible Minister signed 17 (eight percent);[107]
- the Chief Executive of the relevant agency signed 99 (47 per cent); and
- agency officials at levels below the Chief Executive signed 93 (45 percent).

3.15 The relevant Chief Executive signed nine of 22 agreements made in respect of agencies with appropriation items for which the Finance Minister was responsible. Officials below the Chief Executive signed the other thirteen. In December 2005, Finance advised ANAO that, in many cases, the agency officials at levels below Chief Executive that signed agreements were Chief Financial Officers, or similarly senior officials, with overall responsibility for the financial management of the agencies concerned.

Most officials must be authorised, rather than delegated, to sign agreements

3.16 The Chief Executives of agencies with appropriation items for which the Finance Minister is responsible have an express power to delegate to officials in their agency, by written instrument, their power to make Section 31 agreements with the Finance Minister.[108] The Treasurer and Attorney-General are also able to delegate to officials their power, as the responsible Minister under subsection 31(2), to make Section 31 agreements with the Finance

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[107] Fifteen of those had been executed since August 2004.

[108] This derives from the express power to delegate provided by Section 53 of the FMA Act. Section 29 of the Auditor-General Act also provides the Auditor-General with an express power to delegate, by written instrument, any of the Auditor-General's powers or functions under any Act to an FMA official.

Minister.[109] AGS has advised that other Ministers administering the same relevant legislation as the Treasurer and Attorney-General also have a power of delegation.[110]

3.17 However, there is no power for other Ministers to delegate their power under subsection 31(2) to enter into Section 31 agreements with the Finance Minister. Nor is there any express power for Ministers to authorise a person to exercise that power for and on their behalf, or the required form any such authorisation should take. This is in contrast to the *Auditor-General Act 1997* (Auditor-General Act) and the *Commonwealth Authorities and Companies Act 1997* (CAC Act), passed as part of the same package of financial framework legislation as the FMA Act, both of which provide explicit powers for written authorisations.

3.18 Relying on the *Carltona* principle, AGS has advised agencies that, on balance, a Minister does have an implied power to authorise officials to enter into Section 31 agreements for and on behalf of the Minister. These advices have acknowledged that some of the factors (such as administrative necessity), that are usually present where the *Carltona* principle is relied on, may not be applicable in the context of Section 31 agreements. For example, advice provided to one agency in April 1998 noted that:

> it is not clear that 'administrative necessity' makes it impractical for a responsible Minister to *execute* a s.31 agreement personally, given that the Minister would not often be required to enter into such agreements.

3.19 However, the April 1998 advice concluded that, on balance, a Section 31 agreement could be signed by the Chief Executive of the agency involved for and on behalf of the responsible Minister, in reliance upon the *Carltona* principle. In December 2005, Finance advised ANAO that:

> The April 1998 advice was provided four months after the commencement of the *Financial Management and Accountability Act 1997*, and dealt only briefly with the issue of a Minister's implied power to authorise officials. Subsequently, in June 2005, AGS was asked to give full consideration to the issue and to provide a detailed opinion.

3.20 In June 2005, AGS advised Finance that:

> Since 1998, AGS has not departed from this view. We have consistently advised that it would be open to a Minister to authorise a person to act on his or her behalf in entering into s.31 agreement.

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[109] Section 62A of the FMA Act provides the Treasurer with an express power to delegate, by written instrument, his or her powers under the FMA Act. The *Law Officers Act 1964* provides the Attorney-General with an express power to delegate, in writing, his powers under all or any of the laws of the Commonwealth or a Territory to the Secretary to the Attorney-General's Department or to the person for the time being holding or performing the duties of the office specified in the instrument of delegation.

[110] Under Section 19A of the *Acts Interpretation Act 1901*.

> Given the doubts that have been expressed by the ANAO over the legality of Ministers authorising officials to enter into s.31 agreements we have re-examined that issue. That re-examination has led us to the conclusion that there is no significant doubt that a Minister may authorise an official to enter into a s.31 agreement on his or her behalf.[111]

3.21 Agreements are made for individual agencies on an infrequent basis. Including the most recent round of renewal of agreements for all agencies, ANAO identified 150 agreements executed between 1 January 1998 and 30 June 2005 for 54 agencies whose Minister did not have a delegation power. This represents an average of 2.8 agreements per agency over more than seven years. Accordingly, ANAO considers that, in light of the Constitutional significance of a Section 31 agreement, there is much to be said for agencies seeking to have such agreements signed by the relevant Minister. ANAO notes that this practice had been adopted in relation to two of six agreements executed between July and October 2005.

3.22 Having the responsible Minister sign Section 31 agreements may also reflect the expectations of Parliament, given the terms of the Section. In this respect, the Clerk of the Senate has commented to ANAO as follows:

> Until agreements were tabled in the Senate under the Legislative Instruments Act, which came into effect at the beginning of [*2005*], there was no ready way of ascertaining who had signed the agreements. I am quite sure that senators remain unaware of who signs them, and, if any assumption is made, assume that they are signed by ministers in accordance with the apparent effect of section 31.

3.23 In December 2005, Finance advised ANAO that the Federal Register of Legislative Instruments now provides information regarding the content of, and signatories to, Section 31 agreements in a transparent manner.

Implied and express authorisation

3.24 Where the *Carltona* principle applies in relation to a particular function or power of a Minister, an important qualification to its operation is that the Minister's surrogate must be appropriately qualified to act on the Minister's behalf. Authority to so act may arise through an express authorisation from the Minister, or impliedly from the nature of the power or function.

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[111] AGS further advised that, in its view, it is open to the Treasurer and Attorney-General to elect to either exercise their express power to delegate or, relying on the *Carltona* principle, authorise an appropriate official to exercise their power under Section 31 on their behalf. In October 2004, the Treasurer provided agency heads in his portfolio with an Instrument of Authorisation to enter into agreements on his behalf; whereas the Attorney-General provided agency heads in his portfolio with an Instrument delegating his powers under Section 31 (the first occasion on which such a delegation had been made by the Attorney-General).

Chief Executives are impliedly authorised

3.25 The Chief Executive of the relevant agency (as defined by Section 5 of the FMA Act) is considered to be an appropriate person to enter into significant Constitutional documents of this kind on their Minister's behalf. This is based upon the Chief Executive's responsibilities, under the FMA Act, for the financial management of the agency.[112] Further, as has been noted by AGS, where the Chief Executive concerned is also Secretary of a Department, or head of an executive agency established under Section 65 of the *Public Service Act 1999*, the Chief Executive is responsible for managing the agency, and is accountable to the government, the Parliament and the public.

3.26 On the above basis, AGS advice is that a Chief Executive can reasonably act on the basis that he or she is impliedly authorised to enter into Section 31 agreements on behalf of the Minister. Of the 231 agreements examined by ANAO, 49 (23 per cent) were signed by agency Chief Executives in reliance upon an implied authorisation from the relevant Minister.

3.27 Despite the existence of an implied authorisation, it is better practice for agencies to seek a written instrument from the responsible Minister expressly authorising the Chief Executive to enter into Section 31 agreements on the Minister's behalf. In this respect, legal advice provided to ANAO in July 2005 was that:

> We think that it is desirable for there to be a formal document delegating the Minister's power under s 31 or authorising the Chief Executive Officer to act on the Minister's behalf for the purposes of entry into an agreement. Having regard to the significance of s 31 agreements, we think it undesirable that the Chief Executive Officer's power to act be left to implication. We would not, however, say that such an implication could not be drawn from the section and the course of the Minister's dealings in relation to the operation of the section. It is just that it is inappropriate to leave it open to argument whether the power was properly exercised.

3.28 Seeking the Minister's express authorisation also provides the Minister with an appropriate opportunity to consider whether he or she would prefer to exercise their power under Section 31 personally or, if not, whether he or she wishes to place any limitations or restriction on the exercise of the power by the Chief Executive. The importance of this was well illustrated by the express authority provided by the Prime Minister in November 2004 to certain agency heads in his portfolio to sign Section 31 agreements on his behalf. The Instrument of Authority explicitly provided that:

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[112] Section 44 of the FMA Act requires a Chief Executive to manage the affairs of the agency in a way that promotes efficient, effective and ethical use of the Commonwealth resources for which the Chief Executive is responsible.

> This authority is limited to routine and non-controversial changes to existing agreements. My authority is to be obtained for more substantive changes.

Officials below Chief Executive do not have an implied authority

3.29 Legal advice provided to both Finance and ANAO in June and July 2005 respectively was that officials who are not agency Chief Executives are not impliedly authorised to exercise the power to enter into Section 31 agreements on the Minister's behalf.

3.30 Consequently, such officials require an express authorisation from the relevant Minister in order to be empowered to sign a Section 31 agreement (as set out in Figure 3.1). AGS has advised that the Minister may give such an express authorisation either in writing or orally. Where an authorisation is given orally, normal recordkeeping and accountability obligations would require that the relevant officials make and retain a written record of having received such authorisation, the date on which it was received, and any terms or conditions attaching to the Minister's authorisation.

3.31 The first guidance from Finance to agencies on entering into Section 31 agreements was provided in May 1997. This guidance[113] stated as follows:

> An official must not enter into an agreement under s.31 of the FMA Act unless he/she has been authorised by the Minister to do so.

3.32 Ministerial authorisation was also addressed in Finance Circular No. 2004/09 of August 2004. This Circular provided the following guidance to agencies on the requirement for an express authorisation from the responsible Minister before entering into Section 31 agreements:

> …the agency's responsible Minister must enter into the agreement, unless the Minister has explicitly authorised the agency's Chief Executive, in which the case, the Chief Executive may sign on behalf of the Minister. Where a Chief Executive is authorised by a minister, it would be prudent that this occur in writing.[114]

3.33 On 30 June 2005, that Circular was replaced by Finance Circular No. 2005/07, in which the guidance to agencies on authorisations from Ministers was amended slightly, as follows (the change is underlined):

> …the agency's responsible Minister <u>should</u> enter into the agreement, unless the Minister has explicitly authorised the agency's Chief Executive, in which case, the Chief Executive may sign on behalf of the Minister. Where a Chief

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[113] Included in the model set of Chief Executive Instructions (CEIs) produced by Finance to assist agencies in developing their own CEIs to be issued following the commencement of the FMA Act.

[114] Finance Circular No. 2004/09, op. cit., p. 3.

Executive is authorised by a Minister, it would be prudent that this occur in writing.[115]

3.34 In addition, Finance Circular No. 2005/07 included enhanced guidance on the execution of Section 31 agreements. This included guidance in respect to the execution clause (signature block) to be used. ANAO had identified errors in that respect in a number of the agreements examined.

Recommendation No.2

3.35 ANAO *recommends* that, before entering into future Section 31 agreements:

(a) all signatories establish the capacity in which they may legitimately sign the agreement, and correctly identify that capacity in the agreement;

(b) where it is intended that an official will be entering into the agreement, rather than the holder of the statutory power, agencies take steps to obtain written authorisations or delegations (where available) from the responsible Minister (or, for Finance portfolio agencies, Chief Executive); and

(c) delegates of the Finance Minister satisfy themselves that the agreement has been signed by the responsible Minister or an agency official who holds a current authorisation or delegation, as appropriate, from the responsible Minister (or, for Finance portfolio agencies, Chief Executive).

Agency responses

3.36 All agencies that responded to this recommendation agreed to relevant parts (see Appendix 2). In agreeing to the recommendation, agencies commented as follows:

- Australian Federal Police (AFP):

  The AFP has had a valid Section 31 Agreement since 7 December 2004.

- Department of Education, Science and Training (DEST):

  Before entering into future Section 31 Agreements the Department will put processes in place to ensure that:

  - all signatories have established the capacity in which they may legitimately sign the agreement;
  - the capacity is correctly identified in the agreement; and

[115] Finance Circular No. 2005/07, op. cit., p. 2.

- where an official enters into the agreement, rather than the holder of the statutory power, written authorisation from the Minister has been obtained.

- Family Court of Australia:

  The Section 31 Agreement signed by the Court in October 2004 complies with the recommendation, and the Court will continue to comply with regard to future Section 31 Agreements.

- Finance:

  Parts (a) and (b) of the recommendation reflect the best practice advice issued in the relevant Finance Circular (2004/09, subsequently replaced by 2005/07). With respect to part (c) of the recommendation, Finance has implemented practices, set out [*in*] internal guidance material, with the result that recent agreements have been signed by Ministers or appropriately authorised or delegated officials.

Assessing the effectiveness of Section 31 agreements

3.37 A Section 31 agreement that has been effectively executed in accordance with the legislative requirements is a necessary prerequisite for agencies to obtain an annotated appropriation for amounts received from non-appropriation sources. In this context, as part of the development of the Commonwealth's current financial framework, it was recognised that:

> Performance of public sector responsibilities is flawed if there is no realisation that those responsibilities inherently include the obligation to act legally and ethically.[116]

3.38 As part of this performance audit, ANAO sought to assess whether increases in agencies' annual appropriations made under authority of Section 31 of the FMA Act were supported by effective agreements. In addressing and resolving the issues that were identified, legal advice was obtained by Finance, some agencies and ANAO. Most of the advice was obtained from AGS.

3.39 On 26 August 2005, Finance provided Chief Financial Officers (CFOs) of FMA Act agencies with copies of two AGS legal advices obtained jointly by ANAO and Finance in August 2005. Finance also provided CFOs with a further copy of advice obtained by Finance from AGS in June 2005. These advices provided information regarding assessing whether Section 31 agreements had been effectively executed.

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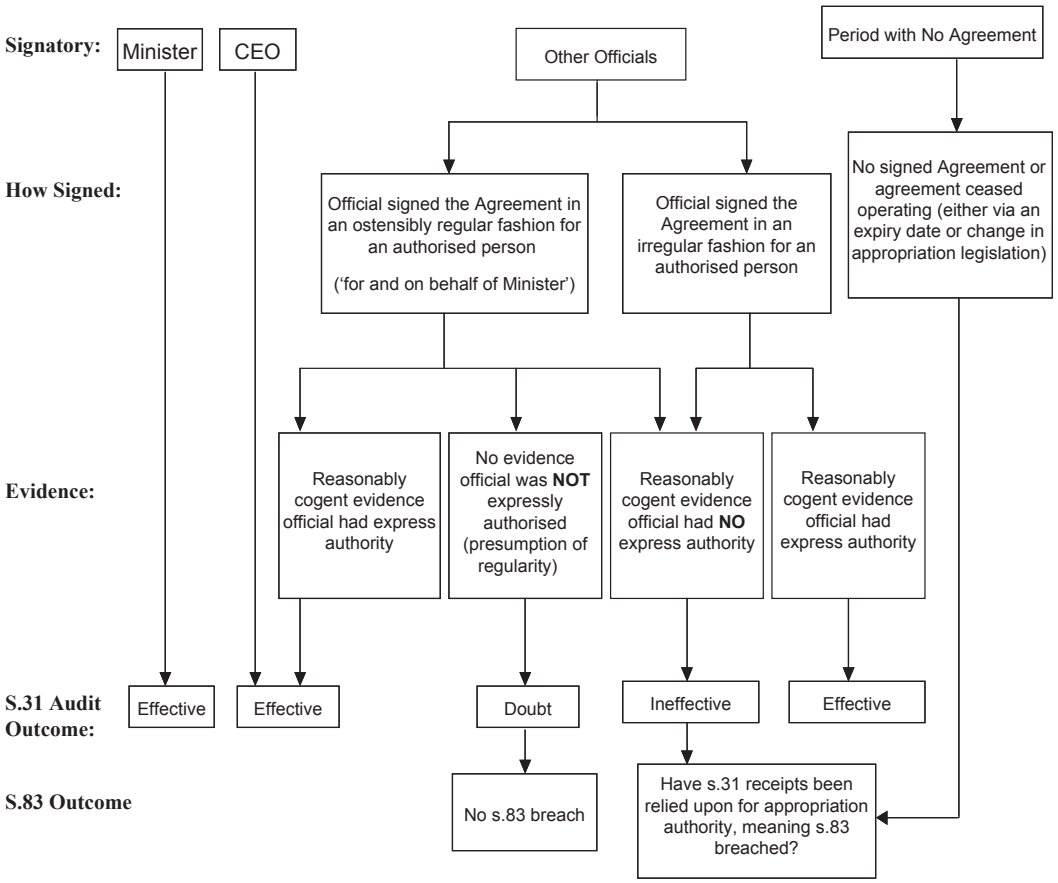
[116] Mr Maurie Kennedy, then Assistant Secretary Accounting Policy Branch, Department of Finance, *Changing Legislation and Financial Concepts to Achieve Accountable Management*, 20 May 1992, p. 2.

3.40 Finance also provided CFOs with a diagram, prepared by ANAO and Finance, that summarised all the recent advice from AGS on assessing the effectiveness of Section 31 agreements, and the related consequences in terms of Section 83 of the Constitution (see Figure 3.1). Prior to it being issued, AGS confirmed that the diagram fully reflected the AGS position.

Figure 3.1

Summary of AGS advice on assessing effectiveness of Section 31 agreements and related consequences



Source: Legal advice provided to Finance and ANAO by AGS in June and August 2005.

Summary of assessment outcomes

3.41 The 231 agreements examined by ANAO[117] were assessed against the decision tree of AGS advices set out in Figure 3.1 in order to form a conclusion as to whether they had been effectively executed by both signatories.[118] Of the 231 agreements examined, 157 (68 per cent) were assessed as effective.[119]

3.42 The 125 agreements signed by the responsible Minister or the relevant agency's Chief Executive (or an official acting in that capacity) were, consistent with legal advice provided to Finance, relevant agencies and ANAO, all assessed as having been effectively executed by the agency. However, seven of these agreements were assessed as being 'ineffective', due to the Finance official who signed on the whole-of-government side not holding the necessary delegation from the Finance Minister, leaving 118 effective agreements.

3.43 Officials at levels below the Chief Executive signed the agency side of the remaining 39 agreements that were assessed as effective. In each case, the relevant agency was able to provide evidence confirming that the official had been expressly authorised or, where relevant, delegated by the responsible Minister (or agency Chief Executive for agencies in the Finance Portfolio) to enter into the agreement. Finance was also able to demonstrate that the Finance official who signed each of those agreements held the necessary delegation from the Finance Minister.

3.44 On the basis of evidence and advice provided by the relevant agencies and Finance in respect to substantiating the authority of their respective signatories, the remaining agreements were assessed as follows:

- 42 agreements (18 per cent) (including the seven agreements noted above) were assessed as 'ineffective'; and
- 32 agreements (14 per cent) were assessed as 'in doubt'.

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[117] Contemporaneous with this performance audit, ANAO assessed the effectiveness of its own Section 31 arrangements. This revealed that ANAO did not have an effective agreement in place in the period 1 July 1998 to 15 November 2004. Disclosure of the affected receipts was made in ANAO's 2004–05 financial statements (Note 23). None of the receipts had been spent. All affected receipts have been captured by ANAO's current agreement.

[118] As noted, for a Section 31 agreement to be effective, both signatories must have the necessary authority to sign the agreement, such that it will represent one that is made between the Finance Minister and the relevant Minister (or agency Chief Executive, for Finance portfolio agencies).

[119] Including an agreement for Finance that, although effectively executed, was unable to operate as intended.

The 'presumption of regularity'

3.45 As discussed in Chapter 1, a decision was taken in the drafting of the FMA Act to make net appropriation agreements perpetual. They would not need to be renewed as part of the annual appropriation and budget process. As a result, many of the agreements examined in this performance audit had been relied upon by the relevant agency for a number of years.

3.46 The drafting instructions for the preparation of the FMA Act provided to the Office of Parliamentary Counsel noted the following in respect to Section 31:

> Notwithstanding that appropriations of an Annual Appropriation Act will lapse at "30 June", the conditions as are agreed, between the Minister for Finance and the Minister responsible for the relevant agency, for enabling additional annual appropriations to be calculated under the "Net annotated appropriations" provisions of an Appropriation Act may, without a fresh agreement having to be made each year, be used as the conditions agreed for enabling appropriations to be calculated under similar provisions of future annual Appropriation Acts.
>
> Reason – to prevent the lapsing of "Revenue Recycling" agreements that are made under any Annual Appropriation Act and to facilitate an orderly administration of such agreements.

3.47 In this respect, agencies have been provided with reduced administrative requirements compared with the previous arrangements. The corollary to that is that, if agencies are to rely on an agreement as the authority for appropriating money from the CRF for a number of years, its recordkeeping practices need to take account of that.

3.48 In particular, agencies need to maintain an ability to demonstrate that the necessary steps were taken in executing their Section 31 agreement to ensure that it provided a legal appropriation in respect of the Section 31 receipts reported in each relevant year. A similar obligation arises in respect to Finance being able to demonstrate that officials who signed the whole-of-government side of an agreement were in a duly delegated position at the time they signed.

3.49 To enable ANAO to assess the extent to which Section 31 agreements had been executed in accordance with the requirements of the FMA Act, Finance and other agencies were requested to provide ANAO with evidence supporting the authority of officials below the level of Chief Executive who had signed agreements to do so. In many cases, agencies were unable to provide ANAO with any such evidence.

3.50 An Issues Paper provided to agencies on 3 June 2005 identified those agreements in respect of which ANAO had not been provided with evidence supporting the authority of the agency and/or Finance signatory. The Issues

Paper noted that, in those circumstances, there appeared to be significant doubt as to whether the relevant agreements had been executed in accordance with the requirements of the FMA Act.

Legal Advice

3.51 In preparing its comments on the ANAO Issues Paper, Finance asked AGS to prepare comprehensive advice addressing the matters raised. AGS's June 2005 advice to Finance was that the question as to whether a written or oral express authorisation existed at the time an official signed an agreement is one of fact. However, AGS further advised that the 'presumption of regularity' principle may apply in certain circumstances where an agency is not able to verify that an official had been expressly authorised by the Minister to enter into a Section 31 agreement on the Minister's behalf. AGS advised that:

> It may be that an agreement signed by an official other than the Chief Executive is presumptively valid in circumstances where:
>
> - the officer signed the agreement 'for and on behalf of the Minister' or in some other way which indicated that the officer understood himself or herself to be acting under an authorisation from the Minister; and
> - there is no evidence to support the view that the officer was not expressly authorised to enter into Section 31 agreements on behalf of the Minister.

3.52 AGS further advised that:

> In our view, the presumption of regularity would, in the kinds of circumstances existing here, carry significant weight. Specifically, in the 'ordinary course of human affairs' it seems unlikely that a senior official of the Public Service when executing a s.31 agreement would act on the basis that he or she was authorised to do so, when he or she was not.
>
> It follows that, we think that an agency which had no evidence that the relevant officer had NOT been expressly authorised by the Minister, either orally or in writing, would be entitled to proceed on the view that the officer was properly authorised to sign the s.31 agreement, and that the agreement was valid, provided that the officer signed the agreement 'for and on behalf of the Minister' or in some other way that indicated with reasonably [*sic*] clarity that the officer understood himself or herself to be acting under an authorisation from the Minister.[120]

3.53 Based on the AGS advice, a number of agencies, including Finance in respect of its execution of some agreements, relied upon the 'presumption of regularity'. In accordance with the AGS decision tree for assessing the

[120] In this respect, it needs to be recognised that Finance provides agencies with a template to complete in making Section 31 agreements. That template includes pre-existing signature blocks over which an official places their signature.

effectiveness of Section 31 agreements (see Figure 3.1), these agreements were assessed as 'in doubt'.

3.54 Eight of the 11 agencies that relied on a 'presumption of regularity' in respect of agency signatory(s) spent $2.86 billion of the amounts added to their annual appropriations under authority of those agreements. Two of the four agencies with agreements in respect of which the Finance signatory relied upon the presumption of regularity had spent $4.67 million of the relevant receipts.

3.55 In August 2005, AGS further advised ANAO that:

> The Auditor-General should only express the view that Section 83 of the Constitution has been breached in situations where the evidence of a breach is able to be established by cogent evidence, such that it is likely that a court would conclude that there has been a breach of Section 83.[121]

3.56 AGS advised that, where the two requirements identified in its advice regarding the application of a 'presumption of regularity' were satisfied, it was unlikely that a court would declare that expenditure in accordance with the Agreement was invalid because of a breach of Section 83 of the Constitution.

3.57 Consequently, the agencies that relied upon a 'presumption of regularity', or whose agreements were otherwise assessed as being 'in doubt', did not make any adjustments in their 2004–05 financial statement appropriation disclosures in respect to Section 31 receipts collected under the authority of an 'in doubt' agreement. Relevant expenditure was reported as having been spent with appropriation authority, but disclosure was made in the notes to the financial statements of the doubt that had arisen in respect to the effectiveness of the agency's agreement(s). Reference to the AGS legal advice in this respect was also included in the appropriations disclosure note to the affected agencies' 2004–05 financial statements.

Evidence of Ministerial authorisations

3.58 Each of the 11 agencies that relied upon a 'presumption of regularity' in respect to agency signatory(s) relied on the relevant agreement(s) as the authority to increase their available appropriations over a number of financial years. Ten agencies relied on an 'in doubt' agreement as the authority to retain Section 31 receipts collected during part or all of the 2004–05 financial year.[122]

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[121] The Legal Services Directions, issued by the Attorney-General pursuant to Section 55ZF of the *Judiciary Act 1903,* require that advice on Constitutional law matters be provided by AGS.

[122] The other agency, DAFF, executed a revised agreement on 20 June 2005, which retrospectively applied to amounts received from 1 July 2004.

3.59 The affected agreements were signed between 1998 and 2001. Agency officials in nine of the 11 agencies where the agency signatory was at issue signed more than one agreement in that time.[123] In addition to being unable to provide ANAO with evidence relating to the authority of the official who signed the agency's first agreement made under the FMA Act, none of those agencies could provide records relating to the relevant officials seeking to confirm their authority to sign the later agreement(s).

3.60 Prior to being required by Estimates Memorandum – 2004/22, issued by Finance on 10 September 2004, to execute revised agreements using the new template issued with Finance Circular No. 2004/09, none of the agencies had taken the necessary steps in the intervening period to address the absence of a demonstrably effective Section 31 agreement.

Archives requirements

3.61 The *Archives Act 1983* (Archives Act) and other key pieces of legislation[124] provide a legal framework for consistent and accountable recordkeeping practices.[125] In February 2000, the National Archives of Australia issued the *Administrative Functions Disposal Authority* (AFDA), which authorises the disposal of records relating to common administrative functions carried out by Commonwealth agencies. The AFDA was issued in accordance with Section 24 of the Archives Act.

3.62 The AFDA was identified as replacing a number of General Disposal Authorities (GDA) and Schedules (including those relating to finance and accounting records) and all entries in agency Records Disposal Authorities that covered records of an administrative nature. The AFDA stipulated that, after February 2000, sentencing activities undertaken by an agency must not use any of the GDAs listed as being replaced by the AFDA.[126]

3.63 The AFDA applies to records created as a result of 'Activities' undertaken in respect of 17 administrative 'Functions', including Financial Management. The Activities specified under the Financial Management Function include 'Authorisation', which is described as: 'The process of delegating power to authorise an action and the seeking and granting permission to undertake a requested action'.[127] The disposal action authorised by the AFDA in relation to records of this nature are:

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[123] Australian Greenhouse Office had one Agreement, signed in June 2001. Although the relevant official in Treasury signed two agreements (one to operate from 1 July 1998 and one to operate from 1 July 1999), both agreements were signed on the same day, 16 June 1999.

[124] Including the *Privacy Act 1988* and the *Freedom of Information Act 1982*.

[125] *Administrative Functions Disposal Authority*, National Archives of Australia, February 2000, p. 5.

[126] ibid., p. 9.

[127] ibid., p. 113.

- Records of delegations of power to agency staff to authorise financial activities and transactions may only be destroyed ten years after the delegation has been superseded (that is, ten years after a new delegation has been made).
- Records of authorisations for administrative actions relating to financial management may only be destroyed ten years after the action has been completed.[128]

3.64 The FMA Act commenced on 1 January 1998. In that context, a breach of the Archives Act may have occurred where agencies have not maintained Section 31 authorisation records until at least January 2008.

3.65 In December 2005, Finance advised ANAO that:

> To the extent that an agency applied the decision tree (developed by the AGS and agreed by Finance and ANAO), but did not form the genuine belief that an express authorisation would have been obtained, the agency would be unable to rely on the presumption of regularity and the relevant agreements would have been ineffective, rather than "in doubt", and would not have provided the agency with the appropriation authority in respect of retaining or spending the affected receipts.

3.66 To the extent agencies made no record of an express authorisation provided by their Minister in respect to an official executing a document with significant Constitutional consequences, those agencies have not fulfilled their accountability obligations to the Government and the Parliament.

3.67 To the extent an express authorisation was not obtained, the relevant agreements would be ineffective and would not have provided the agency with appropriation authority in respect of retaining or spending the affected receipts.

Agencies that relied on a 'presumption of regularity'

3.68 As noted at paragraph 3.38, as part of this performance audit, ANAO sought to confirm that Section 31 agreements on which agencies had relied had been executed in accordance with legislative requirements. As a first step, consideration of this aspect of agencies' management of agreements was initially focused on those instances where the signature block used by an official indicated that he or she had signed the agreement acting under an authority or capacity that was not in accordance with the requirements of Section 31 and other relevant provisions.

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[128] ibid.

3.69 In view of Finance's role in respect to financial framework issues, and as co-signatory to all agreements, on 4 April 2005 ANAO sought Finance's views on the matters raised prior to raising the issue with the individual agencies concerned. As part of that process, ANAO obtained copies of documentation held by Finance in relation to Ministers authorising agency signatories to agreements.

3.70 There were many agreements where Finance did not hold a copy of an authorisation to the agency official from the responsible Minister, including in relation to those agreements being initially considered. This was because, in general, Finance did not, prior to 2004, seek to obtain evidence from agencies as to the power under which the agency signatory was signing an agreement. In this respect, in February 2005, Finance advised ANAO that, while Finance issues guidance to agencies, it is agencies' own responsibility to comply with the legislation and regulations and conform to the guidance affecting them.

3.71 Where Finance did not hold a copy of an authorisation for officials who had signed agreements in an invalid capacity, during April 2005 ANAO sought advice from the relevant agencies as to whether a Ministerial authorisation had been obtained. ANAO also requested a copy of the instrument of authorisation or other relevant documentation. Agencies were advised that this documentation was important because the agency would not have been legally entitled to retain Section 31 receipts in the absence of an agreement signed by a duly authorised official. A number of agencies were unable to provide the requested documentation. Some indicated that they had not previously been aware of a requirement to obtain such authorisation.

3.72 Having regard for the outcomes of this initial request, ANAO examined all agreements signed by officials at levels below the agency Chief Executive in order to establish the substance of their authority to do so.

Second request by ANAO for evidence of authorisation

3.73 An Issues Paper circulated to relevant agencies on 3 June 2005 identified those agencies where officials at levels below the agency Chief Executive had signed agreements, but for whom documentation of authorisation from the relevant Minister had not been sighted by ANAO as at 30 May 2005. Where the official was not acting as the agency's Chief Executive or Secretary at the relevant time, ANAO sought advice from each agency as to whether a written Instrument of Authorisation had been obtained from the responsible Minister in respect of the relevant official signing Section 31 agreements. If so, ANAO requested that a copy of relevant documentation be provided.

3.74 In response, some agencies provided ANAO with evidence of authorisation for the relevant official. However, a number of agencies were

unable to provide either documentary or oral evidence of the relevant official having obtained an express authorisation from the responsible Minister. Some indicated that they wished to rely on a 'presumption of regularity'.

Third request by ANAO for evidence of authorisation

3.75 The application of a 'presumption of regularity' in these circumstances leads to ongoing doubt about the effectiveness of agreements that operate to increase amounts appropriated by the Parliament, and potentially has implications for other aspects of public administration. Accordingly, ANAO sought independent advice from Professor Dennis Pearce, Special Counsel at Phillips Fox and one of the authors of *Delegated Legislation in Australia*.[129] In July 2005, ANAO was advised as follows.

> We do not consider that the presumption can operate to enable an agency to set aside doubts as to the authority of an official to execute an agreement once it has been apprised of those doubts. The following passage from the judgement of Debelle J in *Town of Gawler v Minister for Transport & Urban Planning* [2002] SASC 85 is relevant:
>
> > 30. As Lord Simonds noted in *Morris v Kanssen* [1946] AC 459 at 475-476, there are limits to the application of the presumption of regularity. The presumption is designed for the protection of those who are entitled to assume, because they cannot know, that the person with whom they deal has the authority which is claimed. The principle cannot be invoked if the condition is no longer satisfied, that is to say, if he who would invoke it is put upon his inquiry. He cannot presume in his own favour that things are rightly done, if the inquiry that he ought to make would tell him that they were wrongly done. The effect of Lord Simonds' views is that the presumption does not apply where a person purports to act and his authority to act is in question.
>
> …In the circumstances that exist here, it is the agency that is seeking to justify its actions and it has been alerted to the possibility that an agreement has been signed by an official without authority. The agency cannot justify its action by claiming that it must have acted properly when it lies within its own power to determine if it has done so. In the words of Lord Simonds as endorsed by Debelle J, the agency cannot presume *in its own favour* that things have been rightly done when enquiry might reveal the contrary.
>
> The position here is also different from that which existed in the cases referred to by AGS where the presumption was able to be invoked. In those cases it was a person outside the government who was raising the issue of validity. Here the question is being asked within the government. We are of the view that it is not possible to regard Commonwealth government agencies as

[129] Professor Dennis Pearce and Stephen Argument, *Delegated Legislation in Australia*, 2nd Edition, Butterworths, 1999.

separate entities for the purposes of the presumption of regularity. If there are doubts about the validity of an agreement held by one Commonwealth agency, those doubts enure to other Commonwealth agencies such that the agency immediately involved cannot rely on the presumption of regularity to reject the doubts held.

3.76 Accordingly, on 18 July 2005, ANAO wrote to affected agencies informing them that ANAO's advice was that, in all the circumstances, a 'presumption of regularity' cannot be relied upon as the basis for concluding that an agreement is valid, particularly in view of the significance of Section 31 agreements. Agencies were informed that, in ANAO's view, they should be able to demonstrate that the official who signed an agreement was properly authorised. Accordingly, affected agencies were again asked to provide ANAO with any information that existed concerning the power of relevant officials to sign particular agreements for and on behalf of the responsible Minister.

3.77 From responses received to ANAO's request to agencies for evidence that signatories were properly authorised, it was apparent that some agencies had misinterpreted the AGS advice regarding the 'presumption of regularity' to mean that there were no circumstances in which Section 31 agreements could be assessed as being 'ineffective'. To clarify and resolve any misunderstandings, ANAO and Finance obtained joint advice from AGS on the operation of the 'presumption of regularity' that AGS had advised Finance applied in relation to Section 31 agreements.

3.78 AGS advised that:

> The concepts of 'validity' and 'invalidity' are only meaningful in the context of a judicial determination of a legal question affecting legal rights. When a lawyer advises that particular official action is invalid, he or she is making a prediction as to how a court would determine a particular matter when faced with particular facts.
>
> The issue of the validity of a section 31 agreement makes no sense divorced from the issue of whether expenditure under it was invalid as contrary to sections 81 or 83. In my view, if a court had to determine whether public expenditure had been unauthorised on the basis that the section 31 agreement had been entered into without authority, significant weight would be given to the fact that the relevant official was a senior official who had executed the agreement in an ostensibly regular form. Indeed, in the absence of reasonably cogent evidence that an official who executed a section 31 agreement in a regular form in fact had no authority to do so, it is unlikely that a court would declare that expenditure in accordance with the agreement was invalid because of a breach of section 83 of the Constitution.
>
> In adopting this approach, the Court would be guided by a number of factors, including a reluctance to take action that may be prejudicial to third parties when the alleged basis for invalidity relates to the internal financial administration of the Government.

3.79 AGS also provided advice on the circumstances in which, in their view, the 'presumption of regularity' did apply, such that the agreement should be assessed as being 'in doubt', rather than 'ineffective', and on circumstances that could reasonably give rise to a conclusion that an agreement was 'ineffective'. The AGS advice is reflected in the decision tree that was applied in assessing all agreements in the context of agencies' annual financial statement audits (see Figure 3.1).

3.80 Through this process, some further agencies were able to provide information to demonstrate that the relevant official(s) had been expressly authorised by the responsible Minister, such that the relevant agreements were effective. One or more agreements relating to some other agencies were assessed as 'ineffective' on the basis of the documentary evidence and other information or advice provided in relation to whether the relevant official had been expressly authorised by the responsible Minister at the time the agreement(s) were signed (see Figure 3.4).

3.81 However, 11 agencies remained unable to provide ANAO with reasonably cogent evidence to assess whether or not the relevant officials were authorised when they signed the agency side of 23 agreements. In each case, a 'presumption of regularity' was relied upon to argue that the agreement should be assessed as 'in doubt', rather than 'ineffective'.

3.82 The relevant agencies disclosed the doubt in relation to the effectiveness of their agreement(s) in their 2004–05 financial statements. The agencies, and the affected receipts and spending disclosed by them, are identified in Figure 3.2. In total, those agencies disclosed $4.8 billion as having been added to their respective annual appropriations up to 30 June 2005 under the authority of agreements that they were unable to demonstrate had been effectively executed on the agency side. A total of $2.86 billion of those receipts had been spent.

3.83 In December 2005, Finance advised ANAO that agreements categorised as 'in doubt' have since been replaced with demonstrably effective agreements, and the presumption of regularity does not, and could not be expected to, apply in respect of any current section 31 agreement.

Figure 3.2

Agreements where the agency relied on a 'presumption of regularity'

Agency	Date Signed	Period Affected	Receipts ($)	Receipts Spent ($)	Agency Advice to ANAO
Australian Greenhouse Office	19 June 01	1 July 00 to 3 Nov 04	9 160 598	Nil	Agency Chief Executive Instructions indicate that the official would only have signed if he had been authorised.
Australian Public Service Commission	2 Feb 99	1 July 98 to 30 June 99	8 331 000	8 331 000	We can find no evidence that the official was expressly authorised by the Minister but this is not to say that such an authorisation was not expressly provided at some point.
	4 June 99	1 July 99 to 31 Dec 04	62 006 000	46 492 000	
Australian Taxation Office	25 June 98	1 Jan 98 to 30 June 99	30 560 698	8 067 383	The Tax Office takes these issues very seriously and the time delay has been necessary to attempt to locate and where possible examine documentation and files. We have also, as you are aware, been exploring a range of issues with our lawyers around the application of section 31 agreements. In view of the length of time since the introduction of the FMA Act and the entering into of the first section 31 agreement the Tax Office has had difficulty locating the appropriate files. After research it has been identified that the relevant files have been destroyed. Therefore the Tax Office is neither able to prove that the prior section 31 agreements are valid nor confirm that the agreements are not valid.
	21 June 99	1 July 99 to 18 Apr 05	365 505 017	91 662 525	

Agency	Date Signed	Period Affected	Receipts ($)	Receipts Spent ($)	Agency Advice to ANAO
Department of Agriculture, Fisheries & Forestry	26 Nov 98	1 July 97 to 30 June 99	65 057	65 057	We can find no evidence that the official was expressly authorised but this is not to say that such an authority was not expressly provided at some point.
	30 June 99	1 July 99 to 30 June 04	268 628 000	253 403 000	
Department of Defence	22 June 99	1 July 99 to 29 June 05	3 653 118 584	2 262 079 410	Defence has insufficient evidence to be able to determine whether the relevant officials did or did not seek express authorisation from the Minister.
	26 June 01				
Department of Education, Science & Training	29 June 98	29 June to 30 June 98	Nil	Nil	There is no evidence that the responsible Minister authorised the official to sign for and on their behalf but the official may have been authorised.
	24 June 99	1 July 98 to 30 June 99	18 556 000	Nil	
	24 June 99	1 July 99 to 5 Dec 04	52 402 000	5 520 000	
Department of the Environment & Heritage	8 June 99	1 July 98 to 30 June 99	21 919 000	8 699 626	There is no reason to believe that the Minister would not have authorised the official. We have not uncovered any information which suggests that the Minister did not authorise the official.
	22 June 99	1 July 99 to 28 June 05	251 636 131	169 248 237	
Department of Industry, Tourism & Resources	6 April 98	1 July 97 to 30 June 99	1 146 000[A]	Nil	It is highly unlikely the senior official would have signed without consideration having been given as to whether the agreements were acceptable to the then Secretary and the then Minister.
	12 July 99	1 July 99 to 1 Dec 04	20 789 625	Nil	

Agency	Date Signed	Period Affected	Receipts ($)	Receipts Spent ($)	Agency Advice to ANAO
Department of the Treasury	16 June 99	1 July 98 to 30 June 99	653 044	Nil	AGS advice of 12 September 2005 was that there is no sufficiently cogent evidence that an express authorisation was or was not given by the Treasurer.
	16 June 99	1 July 99 to 2 Mar 05	24 374 358	2 542 289	
Office of the Commonwealth Ombudsman	21 Jan 99	1 July 98 to 30 June 99	432 872	404 895	We cannot demonstrate that the agreements were properly made, nor can we, after inquiry and thoughtful consideration, be satisfied that they were not.
	20 July 99	1 July 99 to 31 Jan 05	4 832 053	2 590 950	
Productivity Commission	22 June 98	16 April to 30 June 98	Nil	Nil	While oral or written Ministerial authorisations may have been provided, the Commission has no record of them.
	29 June 99	1 July 98 to 30 June 99	102 000	Nil	
	4 June 99	1 July 99 to 23 Feb 05[B]	2 438 000	Nil	
		Total	**4 796 656 037**	**2 859 106 372**	

Notes

[A] The affected receipts disclosed by DITR did not include $1 936 538 collected in 1997–98.

[B] The Productivity Commission's 2004–05 financial statements disclosed this agreement as being 'ineffective'. That assessment was based on the information provided by Finance in response to ANAO's 3 June 2005 request for advice as to whether the Finance signatory held the necessary delegation. Subsequently, on 28 September 2005, Finance advised ANAO of advice that it had received from the relevant person in response to a request it had made on 27 September 2005. On the basis of that advice, which related to notes in the person's personal diary records, the Finance signatory was assessed as having effectively executed the agreement. However, doubt remains as to the authority of the Commission's signatory. The Commission has relied upon a 'presumption of regularity' to have that agreement assessed as 'in doubt', rather than 'ineffective'.

Source: ANAO analysis based on examination of Section 31 agreements, agencies' financial reporting, evidence and advice provided by agencies to substantiate the authority of signatories to agreements, and the decision tree of AGS advices on assessing the effectiveness of agreements.

3.84 In addition to the agencies included in Figure 3.2, a further three agencies also had agreements assessed as 'in doubt'.[130] These agencies were unable to provide ANAO with evidence of an express Ministerial authorisation, but there was sufficient and appropriate evidence available to provide sufficient indication that the official may have been authorised. Receipts affected by 'in doubt' agreements in these agencies totalled $153.3 million, with $124.9 million of those receipts having been spent.

Finance reliance on a 'presumption of regularity'

3.85 As discussed, successive Finance Ministers have delegated to the Finance Secretary their power to enter into Section 31 agreements. The Secretary has sub-delegated that power to Finance officials performing identified duties. As at 30 June 2005, four such delegation instruments had been in place at various times since December 1997.

3.86 As part of the audit, ANAO identified a number of instances where it was not apparent that the senior Finance official who signed the Finance Minister's side of the agreement had occupied a delegated position at the time of signing one or more agreements. These instances were raised with Finance in the 3 June 2005 Issues Papers, as well as in earlier discussions.

3.87 Subsequently, Finance provided ANAO with advice on whether there was any information to demonstrate that the relevant officials held the delegated position at the relevant times. In some instances, because of inadequacies in its personnel records, Finance relied upon recollections from individual officers, the organisational structure as presented in the Department's Annual Report or *Hansard* records of the relevant official's attendance at Senate Estimates hearings held around the time the agreements in question were signed. Clearly, it would be preferable for Finance to have more reliable systems in place for identifying which officials are able to exercise delegated powers of the Finance Minister. In this respect, in December 2005, Finance advised ANAO that:

> The audit has raised concerns regarding systems Finance has in place for identifying officials who are able to exercise powers delegated by the Minister for Finance and Administration. In response, Finance is now considering options to enhance the recording of acting arrangements to more easily and reliably ascertain which officials held delegations at a specific time.

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[130] Namely: DCITA for the period 1 July 1997 to 21 June 2005 (receipts affected – $151 871 825; receipts spent – $123 737 127), the Department of Veteran's Affairs (DVA) for 1997–98 (receipts affected – $240 000; nil receipts spent. DVA provided written instruments of authorisation in regard to the signatory to agreements that applied from 1 July 1998); and the Human Rights and Equal Opportunity Commission (HREOC) for 1998–99 (receipts affected – $1 194 877; receipts spent – $1 175 879. The agreement relied upon by HREOC from 1 July 1999 to 1 December 2004 was ineffective due to the Finance signatory not holding the delegation – see Figure 3.4).

3.88 Finance further advised that, in the meantime, it had issued internal guidance advising that when the delegated official is unable to sign an agreement, the agreement should be signed by another official substantively occupying a delegated position, rather than the official in the nominal position.

3.89 Where supporting evidence was provided by Finance, agreements were assessed as effective. Nine agreements were assessed as 'ineffective', as there was evidence that the relevant Finance official did not hold the necessary delegation at the time of signing the agreement (see Figure 3.4).

3.90 There were four agreements in relation to four agencies where Finance was unable to provide reasonably cogent evidence as to whether or not the Finance official who signed as delegate of the Finance Minister occupied the delegated position (General Manager of Finance's Budget Group) at the relevant times. In each of those instances, a 'presumption of regularity' was relied upon to argue that the agreements should be assessed as 'in doubt', rather than 'ineffective'. AGS advice to Finance of 20 September 2005 was that it was arguable that the officer who signed each of these agreements may have signed while temporarily performing the duties of the delegated position. Accordingly, these agreements were assessed as 'in doubt', based on the 'presumption of regularity'.

3.91 The four agencies whose agreements were assessed as 'in doubt' due to the Finance signatory disclosed this issue in their 2004–05 financial statements. The relevant agencies and the receipts and spending disclosed as being affected are identified in Figure 3.3. In total, those agencies disclosed $20.59 million as having been added to their respective annual appropriations up to 30 June 2005 under the authority of agreements that Finance was unable to demonstrate had been effectively executed on the whole-of-government (Finance Minister) side. A total of $4.67 million of those receipts had been spent.

Figure 3.3

Agreements where the Finance signatory relied on a 'presumption of regularity'

Agency	Date Signed	Period Affected	Receipts ($)	Receipts Spent ($)
Federal Magistrates Court	12 July 00 [A]	1 July 00 to 19 Dec 04	843 558	Nil
Insolvency and Trustee Service Australia	25 July 00	1 July 00 to 19 June 05	6 490 611 [B]	93 136
Office of the Commonwealth Director of Public Prosecutions	24 July 00	1 July 00 to 1 Dec 04	8 604 700	Nil
Office of the Privacy Commissioner	11 Aug 00	1 July 00 to 1 Dec 04	4 652 547	4 578 470
		Total	**20 591 416**	**4 671 606**

Notes

[A] The Court's 2004–05 financial statements disclosed this agreement as being 'ineffective', due to the Finance signatory not holding an express delegation. Subsequent to the financial statements being completed, Finance obtained legal advice that resulted in this agreement being assessed as 'in doubt'.

[B] This is the amount disclosed by ITSA in its 2004–05 financial statements as ''Receipts Affected" by the 'in doubt' agreement. The 'in doubt' agreement applied to receipts collected in the period 1 July 2000 to 19 June 2005. ITSA's 2004–05 financial statements identified that the 'in doubt' period extended to 19 June 2005, but did not include amounts received in the period 1 July 2004 to 19 June 2005 in the table disclosing the "Receipts Affected". ITSA separately reported total Section 31 receipts for 2004–05 of $1 314 946. On 20 December 2005, ITSA advised ANAO that all of those receipts were received prior to 20 June 2005 and were, therefore, also receipts affected by the 'in doubt' agreement. This results in the total receipts affected by the 'in doubt' period being $7 805 557.

Source: ANAO analysis based on examination of Section 31 agreements, agencies' financial reporting, evidence and advice provided by agencies to substantiate the authority of signatories to agreements, and the decision tree of AGS advices on assessing the effectiveness of agreements.

Addressing the 'presumption of regularity'

3.92 The accountability obligations of Departments of State and other agencies reasonably require agencies to be able to demonstrate that public money has been administered in accordance with relevant legislation. As noted, AGS has advised that a Section 31 agreement may be presumptively valid where an official has signed the agreement in an ostensibly regular form and there is no evidence to support the view that the officer was not expressly authorised to enter into the agreement on behalf of the Minister (see paragraph 3.51). The agencies that have sought to rely on a 'presumption of regularity' depended upon the absence of any relevant records relating to them obtaining an express authorisation to exercise a statutory power on their Minister's behalf as the basis for claiming that there is no evidence the official was not authorised. In December 2005, Finance advised ANAO as follows:

Finance notes that these decisions were made by Chief Executives of the affected agencies and assessments made against the decision criteria (based on AGS legal advice).

3.93 ANAO's understanding, from separate legal advice received, is that the 'presumption of regularity' is for the protection of those who are entitled to assume, because they cannot know, that the person with whom they deal has the authority that is claimed. For example, 'the person in the street' who cannot know whether a government official with whom he or she deals has the authority to undertake a particular function.

3.94 The application of a 'presumption of regularity' in relation to Australian Government agencies substantiating whether officials within the agency concerned complied with legislative requirements in executing a Section 31 agreement, where it is the agency that has relied on the agreement, is not desirable. Relying upon a 'presumption of regularity' in this context inevitably leaves doubt as to the effectiveness of the agreement and, therefore, the amount of the appropriation that was legally available to the relevant agency. This does not reflect sound administrative practice, in the ANAO's view.

3.95 To put matters beyond doubt, ANAO and Finance agree that agencies should obtain a written authorisation from the responsible Minister before entering into Section 31 agreements on the Minister's behalf. The Circulars issued by Finance advocate this approach as best practice.

3.96 ANAO also considers that there would be merit in Finance taking further steps to limit the opportunity for agencies to rely upon a 'presumption of regularity' when increasing their annual appropriations through Section 31 arrangements. This might involve clearer legislative requirements covering Ministers delegating or authorising officials to exercise the statutory power of entering into Section 31 agreements. It might also involve stronger recordkeeping requirements that are specific to the signing of Section 31 agreements.[131]

[131] The current FMOs include requirements that relate to agencies obligations in relation to appropriations generally, but not specifically to the execution of Section 31 agreements.

Recommendation No.3

3.97 In the interests of an effective and accountable financial framework for the management of appropriations, ANAO *recommends* that:

(a) as part of their financial controls and in accordance with Commonwealth recordkeeping requirements, all agencies maintain adequate records of Section 31 authorisations and delegations provided by Ministers (and, where relevant, Chief Executives), together with records of which official(s) held the power when Section 31 agreements were signed; and

(b) the Department of Finance and Administration examine possible administrative and/or legislative changes that could limit the opportunity for agencies to rely upon a 'presumption of regularity' when increasing their appropriations through Section 31 arrangements.

Agency responses

3.98 All agencies that responded to this recommendation agreed to relevant parts (see Appendix 2). Agencies commented as follows:

- AFP:

  The AFP maintains adequate records of Section 31 authorisations and delegations.

- DEST:

  The Department has improved its financial controls to ensure that adequate records are maintained in relation to:

  - Section 31 authorisations provided by the Minister; and
  - those officials who held the power when the Section 31 agreements were signed.

- DITR:

  This is current Departmental practice.

- Family Court of Australia:

  The Court has retained a record of the Attorney-General's Law Officers Amendment Delegation 2004 covering the 2004 Section 31 Agreement. A record of delegation will be retained as required for future Section 31 Agreements.

- Finance:

  Finance agrees with part (a) of the recommendation and notes that it reflects the best practice advice issued in the relevant Finance Circular (2004/09, subsequently replaced by 2005/07).

Finance also agrees with part (b) of ANAO's recommendation to examine possible changes that limit any need for agencies to rely on a presumption of regularity. For example, the *Financial Management and Accountability Orders 2005* could be amended to include a requirement for agencies to retain these authorities. Non-compliance with this requirement would result in a breach of section 48 of the *Financial Management and Accountability Act 1997*. Further, as part of a broader project to simplify the management of the financial framework, Finance is examining possible policy, administrative and legal changes that could be affected to improve the operation and reduce the scope for compliance issues regarding section 31 agreements.

3.99 In agreeing to the recommendation, the National Archives of Australia commented as follows:

> The Archives notes that the review relates to agreements made from 1998. The Archives' Administrative Functions Disposal Authority (AFDA) covers these records, and was issued in February 2000. AFDA authorises the destruction of financial delegations ten years after the delegation is superseded, and authorisations ten years after action is complete.
>
> Records created prior to the release of AFDA may have been sentenced for destruction according to the predecessor authority, General Disposal Schedule Number 12. This earlier authority authorised the destruction of these records seven years after action is completed. The Archives would expect, however, that, as records created in 1998 would still have been in existence on the release of AFDA in 2000, agencies would have revised the retention period for these records to the new 10-year period.
>
> These retention periods are primarily based on the need for these records to be available for scrutiny by regulatory bodies. The Archives strongly endorses the recommendation and requires that agencies keep proper records of significant delegations and authorisations such as those used in making section 31 agreements.

'Ineffective' agreements

3.100 As discussed, 42 agreements were assessed as having been ineffectively executed by either the agency or Finance signatory. As a consequence, the affected agencies had not obtained the appropriation authority in respect to amounts collected under those agreements that had previously been reported.

3.101 On 22 June 2005, Finance advised the Finance Minister that ANAO had raised issues relating to the effectiveness of many Section 31 agreements. The Minister was advised that, where an agency did not have an effective agreement in place, there may have been breaches of Section 83 of the Constitution.

3.102 On 23 June 2005, the Minister agreed to Finance's recommendation that the Secretary of Finance execute instruments to vary all current Section 31 agreements to cover relevant past receipts and to cancel all agreements that

commenced on or before 30 June 2004. The Minister was advised that these steps would regularise the operation of Section 31 agreements across all agencies, and put the effectiveness of current agreements beyond doubt. In turn, this would reduce the implications for agency financial statements for 2004–05, and ensure that issues concerning 'ineffective' Section 31 agreements would not affect agencies' 2005–06 financial statements.

3.103 Accordingly, on 24 June 2005, the Secretary, as delegate of the Finance Minister, made two instruments under subsection 31(4) of the FMA Act. Both instruments had global application across all agencies, the first time the provision had been used in this way.

3.104 The first instrument cancelled all agreements made on or before 30 June 2004. The objectives of the Cancellation Instrument were to ensure that each agency was operating on the basis of an effective agreement made under the new template, and provide certainty regarding which agreements were in operation.

3.105 The second instrument (the Variation Instrument) varied all current Section 31 agreements to include, as eligible receipts, amounts previously received in purported reliance on 'ineffective' agreements. This instrument applied to all agreements made between 1 July 2004 and 30 June 2005.[132] It provided agencies with an appropriation, as at 30 June 2005, for all receipts that were subject to an 'ineffective' prior agreement. This allowed any unspent amounts to be lawfully spent. This action could not, however, remove past breaches of Section 83 of the Constitution that occurred due to agencies spending those receipts without an appropriation.

3.106 Given the doubts that existed over the execution of many Section 31 agreements at the time the Variation Instrument was made, it did not identify the 'ineffective' agreements in respect of which it would take effect. Instead, the Finance Secretary was advised that a case-by-case assessment would be undertaken after 1 July 2005.

3.107 Applying the decision tree of AGS advices for assessing effectiveness to the evidence and advice provided by the relevant agencies and Finance, one or more of the agreements made for each of 23 agencies were assessed as being 'ineffective'. This was due to either the agency signatory not being expressly authorised or delegated by the responsible Minister (or, where relevant, Finance portfolio Chief Executive) at the time of signing the agreement, or the Finance signatory not holding a delegation from the Finance Minister.

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[132] With the exception of ANAO's agreement. Subsection 52(2) of the Auditor-General Act provides that the Finance Minister must not cancel or vary a net appropriation agreement made with the Auditor-General unless the Auditor-General consents.

3.108 In some cases, the 'ineffective' agreement had not been relied upon by the relevant agency to increase its annual appropriation, or the receipts collected under the agreement were not regularised by the Variation Instrument.[133] In summary, the Variation Instrument applied in respect to receipts totalling $1.76 billion across 19 agencies.

Financial reporting implications

3.109 The financial reporting implications for agencies with one or more 'ineffective' Section 31 agreements were agreed between Finance and ANAO to facilitate timely financial reporting by agencies. Proforma disclosures were provided to CFOs in July 2005. In summary, except where this issue had no effect on available appropriations, agencies were expected to disclose the following in the appropriation note to their 2004–05 financial statements:

- that they had previously operated on the basis of an 'ineffective' Section 31 agreement or agreements, and the period(s) affected;
- the reason the agreement had been assessed as 'ineffective' (because the agency signatory had not been authorised or delegated and/or the Finance official lacked the requisite delegation);
- the quantum of receipts added to the agency's annual appropriation in each relevant year under authority of an 'ineffective' agreement; and
- the quantum of receipts retrospectively captured, as at 30 June 2005, by operation of the Variation Instrument.

3.110 In August 2005, AGS advised ANAO that, where agreements are assessed as 'ineffective', the Auditor-General is able to express a view on whether agencies had spent more money than had been appropriated to them. Accordingly, agency financial statements also included disclosure of any amounts retained under authority of an 'ineffective' agreement that had been spent, and a statement that this spending was made without the authority of the Parliament, in contravention of Section 83 of the Constitution. Amounts

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[133] Two agencies had an earlier, effective agreement on which they could continue to rely for the relevant period (Commonwealth Grants Commission and the Department of the Parliamentary Reporting Staff, which has since been abolished); ARPANSA did not receive any relevant receipts in reliance on the ineffective agreement; and the Office of Asset Sales and IT Outsourcing (OASITO) had been abolished in November 2001, with its functions being absorbed by Finance. The appropriation for the ineffective period for OASITO had lapsed prior to it being abolished. An effective agreement for ONA made in July 1999 was not replaced by an 'ineffective' agreement signed in November 2004. The Variation Instrument captured the receipts collected by Finance between 1999 and 2005 under ineffective departmental agreements. However, the Instrument was not able to cause the administered agreement in place for Finance as at 30 June 2005 to increase the department's administered appropriation item in respect of receipts collected under earlier ineffective administered agreements, due to an error in the terms of the June 2005 agreement.

totalling $1.16 billion were disclosed as having been spent without appropriation between 1997–98 and 2004–05.

3.111 Where the 'ineffective' agreement was a result of the agency signatory not being authorised, a corresponding breach of Section 48 of the FMA Act was also reported.[134] As with relevant agencies that had contravened Section 83 as a result of 'no agreement' periods, the Section 48 breach was reported as consequence of the specific obligations placed on agency Chief Executives under that Section to keep proper accounts and records, and pursuant to the provisions of the Auditor-General Act and the ANAO Auditing Standards.[135]

3.112 Figure 3.4 identifies the 23 agencies with agreements that were assessed as being 'ineffective'. It also identifies the Section 31 receipts disclosed by those agencies as having been collected under an 'ineffective' agreement (and therefore captured by the Variation Instrument) and, where relevant, the amount spent without an appropriation.

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[134] Where the deficiency related to the Finance signatory, the affected agency did not breach Section 48.

[135] See paragraph 2.5 and footnotes 50 and 51.

Figure 3.4

'Ineffective' Section 31 agreements

Agency	Period Affected	Receipts Affected ($)	Receipts Spent ($)
'Ineffective' agency signatory:			
AusAID - departmental	1 July 98 to 27 June 05	3 780 099[A]	Nil
AusAID - administered	1 July 01 to 27 June 05	328 113	Nil
Australian Bureau of Statistics	1 July 97 to 30 June 98	29 600 000	21 400 000
	1 July 99 to 6 Mar 05	135 100 000	128 300 000
Australian Competition and Consumer Commission	1 July 98 to 14 Mar 05	5 938 000	4 653 000
Australian Electoral Commission	1 Jan 98 to 30 Jun 99	7 490 000	7 473 000
Australian Federal Police	1 July 98 to 6 Dec 04	622 495 000	443 355 000
Australian Radiation Protection and Nuclear Safety Agency	1 July 99 to 9 Feb 05	Nil (See Note B)	
Australian Security Intelligence Organisation	1 July 99 to 30 June 04	24 618 000	16 364 000
Department of Family and Community Services	1 July 98 to 30 June 99	1 346 000	Nil
Department of Finance and Administration - departmental	1 July 99 to 30 June 02	39 429 000	2 602 000
Department of Finance and Administration - administered	1 July 99 to 5 June 02	Unknown[C]	Nil
Department of Health and Ageing	1 July 98 to 28 June 05	488 095 000	404 613 000
Department of Transport and Regional Services (incl. Territories)	1 July 98 to 30 June 99	7 988 000	Nil
Federal Court of Australia	1 July 00 to 3 April 05	9 798 958	Nil
National Competition Council	1 July 98 to 1 Mar 05	558 588	Nil
Office of Asset Sales and IT Outsourcing	1 Jan 98 to 30 June 98	62 004[D]	Nil
Office of Film and Literature Classification	1 July 98 to 28 June 05	9 033 076	7 564 227
Office of National Assessments	1 July 98 to 30 June 99[E]	46 001	7 702
'Ineffective' Finance signatory:			
Australian Electoral Commission	1 July 99 to 31 Jan 05	79 655 000	47 918 000
Australian Office of Financial Management	1 July 99 to 30 June 02	312 064	Nil
Australian Secret Intelligence Service	1 July 99 to 30 June 04	Figure protected.	

Agency	Period Affected	Receipts Affected ($)	Receipts Spent ($)
Commonwealth Grants Commission	Nil (See Note F)		
Department of Family and Community Services	1 July 99 to 30 Sep 04	148 196 542	33 887 000
Department of Finance and Administration - departmental	1 July 02 to 27 April 05	22 890 000	20 852 000
Department of Finance and Administration - administered	6 June 02 to 28 June 05	At least 788 355[G]	Nil
Department of Transport and Regional Services - departmental	1 July 99 to 2 March 05	96 482 000	6 727 000
Department of the House of Representatives	1 July 99 to 28 Feb 05	3 287 079	Nil
Department of the Parliamentary Reporting Staff	Nil (See Note H)		
Human Rights and Equal Opportunity Commission	1 July 99 to 1 Dec 04	18 968 130	17 009 898
Office of the Inspector-General of Intelligence and Security	1 July 99 to 20 Feb 05	158 646	52 932
	Total	**1 756 443 655**	**1 162 778 759**

Notes

[A] The affected receipts disclosed by AusAID excluded $894 678 in receipts collected in 1998–99.

[B] The amounts disclosed by ARPANSA as Section 31 receipts in each affected year was a reporting error as those amounts related to Special Account receipts (see Chapter 4).

[C] ANAO raised issues regarding these receipts with Finance, in the context of such amounts having been reported in its PBS, but not as Section 31 receipts, together with differences between amounts received in 2003–04 and the PBS disclosures. Finance did not provide ANAO with details that would allow for the accurate identification of the relevant receipts received in financial years prior to 2003–04.

[D] These receipts were not regularised by the Variation Instrument as OASITO was abolished in 2001. The receipts were not reported as being spent in 1997–98, and the appropriation lapsed as at 30 June 1998.

[E] A further 'ineffective' agreement for ONA, signed on 22 September 2004 using the new template, did not replace an effective agreement that operated from 1 July 1999.

[F] The 'ineffective' agreement, signed on 1 November 2004 using the new template, did not replace an earlier, effective agreement that operated from 1 July 1999.

[G] This reflects actual receipts for 2003–04 and the estimated receipts for 2004–05 advised to the Finance Minister and Secretary. These receipts were not regularised by the Variation Instrument due to a flaw in the administered agreement for Finance executed on 29 June 2005. Issues relating to inconsistencies in Finance's treatment and disclosure of these receipts are discussed in Chapter 4.

[H] A Finance official signed the 'ineffective' agreement on 17 February 2000, to operate from 16 December 1999. That agreement did not replace an earlier, effective agreement signed by a delegated Finance official on 1 July 1999 and the DPRS Secretary on 7 January 2000, to operate from 1 July 1999.

Source: ANAO analysis based on examination of Section 31 agreements, agencies' financial reporting, evidence and advice provided by agencies to substantiate the authority of signatories to agreements, and the decision tree of AGS advices on assessing the effectiveness of agreements.

4. Accountability to the Government and the Parliament

This chapter discusses agencies' obligations in respect to providing the Government and the Parliament with an accurate accounting of their use of net appropriation arrangements.

Introduction

4.1 The financial framework requires accountability for agency use of net appropriation arrangements in three primary ways, as follows:

- Since 1 January 2005, Section 31 agreements have been registered on a publicly available register of legislative instruments, enabling the Parliament to be aware of what agreements have been made since that date and their terms and conditions;
- Disclosure in Portfolio Budget Statements (PBS) and Portfolio Additional Estimates Statements (PAES) of receipts estimated to be collected by the relevant agency under authority of a Section 31 agreement; and
- Disclosure in annual financial statements of the actual increase in the agency's annual appropriation under the authority of Section 31.

4.2 Audit examination has revealed that improvements could be made in respect of each of these accountability mechanisms to assist in providing the Government and the Parliament with a complete and accurate record of the use of Section 31 arrangements. These are discussed below.

Federal Register of Legislative Instruments

4.3 The purpose of the *Legislative Instruments Act 2003* (LI Act) was to establish a comprehensive regime for the registration, tabling, scrutiny and sunsetting (or automatic repeal) of Commonwealth legislative instruments.[136] The LI Act defines a legislative instrument as an instrument in writing that is of a legislative character made in the exercise of a power delegated by the Parliament.[137] An instrument is taken to be of a legislative character if:

(a) it determines the law or alters the content of the law, rather than applying the law in a particular case; and

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[136] Legislative Instruments Bill 2003, Explanatory Memorandum, p. 2.

[137] Subsection 5(1) of the LI Act.

(b) it has the direct or indirect effect of affecting a privilege or interest, imposing an obligation, creating a right, or varying or removing an obligation or right.[138]

4.4 The LI Act established the Federal Register of Legislative Instruments (FRLI), a publicly available register managed by AGD. Legislative instruments made on or after 1 January 2005 must, as soon as practicable after being made, be lodged in electronic form with AGD for registration. At the time of, or as soon as practicable after, the lodgement of the electronic version, the rule-maker must also lodge the original instrument.[139]

4.5 Instruments made before 1 January 2005 must be registered as follows:

(a) before 1 October 2006, for legislative instruments made in the five years prior to 1 January 2005[140]; and

(b) before 1 January 2008, for legislative instruments made earlier than that.

4.6 Legislative instruments must be laid before each House of the Parliament within six sitting days of that House after the registration of the instrument. Failure to do so causes the legislative instrument to cease to have effect immediately after the last day for it to be so laid.[141] Unless otherwise provided, a legislative instrument is subject to disallowance by a motion of a House of the Parliament. The LI Act also provides for the automatic repeal of legislative instruments after ten years from nominated dates. The purpose of that part of the Act is to ensure that legislative instruments are kept up to date and only remain in force for so long as they are needed.[142]

Application of the LI Act to Section 31 agreements

4.7 In December 2005, Finance advised ANAO that, due to the Constitutional effect of Section 31 agreements, it has consistently operated on the basis that, in the interests of accountability and disclosure to the

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[138] Subsection 5(2) of the LI Act. If a person or body having authority to make instruments of a particular kind is uncertain whether such instruments are legislative instruments, they may apply, in writing, to the Attorney-General to determine the matter (Section 10).

[139] See subsection 25(2) of the LI Act. Where the rule-maker cannot comply with that requirement, the Act provides for the lodgement of specified evidence of the text of the instrument.

[140] Section 29(1) of the LI Act originally required that legislative instruments made in the five years prior to 1 January 2005 be registered on FRLI before 1 January 2006. In November 2005, the *Legislative Instruments Amendment Regulations 2005 (No. 4)* extended the period for backcapture to before 1 October 2006.

[141] Section 38 of the LI Act.

[142] See Part 6 of the LI Act on sunsetting of legislative instruments.

Parliament, such agreements are properly regarded as legislative instruments and, therefore, should be registered on FRLI.

4.8 Subsection 5(3) of the LI Act specifies that an instrument that is registered is taken, by virtue of that registration and despite anything else in the Act, to be a legislative instrument. Section 31 agreements registered on FRLI since 1 January 2005 are, therefore, taken to be legislative instruments for the purposes of the LI Act. However, the Act identifies Section 31 agreements as legislative instruments that are not subject to the disallowance or sunsetting provisions of the Act.

Timeliness of registration

4.9 Parliament has recently shown an interest in obtaining additional information to that already publicly available regarding the operation of Section 31 agreements, including the types of receipts covered by agreements.[143] The registration of Section 31 agreements on FRLI will assist in this regard.[144] To improve the benefits obtained, such registration should be timely.

4.10 Finance is responsible for the lodgement of Section 31 agreements for registration. As at 15 December 2005, 56 of 61 agreements made between 1 January 2005 and 30 June 2005 had been registered on FRLI. Of those,

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[143] For example, Finance was asked at the 25 May 2005 Estimates Hearing of the Senate Finance and Public Administration Legislation Committee whether there is a list available of the types of receipts that may be retained by agencies under Section 31 agreements. Finance advised the Committee that there is no list, as the eligible receipts would be detailed in each individual agreement. Source: Senate Finance and Public Administration Legislation Committee, Proof Committee Hansard, Budget Estimates, 25 May 2005, F&PA 107.

[144] In this context, ANAO notes that a user of FRLI should be able to determine the parties to an agreement from its express terms. ANAO noted an example where this would not be the case. Subsection 31(2) of the FMA Act stipulates that, for items for which the Finance Minister is responsible, agreements are to be made with the Chief Executive of the agency. In all other cases, the agreement is to be made with the responsible Minister. The Department of Human Services (DHS) is located within the Finance and Administration portfolio. An agreement for DHS was signed on 22 December 2004 by the DHS Secretary (as Secretary) and a delegate of the Finance Minister. That agreement stated that it was made between the Minister for Finance and Administration and the Secretary of DHS. Under the terms of subsection 31(2), an agreement made between the Secretary and the Finance Minister would only be effective if the DHS appropriation item was an item for which the Finance Minister is responsible. Agreements for all Finance-portfolio agencies were re-made in late June 2005. In the course of that process, Finance sought legal advice as to whether the DHS agreement should be made with the Secretary or the Minister for Human Services. Finance was advised that, although arguments could be made to the contrary, the agreement should be made with the Minister, not the Secretary. A further agreement for DHS was made with the Minister for Human Services on 29 June 2005, with the Finance Secretary signing as delegate of the Finance Minister and the DHS Secretary signing for and on behalf of the Minister. In August 2005, AGS advised DHS that it was entitled to act on the basis that the December 2004 agreement was an agreement made between the Finance Minister and the Minister for Human Services which had been validly made by the Secretary by means of implied authorisation of the Minister, despite the fact that:

- the header of the agreement states that it is between the Minister for Finance and Administration and the Secretary of the Department of Human Services; and
- the signature block is expressed to be signed by the Secretary in her own name.

29 were registered within approximately a month of being made. However, it took up to three months to register a further 22 agreements, over three months for two agreements; and three agreements were registered more than five months after being made.[145] As at 15 December 2005, five agreements made in June 2005 had yet to be registered, including two that were the current agreements of the relevant agency as at that date.

4.11 In December 2005, Finance advised ANAO as follows:

> The report comments on the time it has taken to register section 31 agreements on the FRLI. Finance notes that this has largely been the result of the large number of section 31 agreements executed during 2005 due to the review of section 31 agreements. This has occurred at a time when the FRLI is in its first year of operation, and still being implemented. However, recent developments to the manner in which section 31 agreements are executed will ensure that the Parliament is more quickly made aware of the execution, variation or cancellation of a section 31 agreement in a timely manner. Following discussions with the Attorney-General's Department regarding the LI Act, Finance has recently redrafted the commencement clause of section 31 agreements and variations to specify that the agreement will commence upon registration on the FRLI. While there will still be scope to apply an agreement to amounts already received by an agency in certain circumstances (as discussed further in our response to Chapter 5), Finance proposes that future agreements be executed to commence upon registration on the FRLI (except in circumstances where the instrument is required to commence on a specific date after registration has occurred). As a result of this, section 31 agreements will be provided to Parliament within six sitting days of the instrument commencing.

Uncertain application

4.12 The LI Act provides that a legislative instrument made on or after 1 January 2005 takes effect from the day specified in the instrument for the purposes of the commencement of the instrument.[146] However, subsection 31(1) of the LI Act also provides that such legislative instruments are not enforceable by or against the Commonwealth, or by or against any other person or body, unless they have been registered.[147] On 6 September 2005, ANAO requested advice from Finance as to the application that provision may have to Section 31 agreements.

4.13 On 7 November 2005, Finance provided ANAO with advices it had obtained from the Office of Legislative Drafting and Publishing (OLDP) in

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[145] This includes an administered agreement for Finance made on 29 June 2005 (see footnote 150).

[146] Section 12(1).

[147] Instruments made prior to 1 January 2005 will, except in specified circumstances, cease to be enforceable if they are not lodged on FRLI by the last day for lodging.

AGD and AGS, which both concluded that, in the context of net appropriation agreements, Section 31 of the LI Act does not prevent an agency from relying on an unregistered agreement. However, in the context of resolving that issue, it became apparent that there is ongoing uncertainty regarding the extent to which the LI Act was intended to apply to Section 31 agreements.

4.14 In December 2004, OLDP agreed with Finance that Section 31 agreements were arguably legislative in character, although the question of whether they are legislative will depend on their content. OLDP advised that, to avoid confusion, Finance might wish to lodge all agreements, noting that, once registered, an agreement would be taken to be a legislative instrument.

4.15 Section 7 of the LI Act prescribes certain instruments that are declared not to be legislative instruments for the purposes of the Act, including instruments listed in Schedule 1 to the *Legislative Instruments Regulations 2004* (LI Regulations). Items in Schedule 1 that are relevant for the purposes of Section 31 agreements and associated variation and cancellation instruments are:

> Item 22. An agreement, contract or undertaking authorised to be made or given under legislation, or an instrument made under such an agreement, contract or undertaking.
>
> and
>
> Item 33. An instrument that varies or revokes an instrument that is not a legislative instrument.

4.16 In October 2005, OLDP advised Finance that: 'the argument that item 22 of Schedule 1 to the LI Regulations applies to net appropriation agreements is quite a strong one and is likely to be persuasive'. In that context, a Section 31 agreement would not be a legislative instrument for the purposes of the LI Act unless, and until, registered on FRLI. OLDP further advised that:

> It is unlikely, however, that item 22 of Schedule 1 to the [LI Regulations] would apply to a variation of a net appropriation agreement under subsection 31(4) of the FMA Act. As a variation is made unilaterally by the Minister, it is not itself an agreement. If the agreement is not a legislative instrument when the variation is made (that is, it is not legislative in character or is covered by an exemption such as item 22 of Schedule 1 to the [LI Regulations], and it has not been registered before the variation is made), item 33 of Schedule 1 to the [LI Regulations] will apply to the variation and it will not be a legislative instrument. However, if the agreement being varied is a legislative instrument (either because it is legislative in character or because it has been registered), item 33 of Schedule 1 to the [LI Regulations] will not apply and the variation will probably be legislative as well.

4.17 In November 2005, AGS advised Finance that, but for the application of the LI Regulations, the better view was that a Section 31 agreement was a

legislative instrument within the terms of subsection 5(2) of the LI Act. AGS further advised as follows:

> Item 22 of the LI Regs appears to remove section 31 agreements from the concept of legislative instruments. It might be argued that the reference to agreements do not include intra-Commonwealth agreements, but the more ordinary reading of item 22 is that it is broad enough to cover section 31 agreements. It may be that many of the items in Schedule 1 were put in on the assumption that matters covered by those items would not ordinarily be legislative instruments within the ordinary application of the Act but all doubt over the matter should be removed. The best course might be to check what AGD's policy purpose was underlying item 22, and note that in its application to section 31 agreements it excludes agreements that would otherwise be legislative instruments under the Act.
>
> On the assumption that section 31 agreements should be covered by the LI Act, in accordance with the ordinary application of section 5 of that Act, the simpler course would be to amend the LI Regulations to make it clear that item 22 was not intended to extend to section 31 agreements. The alternative involves the following convoluted analysis (i) the section 31 agreement is a legislative instrument under section 5; (ii) it is excluded by virtue of item 22; and (iii) it is brought back within the operation of the LI Act by registration.

4.18 On 14 October 2005, OLDP advised Finance that:

> Civil Justice Division [*in AGD]* have suggested that, if the [*LI Act*] does not apply to these agreements (as appears to be the case), then their registration under the [*LI Act*] does not seem desirable. If for some reason it is considered desirable, then perhaps you should consider requiring that the agreements do not commence until they are registered on the Federal Register of Legislative Instruments.

4.19 ANAO notes that both of the variation instruments executed by the Finance Secretary on 28 October 2005 in respect to agencies with a 'no agreement' period stipulated that the instrument would come into effect upon registration on FRLI. This was a different approach to that previously taken by Finance in respect to instruments relating to Section 31 of the FMA Act, as follows:

- Section 31 agreements executed since 1 January 2005 have stipulated a date of commencement or that they commenced upon being signed by the second signatory;
- The Cancellation Instrument executed by the Finance Secretary on 24 June 2005, which cancelled all agreements commencing on or before 30 June 2004 as at 30 June 2005, stipulated that: 'This instrument takes effect when it is made.' The instrument was registered on FRLI on 18 July 2005; and

- The Variation Instrument executed by the Finance Secretary on 24 June 2005, which varied current agreements to capture receipts previously received under 'ineffective' agreements, stated that it would commence on 30 June 2005. The instrument was registered on FRLI on 21 July 2005.

4.20 On 7 November 2005, Finance advised ANAO that it was considering the options proposed by AGS. In December 2005, Finance further advised as follows:

> Finance notes that the operation of the Legislative Instruments Act 2003 (LI Act) has been the subject of several pieces of legal advice obtained by Finance from the AGS and the Attorney-General's Department which are quoted in the report. While this advice may give the impression that the operation of the LI Act is uncertain, Finance's preference is to register section 31 agreements to ensure Parliament receives that transparency. Under subsection 5(3) of the LI Act, following registration on FRLI, section 31 agreements are deemed to be legislative instruments. Further, by providing for the commencement of agreements upon registration on the FRLI, Finance is ensuring that a section 31 agreement will be a legislative instrument for the total period of its operation. Finance will continue to work with the Attorney-General's Department to remove any remaining uncertainties.

Portfolio Budget Statement disclosures

4.21 The purpose of the PBS and PAES (as set out in Part A of agency PBSs, 'User Guide') is to inform Senators and Members of Parliament of the proposed allocation of resources to Government outcomes by agencies within the portfolio. The PBS and PAES facilitate understanding of the proposed appropriations in the annual Appropriation Bills. In this sense, the PBS and PAES are declared to be 'relevant documents' to the interpretation of the Bills according to Section 15AB of the *Acts Interpretation Act 1901*.

4.22 A part of providing information to Parliament on the allocation of resources to Government outcomes involves disclosing to Parliament the estimated amount of receipts, including Section 31 receipts, that are available to the agency for expenditure to contribute to the relevant outcome. ANAO identified areas in which agencies' disclosure of Section 31 receipts through their PBS could be improved.

Clearly identifying estimated section 31 receipts

4.23 Each year, Finance provides agencies with guidelines and a template to be used in the preparation of their PBS. The template provided to agencies for use in their 2005–06 PBS required estimated receipts from non-appropriation sources to be disclosed in a table identified as 'Other receipts available to be

used'. This table replaced the table previously used, 'Receipts from independent sources'.

4.24 In addition to amounts that an agency estimates will be collected under its departmental and/or administered Section 31 agreement(s), this table is required to also include receipts of CAC Act bodies that are available to be spent by the agency, estimated receipts to Special Accounts from non-appropriation sources and resources received free of charge. Although some agencies did identify a particular line item in the table as relating to Section 31 of the FMA Act, this was not specifically required. Accordingly, it was often not readily identifiable how much of the estimated receipts related to Section 31, and how much related to other purposes, including Special Accounts.

4.25 For example, Figure 4.1 sets out the 'Other receipts available to be used' table included in Finance's 2005–06 PBS. Finance reported Section 31 receipts totalling $6.8 million in its 2004–05 financial statements.

Figure 4.1

'Other receipts available to be used[(1)]' table in Finance 2005–06 PBS

	Estimated receipts 2004-05 $'000	Budget estimate 2005-06 $'000
Departmental other receipts		
Rent receipts	64 143	74 838
Insurance premiums	127 960	115 718
Insurance recoveries	10 336	6 389
Receipts from the domestic property divestment programme	45 827	5 053
Other	10 734	10 049
Total departmental other receipts available to be used	**259 000**	**212 047**
Administered other receipts		
Travel arrangement commission	3 350	3 350
Miscellaneous receipts	122	125
Total administered other receipts available to be used	**3 472**	**3 475**

Notes:

(1) This table replaces the former table 'Receipts from independent sources'. It represents own source receipts available for spending on departmental purposes.

Source: Portfolio Budget Statements 2005–06, Finance and Administration Portfolio, Budget Related Paper No. 1.9 A, p. 26.

4.26 In this context, the current presentation of estimated non-appropriation receipts does not always assist in providing users of the PBS with a clear understanding of the extent to which the relevant agency expects to increase its annual appropriation for amounts collected under authority of their Section 31 agreement. The guidance provided to agencies does not currently require that Section 31 receipts be separately identified in the relevant table in the PBS. Enhanced guidance in this area may assist in improving the utility of the table in this respect.

4.27 In December 2005, Finance advised ANAO as follows:

> Information on receipts available for use in PB Statements includes Section 31 receipts. Specific receipt items are identified by agencies where they are considered significant. Less significant items, which in some cases may include Section 31 receipts, are aggregated in 'other' to achieve a balance between the level of detail and significance in presentation.

4.28 ANAO's examination also identified that the accuracy and consistency of the Section 31 receipt estimates that are disclosed in agency PBSs could be improved, as the following examples demonstrate.

Finance

4.29 As Figure 4.1 shows, the 'Other receipts available to be used' table disclosed in Finance's 2005–06 PBS included estimated administered receipts of $3.475 million, including $3.35 million relating to travel arrangement commission collected under Outcome 3 ("Efficiently Functioning Parliament"). Receipts for this function have been included in Finance's PBS since 1999–2000 (see Figure 4.2).[148]

[148] Prior to 2005–06, these receipts were included in the 'Receipts from Independent Sources' tables included in the Finance PBS and PAES. As noted in Figure 4.1, that table was replaced in the 2005–06 PBS with the 'Other receipts available to be used' table.

Figure 4.2

Reporting of estimated travel commission receipts in Finance's PBSs

	99-00 $'000	00-01 $'000	01-02 $'000	02-03 $'000	03-04 $'000	04-05 $'000	05-06 $'000	Total $'000
PBS estimate	1 600[A]	1 600	1 304	3 000[B]	3 350	3 350	3 350	17 554
PAES revised estimate	1 600[A]	not separately disclosed	1 304	3 000[B]	3 350	3 350	n/a	>12 604

Notes:

A: Although the 1999–00 PBS and PAES did not identify estimated receipts for travel commission, the prior year comparative disclosed in the 2000–01 PBS reported a 1999–00 estimate of $1 600 000.

B: Although the 2002–03 PBS and PAES did not identify estimated receipts for travel commission, the prior year comparative disclosed in the 2003–04 PBS reported a 2002–03 estimate of $3 000 000.

Source: Department of Finance and Administration PBS and PAES 1999–00 to 2005–06.

4.30 The actual travel commission payments received by Finance in 2003–04, totalling $688 355, were substantially less than the estimate of $3.35 million reported in both the 2003–04 PBS and PAES. ANAO understands that travel commission receipts have further reduced under a revised travel contract Finance has entered into with one airline. In seeking the Secretary's signature to a revised administered Section 31 agreement on 23 June 2005, Finance advised that these receipts would amount to approximately $100 000 in 2004–05. However, this trend has not been reflected in the estimated receipts reported in the 2004–05 PBS and PAES, or the 2005–06 PBS, which continued to report estimated receipts of $3.35 million.

4.31 Travel commission receipts were purportedly covered by an administered Section 31 agreement since 1999–2000. However, the table entitled 'Total Resourcing for Outcome 3', separately disclosed in the PBS, has not included any revenue from other sources in the total estimated administered resourcing for that Outcome. Further, despite receiving eligible receipts in each year, and the inclusion of these amounts in the estimated receipts available to be used reported in its PBS and PAES, Finance's financial statements for each year have not reported any Section 31 receipts as having been added to the available appropriation of its administered item for

Outcome 3. Nor has Finance sought to utilise the administered appropriation arising from those receipts.[149]

Health

4.32 Another example noted by ANAO related to the Department of Health and Ageing (Health). Figure 4.3 identifies the amounts disclosed as departmental Section 31 receipts in Health's PBS, PAES and Annual Report in the period 2000–01 to 2005–06.

Figure 4.3

Reporting of Section 31 receipts in Health PBS, PAES and Annual Reports

	00-01 $'000	01-02 $'000	02-03 $'000	03-04 $'000	04-05 $'000	05-06 $'000
PBS current year estimate	9 681	53 666	52989	66 577	113 864	85 006
PAES revised estimate	51 685	52 927	52 989	72 695	77 933	n/a
Annual Report	71 208	66 455	257 326	179 726[A]	75 128	n/a

Note A: Health's 2003–04 financial statements disclosed $245 331 000 as having been added to the Department's annual appropriation as Section 31 receipts. This amount was revised in the prior year comparative disclosed in Health's 2004–05 financial statements to exclude Special Account receipts incorrectly disclosed as Section 31 receipts.

Source: ANAO analysis of Department of Health and Ageing PBS, PAES and Annual Reports.

4.33 The significant increase in estimated Section 31 receipts in Health's 2000–01 PAES and Annual Report from the amount disclosed in the 2000–01 PBS relates to the adoption of the practice of amalgamating Special Account receipts into the amounts disclosed as Section 31 receipts, despite the significant difference in the nature of the receipts. As noted in Figure 4.3, adjustments in relation to this issue were made in Health's 2004–05 financial statements, as part of the process of identifying the Section 31 receipts affected by the 'ineffective' agreements relied on by Health for the period 1 July 1998 to 28 June 2005 (as discussed in Chapter 3).

4.34 The significant disparities between the Section 31 receipts disclosed by Health in its PBS, PAES and Annual Reports in 2002–03 and 2003–04 largely relate to the exclusion of receipts relating to CRS Australia (CRS) from the

[149] Finance's administered Section 31 agreements relating to Outcome 3 were subsequently found in this performance audit to have been ineffectively executed. Until that time, however, the agency had considered its agreements to be effective. A new administered agreement for Outcome 3, executed by the Finance Minister and the Finance Secretary on 29 June 2005, was unable to operate in the manner intended because it referred, in error, to increasing Finance's Departmental item rather than the Administered item for Outcome 3. A delegate of the Minister for Finance and Administration executed an instrument cancelling the administered agreement on 26 September 2005 (see the *Financial Management and Accountability Net Appropriation Agreement: Department of Finance and Administration – Administered Expenses Cancellation 2005).* Both the June 2005 administered agreement and the September 2005 cancellation instrument were registered on FRLI on 12 December 2005. In the absence of an effective administered agreement, the relevant receipts are not available to Finance to spend.

Section 31 receipts identified in the PBS and PAES.[150] The department's 2003–04 and 2004–05 PBS and PAES noted that CRS was not included in the reported Section 31 receipts because: 'their revenue is largely from the Department of Family and Community Services and not from independent sources.' This approach did not appropriately recognise the requirement for Health's Section 31 agreement to apply in respect to these amounts before they could be expended in respect to CRS's delivery of services.

Financial reporting of annual appropriations

4.35 The financial reporting requirements for Australian Government agencies and authorities are contained in the FMOs made under Section 63 of the FMA Act and Section 48 of the CAC Act. The FMOs provide minimum mandatory disclosure and reporting requirements for each agency and authority. The mandatory requirements of the Finance Minister are combined with guidance (formally identified as Explanatory Notes) prepared by Finance. They are published in a single document.

4.36 As part of their annual financial reporting to the Parliament, FMA Act agencies are required to account for:

- the appropriations available to them;
- the extent to which payments were made from the CRF under authority of those appropriations; and
- for appropriations with a financial limit, the amount of appropriation still available as at 30 June of the relevant financial year (as represented by cash on hand and at bank, GST receivable and appropriation receivable from the OPA).

4.37 That accounting is provided through disclosure tables included as notes to an agency's annual financial statements, in accordance with the requirements of the FMOs. Providing the Government and the Parliament with an accurate and complete accounting of their use of appropriations enables Australian Government agencies to discharge their accountability for the purposes of Section 83 of the Constitution.[151]

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[150] In 2002–03, 2003–04 and part of 2004–05, CRS was part of Health. CRS is the sole provider of Government funded rehabilitation services provided under the *Disability Services Act 1986*. It is fully funded via purchaser provider arrangements with both government and non-government entities. The bulk of CRS funding relates to amounts received from other departments for the purchase of services. Those amounts could only be retained and spent under authority of Health's Section 31 agreement. Although included in the Section 31 receipts reported in Health's Annual Report, those amounts were excluded from the departmental Section 31 receipts disclosed in its PBS and PAES.

[151] See clause 2C.1.1, Finance Minister's Orders, *Schedule 1: Requirements for the Preparation of Financial Statements of Australian Government Entities, Reporting periods ending on or after 30 June 2004, unless amended*, Department of Finance and Administration, p. 35.

FMA Act provisions relating to appropriations

4.38 The FMA Act provides various mechanisms by which a lawful appropriation may be provided to support the retention and expenditure by an agency of amounts received from non-appropriation sources.

4.39 As noted, Section 31 of the FMA Act provides a means by which agencies can increase their annual departmental and, in some cases, administered appropriations by the amount of relevant receipts covered by their Section 31 agreement. An alternative mechanism for the retention and spending of receipts is a Special Account. Sections 20 and 21 of the FMA Act provide a standing appropriation for expenditure for the purposes of a Special Account, up to the balance for the time being of the Account.

4.40 Appropriations and other receipts are to be credited to a Special Account in accordance with the provisions of the establishing Determination or legislation. The balance of a Special Account represents amounts within the CRF that are hypothecated, or set aside, for the specific purposes of that Account.

4.41 Other provisions of the FMA Act that are relevant to appropriations management by agencies are more in the nature of 'recycling' provisions. That is, they do not provide an effective net increase in the appropriation otherwise available for expenditure on approved Outcomes. Relevant provisions are:

- Section 28, which applies if an Act or other law requires or permits the repayment of an amount received by the Commonwealth and, apart from that section, there is no appropriation for the repayment;
- Section 30, which provides for amounts previously paid out of an appropriation and then repaid to the Commonwealth to be re-credited to the appropriation from which the original payment was made, such that the appropriation is available to be paid out again;
- Section 30A, which operates to automatically increase appropriations for the recoverable GST component of payments made; and
- Section 32, which provides the Finance Minister with the authority to issue directions transferring appropriations between agencies upon a change of agency functions.

4.42 These provisions serve discrete purposes in agencies' appropriation management processes. In that context, it is important that agencies provide a clear and accurate accounting of the extent to which they have exercised the authority provided by Section 31 and other provisions of the FMA Act to increase their available appropriations. Inaccuracies in reporting can provide the Government and the Parliament with a misleading impression of the extent

to which an agency has actually generated additional appropriation authority through its transactions with other entities.

4.43 The operation of Section 28 of the FMA Act was examined in the course of ANAO's recent performance audit of Financial Management of Special Appropriations.[152] Finance Circular No. 2004/08, *Appropriation for Repayments under Section 28 of the FMA Act*, was issued by Finance in August 2004.

4.44 Issues concerning the operation of Sections 30 and 32 arose during the course of this current performance audit. As outlined in Chapter 2, deficiencies were identified in the manner in which appropriations were transferred to BoM upon its establishment, including the absence of Section 32 directions to support the transfer of cash. This contributed to BoM breaching Section 83 of the Constitution.

Consolidating Special Account receipts into Section 31 receipts

4.45 ANAO identified four agencies, DITR, Health, the Australian Radiation Protection and Nuclear Safety Agency (ARPANSA) and ACIAR, that had, in a number of financial years, incorrectly consolidated the debits, credits and balances relating to departmental Special Accounts into the disclosures provided in respect to their departmental annual appropriation.

4.46 Those agencies have disclosed independent receipts relating to Special Accounts as also being amounts added to their annual appropriation as Section 31 receipts. Consequently, three of the agencies have significantly overstated the amount able to be legitimately added to their annual appropriation under authority of their Section 31 agreement.[153] The fourth agency, ACIAR, has no such authority, as it does not have a Section 31 agreement.[154] However, ACIAR reported its Special Account receipts as also being Section 31 receipts in 2000–01 and 2001–02.[155]

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[152] ANAO Audit Report No.15 2004–05, *Financial Management of Special Appropriations,* Canberra, 23 November 2004, pp. 41–43.

[153] For example, of the $34.26 million disclosed by DITR as being Section 31 receipts credited to its annual appropriation in 2003–04, $32 million actually related to Special Account receipts. Similarly, Health included Special Account receipts totalling $65.6 million in the $245.3 million of Section 31 receipts disclosed in 2003–04. All of the $8.3 million of Section 31 receipts disclosed by ARPANSA in 2003–04 related to receipts to the ARPANSA Special Account. Each of those agencies made similar errors in prior financial years.

[154] ACIAR operates through a Special Account. Accordingly, it does not require a Section 31 agreement in order to have the appropriation authority to spend amounts received from independent sources. Another of the four agencies noted, ARPANSA, also operates through a Special Account, but has also executed Section 31 agreements.

[155] In 1999–2000, Special Account receipts credited to its annual appropriation were incorrectly reported as being made under authority of Section 20 of the FMA Act. In 2002–03 and 2003–04, the amounts were disclosed as annotations credited to the annual appropriation as 'other annotations–revenue credited to Special Account', without citing an authority.

4.47 Each of those agencies have reported payments made from the CRF under the special appropriations provided for Special Accounts as also being payments made under their annual appropriation. This has overstated the extent to which actual drawings were made on the CRF by each agency in a given financial year. To the extent the amount of Special Account receipts included in the annual appropriation differs from the Special Account payments also included, the annual appropriation available balance reported by each agency will be incorrect.

4.48 DITR, Health and ARPANSA excluded Special Account receipts from the Section 31 receipts disclosed in their 2004–05 financial statements. Health and ARPANSA also included adjustments to the reported annual appropriation balance in relation to this issue. DITR advised ANAO that it would make any necessary adjustments in its 2005–06 financial statements.

4.49 Transactions relating to departmental Special Accounts are consolidated into the primary financial statements of the relevant agency, including the Statement of Cash Flows from which most agencies derive the Section 31 receipts to be disclosed each year. However, the appropriations provided to agencies by the annual Appropriation Acts are separate and distinct from the special appropriations provided by Sections 20 and 21 of the FMA Act in respect to the balance of each Special Account. The amounts debited and credited to each of those appropriations, and their respective available balances, must be accounted for separately.

Disclosing repaid amounts

4.50 Section 30 of the FMA Act provides that if an amount is repaid to the Commonwealth after having been paid out of the CRF under the authority of an appropriation, then the appropriation has effect as if the amount had not been paid out. The amount repaid will be available to be paid out again, subject to any time limits that apply to the appropriation. Upon receipt, a repaid amount is, by operation of law, automatically re-credited to the appropriation from which the amount was originally paid.[156] In this respect, in December 2003, AGS advised one agency as follows:

> The obvious purpose underlying s 30 of the FMA Act is to ensure that the full amount that Parliament has appropriated for a *particular* purpose is available for expenditure on that purpose, but only for that purpose and subject to any time limits that apply to doing so.

[156] In this respect, in October 2004, AGS advised Finance as follows: 'Where it applies, s30 has effect without any particular action by the agency involved: the appropriation has effect as if the amount had not been paid out. It cannot have been intended that an amount could be re-credited by s30 but also be re-credited under a s31 agreement.'

4.51 Four of the six agencies reviewed in detail in this audit did not report any Section 30 refunds to appropriations in any of the financial years 1999–2000 to 2003–04.[157] AusAID reported Section 30 amounts in 1999–00 to 2001–02, but not in 2002–03 or 2003–04. BoM disclosed Section 30 amounts in both 2002–03 (its first year of operation as a separate agency) and 2003–04. More broadly, only 14 per cent of FMA Act agencies disclosed any amounts as being credited to their appropriations under authority of Section 30 in 2003–04.[158]

4.52 In the agencies examined in detail, the non-reporting of amounts re-credited to appropriations by operation of Section 30 arose from agencies either netting repaid amounts from the amount disclosed as payments made from the relevant appropriation[159], and/or disclosing repaid amounts as Section 31 receipts.[160] Although in both cases there is no net effect on the reported balance of the relevant appropriation, neither treatment provides the Government and the Parliament with an accurate acquittal of the agency's appropriation authority, and the use made of that authority.[161] In particular:

- netting repaid amounts from the amount disclosed as payments made from the CRF has the effect of understating the extent to which cash has

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[157] Defence, DIMIA, DITR and Finance. DITR's 2002–03 and 2003–04 financial statements erroneously disclosed a return of appropriation to the Budget as a negative Section 30 refund.

[158] Since 1999–2000, the FMOs have required agencies to disclose the amount re-credited under Section 30 to each appropriation available to them.

[159] For example, Finance advised ANAO in April 2005 that, in respect to its departmental processes, repayments received had been netted from the payments disclosed as being made from its annual appropriation, rather than being disclosed as amounts credited to the appropriation under Section 30.

[160] For example, the sample of 2003–04 Section 31 transactions examined in Defence included repayments totalling at least $842 538. Defence disclosed no amounts as having been re-credited to its appropriations under operation of Section 30.

[161] A further issue in this regard noted by ANAO related to employee compensation payments agencies received from Comcare. In many circumstances, the agency will continue to pay wages and salary to injured employees while awaiting determination of a Comcare claim, and then seek to be reimbursed from the compensation payment. It has been common for agencies to view such amounts as receipts to which their Section 31 agreement applies. In this respect, AGS's October 2004 advice to Finance was that it is Section 30 that operates to re-credit the relevant appropriation for amounts received from employees in relation to Comcare payments. AGS advised Finance that 'where the employing agency is legally part of the Commonwealth (generally, agencies subject to the FMA Act), and the employee consents to set off, s 30 will operate to re-credit the relevant appropriation. In these circumstances, in our view, there is no room for a net appropriation agreement to operate.' ANAO identified that one of the agencies examined in this performance audit, BoM, had credited compensation payments totalling $684 398 received from Comcare in 2002–03 and 2003–04 directly to its annual appropriation, as Section 31 receipts, without obtaining the express consent of the relevant employees, in contravention of the requirements of the *Safety, Rehabilitation and Compensation Act 1998* (This issue was addressed in ANAO Audit Report No. 18 2002–03, *Management of Trust Monies*, Canberra, 27 November 2002, pp. 36 to 38). An Other Trust Monies Special Account for BoM was established on 19 August 2005 to enable the agency to treat payments received from Comcare in a manner that is consistent with their trust money status. In August 2005, BoM advised ANAO that it had now obtained employee consent to it reimbursing its departmental appropriations from the Comcare payments, and that the practice of crediting Comcare payments as Section 31 receipts would be discontinued. BoM disclosed these amounts as Section 30 refunds in its 2004–05 financial statements.

been drawn from the CRF under the relevant appropriation. It also does not provide disclosure of the appropriation that has arisen under authority of Section 30; and

- disclosing repaid amounts as Section 31 receipts can put agencies at risk of purporting to increase their annual appropriation for amounts that had originally been paid from another appropriation, such as a special appropriation or a Special Account. This would result in the agency misstating the balance of both appropriations.

4.53 In response to the issues raised in this performance audit, on 30 June 2005 Finance issued Finance Circular No. 2005/08, *Section 30 of the FMA Act – Reinstatement of appropriations for amounts repaid*. That Circular provided guidance to agencies on the operation of Section 30, including on the distinction that should be drawn between amounts subject to that provision and receipts to which Section 31 applies; the accounting treatment that should be applied to Section 30 receipts; and the requirement for agencies to disclose the repayments to which Section 30 applies for each appropriation in the appropriation acquittal notes to the financial statements.

4.54 In July 2005, AusAID advised ANAO of its revised revenue policy and procedures, which had been amended to provide for the correct reporting and disclosure of amounts eligible to be credited to appropriations. Similarly, the 2004–05 financial statements of Finance, Defence and DIMIA included disclosure of refunds credited to appropriations under authority of Section 30. DITR did not disclose any Section 30 refunds in 2004–05. There was some improvement in this area overall, with the percentage of agencies that reported Section 30 refunds in 2004–05 increasing to 39 per cent.

Non-cash and ineligible items included in reported Section 31 receipts

4.55 As part of the transactions of an agency, Section 31 receipts are included in both the Statement of Financial Performance (generally as other revenue from independent sources) and in the Statement of Cash Flows. However, it should be noted that the financial statements reflect and record economic activity, which is a different concept to the legal ability to spend moneys. Accordingly, there are differences between accounting against appropriations (essentially a cash based compliance measure) and accounting for financial statement purposes (essentially an accrual based assessment of financial performance and financial position).[162]

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[162] *Agency Banking Framework – Guidance Manual*, Fourth Edition, Department of Finance and Administration, October 2003, p. 12.

4.56 The amount by which an appropriation item is increased by operation of a Section 31 agreement is limited to the amount of relevant receipts received. Reflecting the cash-based nature of the CRF, relevant receipts are limited to cash receipts. Accrued revenue not yet received and other non-cash amounts, such as resources received free of charge, may not be included.

4.57 Each of the six agencies examined in detail in this audit derived the Section 31 receipts disclosed in their 2003–04 financial statements from their accrual-based financial accounting systems and financial statements. In each case, errors in the derivation process led to the agency misstating the extent to which it had increased its annual appropriation under authority of Section 31.[163] ANAO also noted instances where ineligible amounts, including non-cash transactions, were included in the Section 31 annotation.[164]

4.58 ANAO also identified errors in the reporting of Section 31 receipts by four of those agencies in at least one prior financial year. For example, the Section 31 receipts disclosed by Defence for 1999–2000 were understated by $61.7 million.[165] Errors in past reporting of Section 31 receipts, or other elements of appropriations disclosures, by other agencies were also identified in the course of calculating the receipts that were affected by an agency having an 'ineffective' or 'in doubt' agreement. While the errors identified were generally not material in terms of the relevant agencies' primary financial statements, accuracy in appropriation disclosures is important in respect to agencies' accountability obligations. Further, the 2003–04 FMOs stipulated that the disclosures required in respect of appropriations were material by nature.[166]

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[163] In the case of Finance, BoM and DITR, similar errors were also reflected in the payments reported as having been made in 2003–04 from their annual appropriations.

[164] For example:

- $5.69 million relating to compensatory work accepted by Defence in lieu of liquidated damages (that is, no cash was received but the contractor undertook compensatory work in lieu of paying liquidated damages); and
- $100 000 received by Finance for payment to the Commonwealth of an agreed settlement in relation to a dispute that had arisen in respect to an asset sale process. An adjustment to correct this treatment was included Finance's 2004–05 financial statements.

[165] An amount of $590.037 million was originally credited to Defence's annual appropriation as Section 31 receipts in its 1999–2000 financial statements. That amount was changed without explanation in the 2000–01 financial statements to $374.910 million. Both reported amounts were incorrect. The basis of the originally reported amount is unclear. The revised amount was incorrectly based on the accrual revenue reported in 1999–2000. Cash receipts in that year totalled $436.607 million. Accordingly, Section 31 receipts credited in 1999–2000 were overstated by $153.43 million (35 percent); and understated by $61.697 million (14 percent) in the revised amount disclosed in 2000–01. As a consequence, the reported appropriation balance carried forward in each year since 2000–01 has been incorrect.

[166] Finance Minister's Orders, op. cit., clause 2C.2, p. 35. This clause was not included in the 2004–05 FMOs.

Addressing reporting and disclosure issues

4.59 The primary focus of ANAO's financial statement audits has been on the appropriateness of the reporting and presentation of the financial statements. However, where legislative breaches have been identified that are material to the reporting and presentation of the financial statements, they have been brought to attention in the audit opinion.

4.60 Recent ANAO performance audit reports have brought to the attention of the Parliament quite widespread difficulties in implementing and complying with key legislative provisions, particularly in relation to the FMA Act.[167] Finance has also noted, in its most recent Annual Report, that a number of audit reports have identified scope for improvements in the financial framework, predominantly in agencies' application of the framework.[168] Through its inquiries on these audit reports, the Joint Committee of Public Accounts and Audit has emphasised the importance it places on compliance with legislation that establishes the financial framework.

4.61 Against this background, there will be an increased focus on legislative compliance as part of ANAO's future financial statement audit coverage, as a supplement to the conventional financial statement audit.[169] This will involve confirming the presence of key documents or authorities, and sample testing of relevant transactions directed at obtaining assurance about entities' compliance with key aspects of legislative compliance in relation to annual appropriations, special appropriations, annotated appropriations (through Section 31 arrangements) and special accounts. This will not provide a guarantee that all legislative breaches will be identified, but will give reasonable assurance as to the state of legislative compliance in key areas.

4.62 Nevertheless, it is agencies' responsibility to comply with relevant legislation. Further, in terms of appropriation management, Section 48 of the FMA Act imposes a positive duty upon each agency Chief Executive to ensure that appropriations are lawfully available before spending funds. Agency Chief Executives are also responsible for the maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error.

4.63 In this context, improvements are required to agencies' reporting and disclosure of appropriations, including in their PBS and PAES. A number of agencies moved to address reporting issues identified in this performance audit in their 2004–05 financial statements.

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[167] Australian National Audit Office, *Annual Report 2004–2005*, Canberra, September 2005, p. 2.

[168] Department of Finance and Administration, *2004–05 Annual Report*, op. cit., pp. 22 and 34.

[169] In this respect, the objective of an audit of a financial report is to enable the auditor to express an opinion whether the financial report is prepared, in all material respects, in accordance with the Finance Minister's Orders, which include the application of the Australian Accounting Standards.

5. Financial Framework Enhancement Opportunities

This chapter discusses opportunities for enhancing the financial framework as it operates in respect to net appropriations.

Retrospective application of net appropriation agreements

5.1 It has been a common practice for agencies to enter into Section 31 agreements some time after the commencement of the period to which the agreement is then purported to apply. Nearly half of the Section 31 agreements made to 30 June 2005 had been applied retrospectively to amounts received prior to the agreement being executed.

5.2 Figure 5.1 sets out the proportion of agreements executed in each financial year since 1997–98 that were expressed in a manner intended to provide a net appropriation in respect to amounts previously received.

Figure 5.1

Agreements made in each financial year 1997–98 to 2004–05 that applied to amounts previously received

Year agreement made	Number of agreements examined	Number of agreements with application backdated		Number of months of intended retrospective application (number expressed as percentage of total agreements made in financial year)							
				<1 month		1 to 6 months		6 to 12 months		>1 year	
1997-98[A]	19	10	53%	0	0%	5	28%	5	28%	0	0%
1998-99	78	44	56%	1	1%	7	9%	36	46%	0	0%
1999-00	26	22	85%	8	31%	10	38%	3	12%	1	4%
2000-01	10	9	90%	4	40%	1	10%	3	30%	1	10%
2001-02	7	5	72%	1	14%	2	29%	2	29%	0	0%
2002-03	1	1	100%	1	100%	0	0%	0	0%	0	0%
2003-04	3	3	100%	0	0%	2	67%	0	0%	1	33%
2004-05	87	19	22%	3	3%	4	5%	8	9%	4	5%
Total	**231**	**113**	**49%**	**18**	**8%**	**31**	**13%**	**57**	**25%**	**7**	**3%**

Note A: Transitional arrangements provided for net appropriation agreements made prior to 1 January 1998 to continue to operate for the remainder of 1997–98, as if they had been made under Section 31 of the FMA Act. Any agreements made from 1 January 1998 onwards, were made under Section 31.

Source: ANAO analysis of Section 31 agreements made 1 January 1998 to 30 June 2005.

5.3 Although 64 per cent of Section 31 agreements made between 1997–98 and 2001–02 were expressed to apply from a date prior to the agreement being signed, the first evidence of Finance or other agencies seeking legal advice regarding the capacity for agreements to operate in that manner was in April 2002. That was advice obtained by Finance from AGS in respect to the Australian Research Council, for which no Section 31 agreement had been made at the time of its establishment on 1 July 2001. Finance was advised that it would be possible to enter into an agreement in April 2002 that applied to amounts received by that agency since 1 July 2001.

5.4 In forming this view, AGS noted that there is nothing in Section 31 of the FMA Act which expressly indicates that agreements may only operate prospectively. The legal advice further advised that, although there is typically a general presumption against powers conferred by Acts being construed as being capable of being exercised with retrospective effect, that presumption is rebuttable. Finance was advised that the presumption against retrospectivity is relatively weak in a context such as Section 31 agreements, where individual rights and liabilities are not affected, and where what results concerns only the internal accounting practices of the Commonwealth.

5.5 In July 2004, AGS further advised Finance that, in its view, a Section 31 agreement could also be expressed to cover receipts from previous financial years.[170] The legal advice stated that the language of Section 31 is broad and there seems to be no compelling reason to read it as preventing the capture of previous receipts if the Finance Minister considers that appropriate. This view was confirmed in legal advice provided to Finance in June 2005.

Retrospective application where amounts already expended

5.6 However, the legal advice has also stated that the appropriation item in the annual Appropriation Act may not be increased by the amount of receipts covered by a Section 31 agreement until such time as the agreement is executed. In this respect, AGS has consistently advised agencies that it is not possible to retrospectively provide an appropriation to cover expenditure that has already been made.

5.7 Accordingly, while legal advice is that it is possible to apply Section 31 agreements to amounts already received, care must be taken in how such amounts are handled prior to an agreement being signed. Retaining cash receipts for significant periods in anticipation of subsequently obtaining the necessary appropriation authority to spend those amounts, or operating for a

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[170] ANAO notes that prior to obtaining that advice, Finance had executed at least one agreement that was expressed to apply to amounts received in a previous financial year (the agreement signed for BoM by the Finance delegate on 8 June 2004). In December 2005, Finance advised ANAO that it did so based on its view that the language of Section 31 was broad and did not appear to operate to prevent capturing these receipts.

period of time as if that authority existed when it did not, may put an agency at risk of spending in excess of its legally available appropriation. In that context, the approach taken in many cases to applying Section 31 agreements retrospectively has not contributed to the orderly governance of appropriations by agencies.

Circumstances in which retrospectivity has been used

5.8 In accordance with the provisions of the FMA Act, Section 31 agreements are usually expressed so as to apply for an open-ended period. Accordingly, where an agency replaces an existing, effective agreement, it is usually doing so for the purpose of changing, or adding to, the eligible receipts specified in the agreement. This has been the case with 30 agreements that have been applied to amounts received prior to the agreement being executed.

5.9 ANAO considers that, where an agency identifies a type of receipt in respect of which its existing agreement does not apply, or where there is uncertainty as to whether its agreement applies, it is important that Finance obtain adequate assurance that the agency has not previously added to its appropriation, or spent, amounts relating to the receipts in question before agreeing to retrospective application of the amended agreement. This has not always occurred in the past, although a greater focus has been applied to such matters in more recent times.

5.10 The most significant uses of the capacity to apply Section 31 agreements retrospectively to amounts previously received were the variation instruments executed by the Finance Secretary in June and October 2005 in response to issues raised in this performance audit. The instruments relating to periods not covered by an agreement were discussed in Chapter 2. The instrument relating to 'ineffective' agreements was discussed in Chapter 3.

5.11 Prior to that, the most frequent circumstance in which agencies had sought to have an agreement apply to amounts previously received has been where the agency had been retaining non-appropriation amounts without having a current agreement in place. This has been the case in 70 per cent of the instances of retrospective application of Section 31 agreements, and was due to either:

(a) a previous agreement having expired; or

(b) a new agency having operated for some period before a Section 31 agreement was executed.

Prior agreement expired

5.12 All of the 44 agreements executed during the 1998–99 financial year for use in that year were expressed to 'operate' from an earlier date, typically 1 July 1998. Of those, 82 per cent were backdated by between six and

12 months. This arose due to delays by a large number of agencies in replacing agreements that had expired on 30 June 1998.[171]

5.13 As a consequence, many agencies operated for a large part of the 1998–99 financial year without having a net appropriation agreement in place. For most agencies, it is difficult to establish, from the available end-of-financial year reporting, whether their spending exceeded the appropriation available under the Appropriation Acts prior to their agreement being signed. However, as was noted in Chapter 2, at least one agency, Centrelink, spent $1.56 billion in Section 31 receipts prior to having an agreement in place for 1998–99.

Establishing an agency's first Section 31 agreement

5.14 The FMA Act applies to Departments of State, Parliamentary Departments and prescribed agencies. Departments are created by order of the Governor-General in Council, in accordance with the Administrative Arrangements Order. Prescribed agencies are those agencies identified in Schedule 1 to the *Financial Management and Accountability Regulations 1997*, as amended.

5.15 Once created, an agency is required to separately comply with all financial management and reporting obligations set out in the FMA Act and its supporting Regulations and Orders. In particular, a new agency requires appropriation authority in its own right in order to validly spend money from the CRF. In that context, a Section 31 agreement must be established in respect of a newly created or prescribed agency before that agency will have authority to retain and spend amounts received from non-appropriation sources.

5.16 Some newly created agencies have had agreements executed in a timely manner after being established. However, ANAO identified a number of examples in which there was considerable delay in establishing a Section 31 agreement for a newly created agency (see Figure 5.2).[172]

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[171] Transitional arrangements put in place in respect to the commencement of the FMA Act on 1 January 1998 enabled existing Section 35 agreements to continue to operate for the remainder of the 1997–98 financial year. Regulation 24 of the *Audit (Transitional and Miscellaneous) Regulations 1997* provided that an agreement in force immediately before 1 January 1998, under the net annotated appropriation provisions of the 1997–98 annual Appropriation Act No. 1 and Parliamentary Department Appropriation Act, had effect on and after 1 January 1998 as if it were made under Section 31 of the FMA Act. Since agreements made under those provisions had to be renewed annually, agencies' existing agreements were expressed so as to apply to the 1997–98 financial year only. Accordingly, agencies required a new agreement to operate from 1 July 1998 onwards. This was reflected in advice provided by Finance which advised that, due to the transitional arrangements: 'Section 35 agreements made before 1 January 1998 will remain valid until the end of the 1997/98 financial year without any special action being required from Budget officers.' (Budget Circular 1997/107, *Financial Management Act 1997 – Implications for Section 35 agreements*, 23 December 1997). Also, some agencies had signed Section 31 agreements after 1 January 1998 that applied to part or all of 1997–98, but which specified that they expired on 30 June 1998.

[172] A Section 31 agreement for the National Water Commission was executed on 18 May 2005, just over three months after it was prescribed as an FMA Act agency on 15 February 2005. In December 2005, the Commission advised ANAO that no monies covered by the agreement were received until two months after the agreement became effective.

Figure 5.2

New agencies for which a Section 31 agreement was executed over three months after the agency was prescribed/created

Agency	Date prescribed/ created	Date Section 31 agreement executed	Months taken to execute Section 31 agreement
Australian Greenhouse Office	1 July 2000[A]	25 June 2001	12
Australian Research Council	1 July 2001	25 June 2002	11.5
Biosecurity Australia	1 Dec 2004	24 June 2005	7
Bureau of Meteorology	12 Sep 2002	8 June 2004	21
Inspector-General of Taxation	7 Aug 2003[B]	17 Feb 2005	18
National Blood Authority	1 July 2003	7 March 2005	20[C]
National Oceans Office	1 July 2001	28 June 2002	11.5
National Office for the Information Economy	1 July 2001	19 Nov 2001	4
Office of the Renewable Energy Regulator	1 July 2003	26 May 2005	23[D]

Notes:

[A] The Australian Greenhouse Office was prescribed in the FMA Regulations of 21 May 1999, but did not receive direct appropriation funding until the 2000–01 financial year (it operated through a Special Account during that period). As a Section 31 agreement can only operate in conjunction with a marked appropriation item, the delay in establishing an agreement has been calculated from 1 July 2000.

[B] IGT was prescribed in the FMA Regulations of 1 July 2003, and established by the *Inspector-General of Taxation Act 2003* on 7 August 2003. The Section 31 agreement executed for IGT on 17 February 2005 stated that it would apply to amounts previously received on or after 7 August 2003. Accordingly, the time taken to establish an agreement has been calculated from 7 August 2003.

[C] In July 2005, NBA advised ANAO that, while the process followed in establishing its Section 31 agreement may have been long, it had wanted to ensure that the agreement was robust and accounted for all possible receipts that could eventuate.

[D] Appropriation was transferred to ORER from the Australian Greenhouse Office under two Section 32 directions. AGS have advised that a newly prescribed agency can be enabled to spend receipts by means of a Section 31 agreement that is expressed to relate to the appropriation transferred to it under Section 32. Further, a departmental item for ORER was included in *Annual Appropriation Act (No.3) 2003–04*. In that context, ORER had a departmental appropriation item available to it in 2003–04 for the purposes of Section 31. In December 2005, the Renewable Energy Regulator advised ANAO that: 'ORER had during [*the 23 month period]* on two separate occasions approached Finance to establish a Section 31 agreement. On the first occasion (beginning about December 2003), the ORER was advised by Finance that a Section 31 agreement was not required by the ORER. On the second occasion (earlier this year), the ORER executed a Section 31 agreement with Finance within days of me receiving from the Minister for the Environment and Heritage his authorisation to enter into net appropriation agreements. The total time involved in developing, agreeing (with Finance) and executing the agreement was about one month. To be clear, the ORER was not attempting to execute a Section 31 agreement with Finance for the entire period 1 July 2003 through to 26 May 2005". In this respect, ANAO notes that the Section 31 agreement executed for ORER on 26 May 2005 was expressed to retrospectively apply to amounts received from 1 July 2003, the date of ORER's prescription as an FMA Act agency. See also Figure 2.1.

Source: ANAO analysis of FMA Regulations and Section 31 agreements.

5.17 The Section 31 agreements ultimately executed in respect of eight of the nine agencies identified in Figure 5.2 were expressed so as to apply retrospectively to amounts already collected. This included the agreement executed for BoM, which, as discussed in Chapter 2, had already spent some of the relevant receipts without appropriation authority.

5.18 ANAO notes that, since 1 July 2005, Section 31 agreements have been executed for two newly created agencies. One, for Medicare Australia, was made in advance of the agency commencing operations.[173] The other, for the Australian Communications and Media Authority, was made nearly three months after the agency had commenced operations on 1 July 2005.

Desirability of permitting retrospective application of net appropriation agreements

5.19 While administratively convenient, applying net appropriation agreements to amounts received at some earlier time does not promote discipline by agencies in complying with their financial management requirements and Constitutional obligations.

5.20 The basis on which legal advice provided to agencies has concluded that agreements made under Section 31 of the FMA Act can be expressed so as to apply to amounts previously received has been the broad nature of the language of that Section, and the absence of any provision requiring that such agreements may only operate prospectively. Similarly, the relevant provisions of the annual Appropriation Acts only require that a Section 31 agreement apply to an appropriation item for that item to be taken to be increased (for the amount of relevant receipts received) in accordance with the agreement. There is no reference to the 'time relationship' required.

5.21 The desirability of Section 31 agreements having the capacity to be made or varied so as to have retrospective application for apparently unlimited periods should also be viewed in the light that they are not subject to Parliamentary disallowance.

5.22 On this issue, in October 2005 Finance advised ANAO as follows:

> Finance considers that, while care must be taken in any decision to apply a section 31 agreement to receipts that were received prior to executing the agreement, it is administratively sound to do so when warranted.
>
> Finance considers that there is a range of circumstances where it is entirely appropriate to give retrospective effect to receipts retained by an agency. For example, this may occur where there is an "in principle" agreement between

[173] Medicare Australia (formerly the Health Insurance Commission) became a prescribed agency on 1 October 2005. A Section 31 agreement for Medicare Australia was executed on 27 September 2005, to commence on 1 October 2005.

> the Finance Minister and the relevant Minister that an agency should be permitted to retain certain receipts, while other receipts are still subject to discussion or negotiation. All agencies subject to such consideration are made aware that the items cannot be expended without an appropriation, which is only provided when the agreement is executed…legal advice supports the ability to retain receipts that were received prior to the execution of an agreement…
>
> Finance considers that such a limitation [*on agencies' ability to make Section 31 agreements that retrospectively capture amounts previously received*] would not be desirable, as it may prevent the Finance Minister and relevant Ministers from giving effect to their agreed intentions. For example, changes following revised Administrative Arrangements Orders often take time and there may be a persuasive case for receipts to be retained until an appropriation authority can be effected. Agencies in these circumstances have been advised in Finance Circular 2005/07, not to spend the amounts received, until such time as a section 31 agreement has been put in place.

5.23 As it stands, the Government has considerable authority under the terms of the annual Appropriation Acts to enter into arrangements that provide agencies with appropriation authority to spend amounts received into the CRF. While there may be a range of circumstances where it is appropriate to apply Section 31 agreements retrospectively, as advised by Finance, there may also be merit in providing limits on the extent to which past receipts should be captured by these agreements. More traditional methods of explicitly appropriating funds for government programmes in circumstances that may fall outside any specified limits would always be available. These are properly matters for the Government and the Parliament to decide.

Recommendation No.4

5.24 ANAO *recommends* that, as part of its responsibilities for developing and maintaining the Commonwealth financial framework, the Department of Finance and Administration consider the merits of including greater specificity in the relevant legislative provisions regarding the conditions under which net appropriation agreements may be applied retrospectively to amounts previously received by an agency.

Agency responses

5.25 BoM agreed with qualification, commenting as follows:

> It is suggested that any conditions placed on the retrospectivity of net appropriation agreements must be practicable. The view of the Department of Finance and Administration that there may be persuasive cases for receipts to be retained until an appropriation authority can be effected is very pertinent. Such a situation certainly applied to the Bureau of Meteorology on its prescription.

5.26 All other agencies that responded to this recommendation agreed (see Appendix 2). In agreeing to the recommendation, Finance commented as follows:

> Finance agrees with this recommendation and has developed a policy regarding when agreements should be applied to past receipts of an agency. Finance will also examine, in conjunction with considering simplification options in response to Recommendation No. 5, the merits of including greater specificity in the relevant legislative provisions.
>
> Finance considers that there are a limited number of circumstances where permitting an agency's section 31 agreement to cover receipts received prior to the execution of the agreement is appropriate. Such circumstances include:
>
> 1. where an agreed clause has been inadvertently omitted from a finalised agreement;
> 2. where it is agreed at the commencement of negotiations for a new section 31 agreement that the new agreement shall, when concluded, cover receipts received during the negotiation phase; and
> 3. where a new agency is unable to get a section 31 agreement into place prior to being established and the agreement is expressed to cover amounts received since establishment. Agencies executing agreements that cover past receipts have been advised that their appropriation is not increased (and, consequently, spending is not authorised) until the agreement is executed. Finance has issued guidance to this effect, including Finance Circular 2005/07 (paragraph 19).
>
> Until an agreement is in place covering particular receipts, those receipts should be dealt with in the same manner as other receipts and be swept back to the Official Public Account (OPA). This is set out in the Agency Banking Framework – Guidance Manual (October 2003). Where a section 31 agreement is made covering past receipts (that have been returned to the OPA), the additional appropriation can be accessed in the same manner as other appropriations. The new Appropriation and Cash Management module of the Central Budget Management System will not permit an agency to record a section 31 receipt until a valid section 31 agreement is in place. This process avoids the risk of breaching section 83 of the Constitution and allows for more transparency and accountability in agency funding.

Role of Section 31 agreements

5.27 One of the more significant changes under the FMA Act was the change in the role played by the net appropriation agreement itself. Previously, the annual Appropriation Acts specified the sources from which net appropriations could be received. The agreements made under those arrangements identified, in a Schedule, the types of receipts an agency would be able to collect under the broad sources specified in the Appropriation Acts,

and the quantum of such receipts expected to be collected in the relevant financial year.

5.28 Under the FMA Act, the receipts each agency may add to its annual appropriation are established by the terms of its particular Section 31 agreement.

5.29 In this context, there may be merit in examining the on-going role of individual agency agreements in the management of net appropriations. Areas that could be examined include:

- the nature of the instrument that is used to provide an agency with access to net appropriations; and
- whether instruments relating to individual agencies should be retained as the means of specifying eligible receipts.

Options for executing net appropriation instruments

5.30 The terms of Section 31 are such that the instrument that provides a particular agency with authority to retain and spend amounts received from non-appropriation sources must be in the nature of an agreement. Accordingly, each instrument must be executed by both an agency signatory and a whole-of-government (Finance Minister) signatory.

5.31 As was discussed in earlier chapters, errors and misunderstandings by officials in ensuring that an agreement applying to amounts received in a particular period had been signed by both the Finance Minister (or a delegated Finance official) and the responsible Minister or Chief Executive (or a duly authorised agency official) has had significant consequences for some agencies.

5.32 One option to prevent the recurrence of these issues may be to revise the relevant legislative provisions so that the Finance Minister (or his or her delegate) may, following consultation with the relevant Minister, issue a direction regarding the conditions under which specified receipts may be retained by an agency. This would be similar to the manner in which the Finance Minister (or delegate) currently issues a direction under Section 32 of the FMA Act regarding the transfer of appropriation between agencies upon a change of function.

5.33 While such an approach would not remove the potential for a Finance official to sign such directions without holding the necessary delegation, it would represent a significant simplification in the process. It would also remove the potential for agency officials to misunderstand the extent to which they do or do not have the necessary authority to sign a Section 31 agreement on their Minister's behalf. The effectiveness of perpetual agreements could also be more simply demonstrated over their life, with the authority of only one

signatory, who must be delegated by written instrument, needing to be verifiable.

Role of the annual Appropriation Acts

5.34 There may also be merit in examining options for returning the central role in net appropriations from individual agency agreements to the annual Appropriation Acts. This could be achieved by reintroducing the inclusion in the Appropriation Acts of the types of receipts that will be eligible receipts for all agencies for the purposes of net appropriations. This approach may allow for the removal of individual agency agreements in all or most circumstances.

5.35 The revised template developed by Finance already sets out a number of standard items that are included in the agreements of most agencies. While some agencies have negotiated more tailored agreements, many agencies' agreements do not include any additional or different receipts to those set out in the template. Where considered necessary, it may be possible to provide for individual agreements to be executed on an exception basis, or for additional provisions in the Appropriation Acts to address the particular circumstances.

5.36 This approach would provide certainty and transparency in relation to the majority of net appropriations that will be available to agencies, without the need for separate agency agreements in all cases. It would provide for enhanced Parliamentary scrutiny of the types of receipts agencies are able to retain and spend. Although the registration of Section 31 agreements on FRLI, and associated tabling in the Houses of the Parliament, since 1 January 2005 has improved the transparency of agreements, this does not occur until after the agreement has been made. As noted, Section 31 agreements are not subject to Parliamentary disallowance.

5.37 An approach of this nature would also assist in avoiding inadvertent errors or omissions in the eligible receipts or other terms included in an agency's agreement, which may result in the agreement not providing the authority to spend amounts that the agency had thought to be covered or in some other way being rendered inoperative. The removal of the requirement for separate agreements would also assist in avoiding the potential for a change in appropriation legislation creating a disconnect with agreements already signed, as occurred in respect to the five agencies discussed in Chapter 2, or due to a change in the Administrative Arrangements Order.

Recommendation No.5

5.38 ANAO *recommends* that, as part of its current work examining opportunities to simplify the financial framework, the Department of Finance and Administration examine options to improve the framework for net appropriation arrangements, including the merits of specifying the relevant terms and conditions (including common eligible receipts) in the annual Appropriation Acts, rather than through delegated legislation (Section 31 agreements).

Agency responses

5.39 All agencies that responded to this recommendation agreed (see Appendix 2). In agreeing to the recommendation, agencies commented as follows:

- ABS:

  The ABS further supports the consideration of the merits of the Appropriation Act providing the authority for agencies to operate on a net appropriation and for Section 31 agreements to only be required where restrictions on access to self generated revenues are to be applied.

- BoM:

  The inclusion of common eligible receipts in the annual Appropriation Acts would carry an administrative overhead, but transparency would be enhanced by the identification of broad groupings of section 31 receipts in the budget process.

- DoS:

  There would be improved transparency and accountability if the Appropriation Acts were to provide the conditions for as large a number of section 31 agreements as is possible.

- National Capital Authority (NCA):

  NCA considers that provision of agency specific eligible receipts should remain available under Section 31 agreements, not withstanding any specification of relevant terms and conditions in annual Appropriation Acts.

- Finance:

  Finance agrees with this recommendation and is currently considering the first and second options proposed by ANAO, among others. Finance is currently examining the possibility of executing net appropriation instruments in the form of directions of the Minister for Finance and Administration (or delegate) (executed following consultation with the relevant agency), as part of its current work.

Ian McPhee
Auditor-General

Canberra ACT
31 January 2006

Appendices

Appendix 1: Agency comments on proposed audit report

Department of Finance and Administration (Finance)

Agencies that relied on a presumption of regularity

The report has highlighted a number of shortcomings in record keeping practices, in some instances, going back to the late 1990s. In order to resolve the legal issues surrounding the validity of the agreements, ANAO and Finance jointly commissioned legal advice from AGS.

There are a number of references in the proposed report to the way in which the presumption of regularity operates and the impact of the presumption on the effectiveness of agreements. Essentially, a presumption of regularity applies in cases where evidence is not available to support an express authority from a responsible Minister for an official to enter into a section 31 agreement on his or her behalf. While Finance agrees that the use of the presumption of regularity generally reflects poor record keeping practices, it is considered that the presentation of the operation of the presumption of regularity in the report could be clearer in some instances.

Mr Henry Burmester QC, AGS Chief General Counsel, provided advice to ANAO and Finance jointly, on the operation of the presumption of regularity. Mr Burmester advised of the circumstances in which agreements are "presumptively valid", for the purposes of determining whether a breach of section 83 has occurred. Subsequently, AGS developed a decision tree setting out criteria for assessing section 31 agreements. The decision tree was agreed by Finance and ANAO, and formed the basis for assessing agency agreements in the context of agencies' annual financial statement audits. Agency financial statements, prepared in a manner consistent with the decision tree, provide (in respect of this issue) a true and fair presentation of the agency's financial position, and comply with accounting standards, other mandatory financial reporting requirements and the Finance Minister's Orders made under the *Financial Management and Accountability Act 1997*.

Finance has implemented a range of procedural changes to ensure agencies maintain proper records of express authorisations to enter into agreements on behalf of Ministers. Agreements categorised as "in doubt", which were generally entered into in 1998 and 1999, have since been replaced with demonstrably effective agreements, and the presumption of regularity does not, and could not be expected to, apply in respect of any current section 31 agreement. Finance also agrees with ANAO's recommendation to examine possible changes that limit any need for agencies to rely on a presumption of regularity. For example, the *Financial Management and Accountability Orders 2005* could be amended to include a requirement for agencies to retain these authorities. Non-compliance with this requirement would result in a breach of section 48 of the *Financial Management and Accountability Act 1997*.

ANAO comment

Paragraph two of Finance's comments describe a 'presumption of regularity' as applying '*in cases where evidence is not available to support an express authority from a responsible Minister for an official to enter into a section 31 agreement on his or her behalf.*' ANAO notes that the advice provided by AGS was not that a 'presumption of regularity' would automatically apply in any instance where an agency was not able to verify the existence of an express authorisation from the relevant Minister. As discussed at paragraph 3.51 of the report, and as shown in the decision tree of AGS advices at Figure 3.1, the question as to whether a written or oral express authorisation existed at the time an official signed an agreement is one of fact. AGS have advised that, where an agency is unable to verify the existence of an express authorisation, it may be that an agreement signed by an official other than the Chief Executive is presumptively valid in circumstances where both of the following conditions are satisfied:

- the officer signed the agreement 'for and on behalf of the Minister' or in some other way which indicated that the officer understood himself or herself to be acting under an authorisation from the Minister; and
- there is no evidence to support the view that the officer was not expressly authorised to enter into Section 31 agreements on behalf of the Minister.

As discussed at paragraphs 3.92 to 3.96 of the report, the application of a 'presumption of regularity' in relation to Australian Government agencies substantiating whether officials within the agency concerned complied with legislative requirements in executing a Section 31 agreement, where it is the agency that has relied on the agreement, is not desirable. Relying upon a 'presumption of regularity' in this context inevitably leaves doubt as to the effectiveness of the agreement and, therefore, the amount of the appropriation that was legally available to the relevant agency. This does not reflect sound administrative practice. Finance has agreed to ANAO's recommendation that the Department examine possible administrative and/or legislative changes that could limit the opportunity for agencies to rely upon a 'presumption of regularity' when increasing their appropriations through Section 31 arrangements.

Administrative Appeals Tribunal

The Tribunal is a small non-Canberra based agency. We were unaware of the need to amend our Section 31 agreement as required by the change to the wording of the Financial Management and Accountability Act.

The Tribunal acted in good faith on the understanding that the agreement remained valid.

I note that the funds were not expended by the Tribunal and have been subsequently approved to remain with us. We welcome the attention on this issue to enable the Tribunal to act in a lawful manner with respect to the expenditure of public money.

Australian Bureau of Statistics (ABS)

The ABS has been able to supplement its budget from revenue from third parties for some time (previously known as Section 35 agreements). During the period where the ABS has been identified as not effectively entering into valid Section 31 agreements (1 July 1997 until 6 March 2005) the ABS was operating in good faith. The technical non-compliance concurred with the introduction of the *Financial Management and Accountability Act 1997* and it should be noted the ABS disclosed estimated receipts in budget papers and actual receipts in its financial statements during this period and was of the understanding that effective Section 31 agreements were in existence.

Australian Federal Police

The AFP's Section 31 Agreement was assessed as ineffective based on a legal technicality. The AFP has had an effective Section 31 Agreement in place since 7 December 2004.

Australian Public Service Commission

The Commission supports all the recommendations as it is expected that their implementation will contribute to improved agency compliance with net appropriation legislation and policy framework(s) and the management of net appropriation arrangements.

Australian Radiation Protection and Nuclear Safety Agency (ARPANSA)

This report highlights the fact that understanding of appropriation in general has not been as good as it should be in the APS. The performance audit has helped to improve agency understanding of appropriation management in general and arrangements in relation to net appropriation in particular.

Under section 56 of *ARPANS Act*, ARPANSA does not require a net appropriation agreement to have a legally valid appropriation of its receipts

from the provision of goods and services and costs recovered from regulatory activities. The ineffective s31 agreement which was in place prior to February 2005 did not give rise to any appropriation management or cash management issues for the agency. The fact that amounts disclosed before 2004–2005 as Section 31 receipts were in fact credited directly to the ARPANSA Special Account was included in a note to ARPANSA's 2004–2005 accounts.

ARPANSA agrees with all 5 recommendations suggested in the report.

Biosecurity Australia (BA)

I agree with all five recommendations made in the report.

Page 134 of the report observes the delay in executing an agreement for BA along with a number of other Agencies. I agree that agreements should be executed on a timely basis for new Agencies but the pressures associated with the establishment of small Agencies should also be taken into account. It should also be noted that BA is primarily funded by Government appropriation and at no stage was there any risk of receipts being spent without authorisation.

Department of Agriculture, Fisheries and Forestry

The Department is dependent on revenues brought to accounting under our Net Appropriation Agreement to fund a significant proportion of our activities. We therefore welcome the report's recommendations directed toward providing a greater level of certainty over the management of these funds.

In the proposed audit report ANAO make a number of recommendations in relation to the management of these agreements. We agree with all five recommendations contained in the report.

Department of Education, Science and Training

The Department believes the audit review has been beneficial particularly because the resulting recommendations provide for a more robust financial framework for Government Agencies. The review has also reinforced how critical it is for Department's to have a sound appropriation management system in place.

Department of Employment and Workplace Relations

I have reviewed the proposed report, and agree with the audit recommendations provided. I am pleased to advise that the Department of Employment and Workplace Relations is fully compliant with recommendations 2(a), 2(b) and 3(a). All other recommendations relate to the Department of Finance and Administration.

Department of the Environment and Heritage (DEH)

DEH appreciates the opportunity to comment on the proposed report and the consultation and guidance provided by the ANAO in relation to this matter.

DEH agrees with the recommendations in the draft audit report.

The audit identified a number of issues concerning the administration of net appropriation arrangements by Commonwealth agencies. DEH supports any measures to simplify and strengthen the financial framework for net appropriation agreements.

Department of Health and Ageing

The Department is supportive of the report and its recommendations. The Department notes that it had a valid Section 31 agreement in place as at 30 June 2005.

Department of Human Services

Noting that the Department of Human Services was in compliance with net appropriation legislative requirements I agree with recommendation 2 and 3(a). The remaining recommendations of the report are the responsibility of the Department of Finance and Administration. I support the recommendations referred to the Department of Finance and Administration as they will assist in clarifying the Commonwealth financial framework around net appropriations.

Department of Immigration and Multicultural and Indigenous Affairs

The department agrees with the recommendations and findings included in the report.

Department of Industry, Tourism and Resources (DITR)

The Department agrees with the audit findings. DITR considers that the policy guidance is not clear enough and is seeking Department of Finance and Administration assistance.

Department of Transport and Regional Services

The Department of Transport and Regional Services supports the recommendations of the report and believes that they will strengthen the financial framework for the management of net appropriations.

With regard to authorisations, the Secretary of the Department has been the signatory to departmental and administered net appropriation agreements since 1999 and our current procedures require confirmation of the authority of the Department of Finance and Administration's signatory at the time new agreements are made.

Family Court of Australia

The Court considers that the findings and recommendations of the report are fair and reasonable, as they relate to the Court. The Court has had three Section 31 Agreements in place since 1998. The Court has not been required to make additional disclosures, or restate financial information, in relation to those agreements.

Federal Court of Australia

The Federal Court of Australia supports the five recommendations.

The Federal Court has commenced a review of its financial framework and as part of this review we will be ensuring that appropriate controls are in place to make certain that only appropriately authorised officials will enter into section 31 agreements (Recommendation No.2 a & b) and that appropriate records are maintained (Recommendation No. 3a) of agreements and the authorisations and delegations of the signing official.

The Court appreciates the further clarification provided on net appropriation agreements in Finance Circular No. 2005/07. The Court would also support any further clarification and simplification of net appropriation agreements.

Insolvency and Trustee Service Australia (ITSA)

ITSA makes general comment that this report and the work leading up to it have clarified a number of operational implications of section 31 agreements, which should assist agencies to fulfil relevant statutory responsibilities under the financial management framework. ITSA agrees with all five recommendations in the proposed report.

Inspector-General of Taxation

The Inspector-General of Taxation (IGT) notes the ANAO's view that many of the issues raised by this audit are quite technical. The IGT agrees with this view. The IGT also agrees that there are important issues of legality and accountability.

Overall, the IGT notes and supports the review's findings and recommendations.

However, the IGT considers that the report could have acknowledged more fully the sometimes untidy realities of effecting machinery of government changes, especially the practical challenges of establishing a new agency from scratch. In this context, the IGT agrees with the Department of Finance view that there is a strong place in effective, practical administration for retrospective Section 31 agreements.

National Capital Authority (NCA)

The NCA fully supports the recommendations in the report, in particular those related to the enhancements to the legislative framework and the recommendations to the Department of Finance and Administration to provide additional guidance to agencies.

The NCA looks forward to the final report and the Department of Finance and Administration's positive response to the recommendations.

Office of the Renewable Energy Regulator (ORER)

The nature of the ANAO's recommendations are such that the ORER has no comments to make other than welcoming all attempts to simplify and clarify the relevant requirements of the *Financial Management and Accountability Act (1997)* (FMA Act). As an administrator of an Act myself, I believe it is important to explain to those affected the requirements of legislation, especially those inevitable parts that are less clear and more subject to interpretation.

Appendix 2: Summary of agency responses to ANAO recommendations

Agency	Rec. No. 1	Rec. No. 2	Rec. No. 3	Rec. No. 4	Rec. No. 5
Administrative Appeals Tribunal	Response to proposed audit report did not comment on the recommendations				
Attorney-General's Department	Agree	Agree	Agree	Agree	Agree
AUSTRAC	Agree	Agree	Agree	Agree	Agree
Australian Bureau of Statistics	Agree	Agree	Agree	Agree	Agree
Australian Centre for International Agricultural Research	Agree	Agree	Agree	Agree	Agree
Australian Competition & Consumer Commission	Agree	Agree	Agree	Agree	Agree
Australian Customs Service	Agree	Agree	Agree	Agree	Agree
Australian Federal Police	No comment	Agree	Agree	No comment	No comment
Australian Office of Financial Management *AOFM advised that it accepts the recommendations so far as they apply to it.	Agree*	Agree*	Agree*	Agree*	Agree*
Australian Public Service Commission	Support	Agree 2(a) and 2(b) Support 2(c)	Agree 3(a) Support 3(b)	Support	Support
Australian Radiation Protection and Nuclear Safety Agency	Agree	Agree	Agree	Agree	Agree
Australian Taxation Office	Response to proposed audit report did not comment on the recommendations				
Biosecurity Australia	Agree	Agree	Agree	Agree	Agree
Bureau of Meteorology	No comment	Agree	Agree	Agree with qualification	Agree

Agency	Rec. No. 1	Rec. No. 2	Rec. No. 3	Rec. No. 4	Rec. No. 5
Centrelink	No comment	Agree 2(a) and 2(b) No comment 2(c)	Agree 3(a) No comment 3(b)	No comment	No comment
Commonwealth Ombudsman	No comment	Agree 2(a) and 2(b) No comment 2(c)	Agree 3(a) No comment 3(b)	No comment	No comment
Dept. of Agriculture, Fisheries & Forestry	Agree	Agree	Agree	Agree	Agree
Dept of Defence	No comment	Agree 2(a) and 2(b) No comment 2(c)	Agree 3(a) No comment 3(b)	No comment	No comment
Dept. of Education, Science &Training	No comment	Agree	Agree	No comment	No comment
Dept. of Employment & Workplace Relations	Agree	Agree	Agree	Agree	Agree
Department of the Environment & Heritage	Agree	Agree	Agree	Agree	Agree
Dept of Family & Community Services	No comment	Agree 2(a) and 2(b) No comment 2(c)	Agree 3(a) No comment 3(b)	No comment	No comment
Dept. of Finance & Administration	Agree with qualification	Agree	Agree	Agree	Agree
Dept. of Foreign Affairs & Trade	Agree	Agree	Agree	Agree	Agree
Dept of Health & Ageing	Agree	Agree	Agree	Agree	Agree
Dept. of Human Services	Support	Agree	Agree 3(a) Support 3(b)	Support	Support
Dept. of Immigration & Multicultural & Indigenous Affairs	Agree	Agree	Agree	Agree	Agree

Agency	Rec. No. 1	Rec. No. 2	Rec. No. 3	Rec. No. 4	Rec. No. 5
Dept. of Industry, Tourism & Resources	No comment	Agree	Agree	No comment	No comment
Dept. of the Prime Minister & Cabinet	Agree	Agree	Agree	Agree	Agree
Dept. of the Senate	Agree	Agree	Agree	Agree	Agree
Dept. of Transport & Regional Services	Agree	Agree	Agree	Agree	Agree
Dept. of Veterans' Affairs	Agree	Agree	Agree	Agree	Agree
Family Court of Australia	No comment	Agree 2(a) and 2(b) No comment 2(c)	Agree 3(a) No comment 3(b)	No comment	No comment
Federal Court of Australia	Agree	Agree	Agree	Agree	Agree
Geoscience Australia	Agree	Agree	Agree	Agree	Agree
Human Rights & Equal Opportunity Commission	No comment	Agree 2(a) and 2(b) No comment 2(c)	Agree 3(a) No comment 3(b)	No comment	No comment
Insolvency and Trustee Service Australia	Agree	Agree	Agree	Agree	Agree
Inspector-General of Taxation	Agree	Agree	Agree	Agree	Agree
Migration Review Tribunal	No comment	Agree	Agree	No comment	No comment
National Archives of Australia	No comment	Agree	Agree	No comment	No comment
National Capital Authority	Agree	Agree	Agree	Agree	Agree
National Competition Council	Response to proposed audit report did not comment on the recommendations				
National Water Commission	Agree	Agree	Agree	Agree	Agree

Agency	Rec. No. 1	Rec. No. 2	Rec. No. 3	Rec. No. 4	Rec. No. 5
Office of the Inspector-General of Intelligence & Security	Agree	Agree	Agree	Agree	Agree
Office of the Official Secretary to the Governor-General	Agree	Agree	Agree	Agree	Agree
Office of the Privacy Commissioner	No comment	Agree 2(a) and 2(b) No comment 2(c)	Agree 3(a) No comment 3(b)	No comment	No comment
Office of the Renewable Energy Regulator	Response to proposed audit report did not comment on the recommendations				
Refugee Review Tribunal	No comment	Agree	Agree	No comment	No comment

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