

Public Seminar Series, Graduate
Program in Public Policy, 'Democratic
Governance: Improving the Institutions
of Accountability', The Australian
National University

**Auditing in Contemporary Public
Administration (Covering the
Responsibilities of the Auditor-
General)**

17 May 1999

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I. INTRODUCTION

Noting that the theme of this public seminar series is *Democratic Governance: Improving the Institutions of Accountability*, I thought it might be apt to lead off my presentation with the following quote from Professor Owen Hughes:

'It is accountability which is fundamental to a democratic system'.¹

One of the earlier speakers in this Public Seminar Series, the Hon. Philip Ruddock, MP, conveyed the same sentiment and went on to add that:

'Without appropriate checks and balances even the most well intentioned institutions in a democracy could fail to act in the best interests of the society of which they form a part.'²

It is also not difficult to agree with Dr John Uhr that:

'Effective democratic governance demands that the community have at its disposal access to as many instruments of accountability as are necessary to maintain community confidence in government.'³

In the context of accountability as a fundamental element of our democratic system of government in Australia, I have been asked to talk about the responsibilities of the Auditor-General which bear directly on John's observation. But in talking about the responsibilities of the Auditor-General I need to include the Australian National Audit Office (ANAO).

Section 38 of the *Auditor-General Act 1997* states that 'the Audit Office consists of the Auditor-General and the staff'. An Auditor-General does not do much without the very able support of his or her staff. No doubt the former also brings a lot to the latter such as leadership, insights, professionalism, balance, honesty and maybe, on occasions, some eccentricity. One would hope so, as it can be difficult to remove an Auditor-General from Office (see Section 6 of Schedule 1 of the *Auditor-General Act 1997*) before completion of his or her term (10 years under Section 1 of Schedule 1).

One of the important responsibilities of an Auditor-General is to try to know 'what you do not know'. A good start is to ensure you know as much as possible about the public sector environment and the functions and/or business of public sector agencies and bodies. Both require positive and open relationships with the various stakeholders in an atmosphere of mutual trust and confidence, even if sometimes uncomfortable, to ensure that, firstly, the audit function is effective and, secondly, that performance is improving. The challenge is how best to assess what you do and do not know and develop useful recommendations that make a real difference.

Against this background, I have titled my presentation 'Auditing in Contemporary Public Administration' in recognition of the fact that auditing and the issues that auditors face in the public sector are heavily influenced by the administrative framework and cultural environment that are in place which they need to be familiar with and fully understand in carrying out the responsibilities of the Auditor-General.

This address:

- briefly describes the main features of today's public sector environment and the more responsive ways in which entities - departments, agencies, statutory bodies and Government Business Enterprises (GBEs) - deliver public services;
- outlines the role and mandate of the Auditor-General, including his/her relationship with the Parliament (primarily through the Joint Committee of Public Accounts and Audit - JCPAA) and with the Executive Government;
- describes the outputs of the ANAO and how they contribute to public administration (outcomes);
- discusses some of the major issues that the ANAO addresses in carrying out its work; and
- indicates briefly how the ANAO manages itself in a contemporary public sector environment.

I will not be reviewing the responsibilities of the Auditor-General in an historical context as John Uhr did so well in his book, *'Deliberative Democracy in Australia: The Changing Place of Parliament'*⁴, published last year nor when I traced the development of performance auditing in 1995⁵. But I will be building on comments I made in an article in the Australian Journal of Public Administration in 1996⁶ covering today's same broad topic.

II. CONTEMPORARY PUBLIC ADMINISTRATION

As with many other democracies, Australian governments have been under increasing pressure over the last decade to achieve a better performing public service and less costly, more tailored or better focussed and higher quality services to citizens. The Australian Public Service (APS) has been steadily evolving towards a more private sector orientation, influenced by the momentum of the National Competition Policy reforms⁷ and the Industry Commission inquiry into competitive tendering and contracting⁸. As well, the Government's acceptance of the basic principles set down by the National Commission for Audit for determining what activities should be undertaken within the public sector has led to an increased focus on privatisation and outsourcing of government services and activities.⁹ The Government has made it clear that the challenge of public sector reform, including contestability with the private sector, remains both substantial and urgent.

There is a new emphasis on the contestability of services, the outsourcing of functions which the private sector can undertake more efficiently and on ensuring a greater APS orientation towards outcomes, rather than just on process, and an accent on continuous improvement to achieve better performance in an environment of devolved authority and greater management flexibility.

These developments have given rise to a couple of issues which are increasingly being debated in public sector management circles. First, there is a focus on what constitutes 'core' public sector activities as opposed to 'non-core' ones. That is, what are those functions which can, and should, only be performed and delivered by government. Clearly, the size of the core is shrinking as evidenced by outsourcing and privatising in areas which, hitherto, were considered traditional public sector activities - for example, employment services are now provided through a competitive market. Just how small the core can become is open to debate. But even areas where the public sector has traditionally held a monopoly, such as the provision of policy advice, are becoming increasingly open to competition.

As somewhat of an aside, I should point out that 'core' public sector activity has not always covered a vast array of public services. Last century and early this century, a number of health, education and other welfare services were delivered by the private sector. Governments' relatively recent involvement in these activities was largely in response to the impact on the community of two world wars and a depression. Thus, to some extent, the 'core' is contracting back towards the state that it was in some 100 years ago. I make no philosophical judgement about that situation, except to observe that we now live in a far more complex society that has become increasingly globalised.

Related to the 'core' and 'non-core' dichotomy is the notion that, where the public sector is still delivering government programs and services, there is a growing convergence of the public and private sectors as both sectors either compete and/or operate in partnership in the delivery of public services. I shall talk about this issue in greater detail later in my presentation but I would make the comment here that problems can arise if public sector activity is viewed solely through the eyes of the private sector. Clearly, we have to look at the changing environment and the greater involvement of the private sector, but at the same time, we need to recognise that there are fundamental differences between the two sectors not least of all because of the political dimension to which I would also add 'public service values'.

The provision of public services is not just about the lowest price or concepts of profit or shareholder value. It is about maximising overall 'value for money' for the taxpayer. This requires consideration of issues other than production costs, such as citizen satisfaction, the public interest, openness, fair play, honesty, justice, privacy and equity. How important the latter issues are is largely dependent on the nature and type of product and/or service but even that is changing.

The last decade or so has also seen a steady devolution of responsibility and authority away from central agencies such as the Departments of Finance and Administration, Employment, Workplace Relations and Small Business, and the Public Service and Merit Protection Commission. 'Line', or operational, agencies now have greater autonomy in their decision-making as well as greater flexibility in how they manage their affairs. There has been emphasis on commensurate accountability for resource use and achievement of required outputs and outcomes. But questions continue about differences, particularly between Parliamentary expectations and perceptions about agency management performance.

New financial management legislation enacted in January 1998, replacing the *Audit Act 1901*, illustrates how significantly the management framework has changed. Voluminous and detailed rules and prescription were largely replaced by principles based legislation which clearly places the responsibility for the efficient, effective and ethical management of public sector organisations in the hands of chief executives and directors of boards. Similarly, the Public Service Bill promises to considerably deregulate and decentralise the APS people management framework, as indeed the *Workplace Relations Act 1996* has already done with more likely to come.

Greater responsibility and flexibility in decision-making needs to be matched by at least a commensurate focus on strengthening the associated accountability arrangements to ensure that decisions are appropriately made and that those people making decisions can be properly called to account should the question arise. To provide such assurance, public sector entities need to have robust corporate governance arrangements and financial management and other control structures in place. However, it is during the transition period, as these accountability arrangements and changed organisational structures are bedded down, that the greatest risk to effective decision-making arises. In my view, such risk is accentuated with greater involvement of the private sector in contractual arrangements; loss of corporate memory in agencies with downsizing of the APS; the greater use of computing technology with attendant control and fraud related issues, particularly when outsourced; and lack of required skills in project and contract management in the public sector. I shall address this issue of risk management in more detail later in my presentation.

Another feature of contemporary public administration is the emphasis on the provision of quality client services. In March 1997, the Government announced its decision to introduce Service Charters to promote a more open and customer-focused Commonwealth Public Service. All Commonwealth agencies, authorities and GBEs which have an impact on the public need to develop a Service Charter. These Charters represent a public commitment by each organisation to deliver high quality services to their customers. One hundred and twelve Charters have been developed across the APS to date and it is anticipated that over one hundred and fifty Charters will be in place by 30 June next.

Where relevant, the charters guarantee specific standards for service delivery. They also fairly typically include a review facility. The foregoing arrangements have recently been described by the Ombudsman as follows:

*'The aim of client service charters and internal review is to create a more open and responsible public service and provide the community with an effective and easily accessible problem resolution mechanism.'*¹⁰

Having sketched out important elements of the current and changing public administration landscape, I shall now outline the role of the Auditor-General who, as I have already noted, cannot be considered to be, in any practical sense, separate from the Audit Office.

III. ROLE OF THE AUDITOR-GENERAL

The Auditor-General is the external auditor of the Commonwealth Public Sector. Briefly put, I provide an independent view of the performance and financial management of Commonwealth public sector agencies and bodies. My performance audit reports, numbering about 50 per year, and around 320 audit opinions on financial statements, are an important means of assisting the Parliament to fulfil its accountability role on behalf of the Australian community. In round figures, I am assisted by 280 staff in the ANAO, a statutory body, with an accrual-based budget of about \$50 million of which around a quarter is outsourced to the private sector for the provision of audit and other services. The latter largely relates to what I have defined as ‘non-core’ business which broadly covers organisations, such as Government Business Enterprises (GBEs), that are not directly budget funded.

The Office of the Auditor-General was originally established under the *Audit Act 1901*, the fourth Act of the Australian Parliament. I have borrowed the following quote from John Uhr’s book, quoted earlier, to describe the rationale for the establishment of the Office:

‘The primary purpose of the new office was stated by Treasurer Sir George Turner as ‘to prevent frauds and defalcations.’¹¹

That would be considered a rather narrow focus today with the emphasis on wide-ranging accountability and performance. Nevertheless, many continue to believe that is my primary purpose as illustrated by media comments and a range of personal correspondence on matters that ‘need investigation’. Our role is that of ‘watch-dog’ not a policeman. I can, and do, refer matters for investigation to the Australian Federal Police. For further background on the evolution of the office, including the policies both bureaucratic and political, I suggest you might find it of interest to refer to pages 180 to 190 of John’s book.

As I noted earlier, from 1 January last year, the Audit Act was replaced with three Acts which provide a robust framework for the financial management of the Commonwealth public sector¹². They took almost ten years in the making and will continue to evolve, hopefully without significant change for the foreseeable future, as they are largely principles, rather than process, based legislation.

The Office of the Auditor-General and the Australian National Audit Office are now established by the *Auditor-General Act 1997*. Under the Act, the Auditor-General is an ‘Independent Officer of the Parliament’. That description reflects the concern to emphasise the total independence of the Auditor-General. The Act also includes a number of fundamental elements which are aimed at safeguarding the independence of the Auditor-General and preventing inappropriate influence being exerted on the Auditor-General by either the Executive or the Parliament. They are mainly reflected in the following:

- the Auditor-General cannot be directed by anyone in relation to the performance of his/her functions;

- the Auditor-General is appointed by the Governor-General following approval by the JCPAA;
- he/she is appointed for a period of ten years and can only be dismissed by a resolution of both Houses of the Commonwealth Parliament;
- availability of powers of access to information relating to the performance of an audit function; and
- guaranteed availability of funds appropriated by Parliament for ANAO operations.

The importance of the independence of the Auditor-General is encapsulated in the following comment by the tenth Auditor-General for Australia, Mr Keith Brigden AO:

‘Audit independence and audit effectiveness can amount to much the same thing. If an auditor does not enjoy independence from the bodies subject to audit it will only be a matter of time before some measure of control by auditees becomes apparent. When that happens, the effectiveness of the audit process will inevitably suffer. In practical terms, impairment of the auditor’s independence is synonymous with impairment of audit effectiveness.’¹³

However, while I and my Office enjoy a high degree of functional independence, that certainly does not mean I operate without reference to the Executive and the Parliament. Nor does it mean I have an ‘open cheque book’ for resources.

Our principal client is the Parliament. We maintain a strong relationship with the Parliament, working through the JCPAA as the Audit Committee of the Parliament. That Committee has the responsibility to advise me of the audit priorities of Parliament and to review the resources for the ANAO and recommend to the Parliament an annual budget for the Office. This year that recommendation will be presented to Parliament by the JCPAA Chairman before the budget is brought down.

The significance of the new legislation is illustrated by the following comment made by Chairman of the JCPAA, Mr Bob Charles MP, in relation to the effect the new legislation has had in shifting the distribution of powers between the Commonwealth’s Executive Government and the Parliament:

‘... the Executive has transferred power to the Parliament (to be exercised on Parliament’s behalf by the Joint Committee of Public Accounts and Audit), with respect to the independent audit oversight of Government and the Public Service. This important transfer of power is perhaps the most significant for either the Commonwealth or any State parliament, and their respective executive governments since Federation. The Committee’s independence to examine executive action and the machinery of government is unencumbered.’¹⁴

Importantly, the JCPAA reviews all our audit reports and conducts public inquiries of selected reports quarterly depending on the issues raised in the reports. In this way, the JCPAA provides a vital link in the accountability chain between the Government, Parliament and the citizens of Australia. As well, we have considerable involvement with other Committees which may also review our reports. However, the accountability of the Parliament means that we too are ultimately accountable to the Australian people both for providing a measure of assurance about financial management and reporting as well as about achievement of required APS performance and a shared responsibility for assisting to improve that performance. In these ways we can assist Parliament in its role as the major 'Institution of Accountability'. It is Parliament that has to ensure the government of the day is held accountable. The issues raised by Harry Evans in his earlier presentation in this Series, particularly about 'suppressing parliamentary accountability',¹⁵ have to be resolved in that forum.

The Government is accountable to its citizens for the provision of public services, in at least two interrelated ways. First, it has to ensure that a responsive public sector provides quality services that are appropriate, effective and equitable, at minimum cost to the taxpayer. This is a major driver behind the Government's policy of 'market testing' public services to improve their effectiveness. However, the Government also has to ensure that the accountability, and therefore transparency, of the public sector in the delivery of these services is maintained, and, indeed I would argue, enhanced over time. It is the balance between these responsibilities that is difficult to ascertain and maintain.

My Office's role is to provide assurance to the Parliament and the Australian community on these two aspects, that is, public sector performance and accountability for that performance, as I mentioned earlier. While the public sector reforms demand a greater focus on achieving efficient and effective outcomes for citizens, we also need to recognise that such outcomes also depend importantly on robust and credible administrative and management processes. In short, good processes should ensure good outcomes. They are complements not alternatives.

A particular focus on outcomes does not necessarily mean less of a concern with supportive, robust administrative processes both of a financial and non-financial kind. Moreover, the risks of less than satisfactory outcomes can be significantly increased if sound (systematic) processes are not followed. There is a balance to be struck, as I earlier indicated, taking note of Dr Uhr's observation that:

'Doubts persist in this new form of accountability (results-oriented), and it is not clear where merit does, or should, fit into the emerging framework of accountability'

and that

'... there is still a vital role for accountability institutions to verify that administrative processes are consistent with proclaimed public sector values'.¹⁶

The latter observation has particular significance for the ANAO where the *Financial Management and Accountability (FMA) Act 1997* requires Chief Executive Officers (CEOs) to promote the efficient, effective and ethical (my underlining) use of resources. Not surprisingly, we seek to establish whether agencies have implemented management frameworks that deal proactively with this requirement. As well, our audit systems aim to detect weaknesses and/or breaches of ethical behaviour. However, we also recognise that any code of conduct is just a starting point and that:

*‘Care must be taken in ethics management to ensure that employees do not get the impression that the more mechanical or legalistic adherence to the code will result in satisfactory behaviour’.*¹⁷

Therefore we proceed on the basis that ‘action speaks louder than words’ and acknowledge the implicit challenge raised by Dr Uhr that:

*‘Our capacity to manage public sector ethics lags behind our ability to raise public expectations about higher ethical standards’.*¹⁸

One particular difficulty I have is that legal advice indicates it is doubtful that questions of integrity and propriety are, of themselves, matters of economy and efficiency and, therefore, proper subjects for an efficiency (or performance) audit. However, I have assured the JCPAA that the ANAO would look at ethical considerations as ‘an endemic part of accountability’.¹⁹ We have carried out a number of probity audits which have examined, among other issues, principles of fairness and equity, including ethical conduct.²⁰

IV. THE ANAO - ADDING VALUE

The vision of my office is ‘Recognised Excellence in Public Sector Audit Services’. We aim to add value to public sector performance through achieving the following outcomes:

- *Improvement in Public Administration* - a more efficient Australian Commonwealth public sector implementing better practices in public administration; and
- *Assurance* - independent assurance of Commonwealth public sector financial reporting, administration, control and accountability.

In a continuing environment of change, our key values are independence, objectivity, professionalism, and knowledge and understanding of the public sector environment. We are highly regarded for the role we play in encouraging improved accounting and financial management practices that contribute to the efficient functioning and processes of the public sector. One of our most important values is a client focus. We challenge the traditional ‘gotcha’ mentality usually attributed to auditors. Rather, we see ourselves as well-placed to assist agencies to manage their functions (business) in a WIN-WIN outcome. Our values are also importantly guided by the ANAO Code of Ethics which have been developed within the framework of the

Australian Public Service (APS) values, included in Public Service Regulations as part of the Government's March 1998 administrative reforms, and the APS Code of Conduct together with the Codes of Ethics promulgated by the professional accounting bodies. The United States General Accounting Office captures its values in three words - accountability, integrity and reliability.²¹

We focus on adding 'real' value to public administration, that is, more than just audit providing an assurance of 'compliance', important though that might be. No-one wants fraud and corruption but, equally, no-one wants waste, inefficiency or programs that do not meet their objectives cost effectively. Value for money does not necessarily mean lowest cost or price but it does mean specifying what we mean by 'value'. This we endeavour to do, recognising that this might often involve qualitative assessment.

To achieve our outcomes and meet our other responsibilities to the Parliament, Government, audit clients, public sector agencies and the general public, we produce a range of audit reports and related products and services. Our main products are financial statement and performance audits, complemented by audits of financial control and administration, and assurance control and assessment audits, as well as better practice guides.

The development and delivery of our products and services are based on an integrated strategic approach at two levels. First, at the broader level across the public sector, we need to ensure that our product mix and coverage are tailored to the environment in which we operate and to the accountability needs of our principal client, the Parliament. As the environment changes, so do the associated accountability arrangements. We have to regularly ask ourselves 'have we got the balance right?' We are currently addressing this very question and it involves looking at the balance not only between different products and services, but also within our products. For example, within our performance audit area, there is a question as to how much effort should be applied to administrative effectiveness issues as opposed to efficiency concerns. As well, recognising the increasing risks in the public sector, noted earlier, we are looking at achieving a better balance in our audit products reflecting Parliamentary concerns about compliance, particularly of a legislative or quasi-legislative nature.

The second layer of our integrated service approach occurs at the entity level where we aim to ensure that our audit services assist public sector entities to improve their performance and accountability, as well as to better manage their functions and/or business. In developing a strategy in relation to a particular entity we need to look at the perceived relative strengths and weaknesses of the entity in terms of its performance and accountability, and to take into account any complementary internal or external reviews, investigations and evaluations. We aim to minimise any unnecessary overlap and duplication of such activity and its impact on the entities concerned. The reality is that frequently the same people are involved as are needed to achieve the required entity outputs and outcomes.

I should add that, although our integrated audit service can be thought of as having two dimensions, that is financial statement and performance, they are not exclusive.

The ongoing challenge is to strike the right balance of audit activity across the public service to fulfil our statutory obligations while meeting the particular needs of Parliament and of individual entities. A vital key to achieving the right mix is clearly understanding the Parliament's priorities and we take considerable effort to ensure that we maintain a strong relationship and communication with the Parliament.

A better appreciation of our responsibilities may come from a more basic understanding of our products and services which I will now discuss. Further information on these can be found in our recently released Audit Activity Report²².

Auditing Financial Statements

My financial statement mandate covers audits of government departments, statutory authorities and GBEs. The public sector is currently facing a number of challenges with the recent changes to the financial reporting environment. The new legislation I mentioned earlier, primarily the FMA Act, has resulted in a reduction in centralised control and monitoring, and this is being accompanied by the introduction of accrual budgeting and accounting. The major challenge for the public service is to manage outputs and outcomes on an accrual basis.

Through our financial statement audits, we aim to improve the standard of financial management and administration across the public sector. While the Auditor-General Act (Section 24) requires the Auditor-General to set auditing standards to be complied with for financial statement and performance audits, in practice we adopt the professional standards set by the accounting and auditing profession. Again, the ANAO sees it as our responsibility to contribute to those standards.

We use a number of means, such as client seminars, the publication of a quarterly Financial Reporting Bulletin and acting in an observer role on public sector audit committees, to provide professional advice and assistance in relation to auditing and accounting matters generally. We need to ensure there is no conflict of interest in such activity which could adversely impact on the independence of the audit function. This concern particularly applies to outsourced audits to the private sector accounting firms which may be engaged in consultancy services to the organisations involved. Some audit offices will not agree to such activity as part of their outsourcing contracts. The ANAO requires its contractors to seek approval to engage in consultancies with the agencies concerned. I note that, although the observation related to performance audits, the performance audit of the Victorian Auditor-General's Office conducted by Ernst and Young in late 1998 pointed to a similar conflict:

'... the likely inability of the larger private sector firms to continually meet the independence requirements of the Auditor-General in relation to the agencies for which performance audits are likely to be conducted because of their involvement in consulting and other engagements for the auditee'.²³

The major imperative is to maintain the independence of the audit. The problem is more apparent with financial statement audits because most outsourcing occurs in that area.

Audits of financial control and administration are conducted as major across-agency investigations focussing on a range of operational matters including common support business processes such as purchasing and asset management. Assurance control and assessment audits examine basic administration processes in agencies to provide assurance that agencies are meeting their obligations under financial legislation, for example, receipts and payments of money and payroll arrangements.

The first audited Whole-of-Government financial statement report on an accrual basis was prepared for the year 1996-97²⁴. The report is based on an accrual accounting approach for all Commonwealth agencies and bodies, similar to that used in the private sector, and is accompanied by a commentary on overall financial management by the Government. The latter was enhanced in the report for 1997-98²⁵. Such reporting contributes to improved public sector management by providing credible information upon which more informed decisions can be made about the Government's overall objectives and choices about the allocation of scarce resources to its various priorities and commitments. Primary statements focus on revenue and expenses (to show financial performance); assets and liabilities (to show financial position); and cash flows (to show how activities are financed).²⁶

The move to whole-of-government of reporting has given rise to a number of issues that need to be resolved. For example, the Corporations Law currently requires executive remuneration to be disclosed in companies' financial statements; for Commonwealth statutory bodies and agencies, Orders issued by the Finance Minister under the Financial Management and Accountability Act require an equivalent disclosure. Although there is presently no such reporting requirement, our view is that executive remuneration should also be disclosed at the whole-of-government level, together with the remuneration of Parliamentarians. So far our proposal has not been agreed. However, the issue is currently being considered by the Public Sector Accounting Standards Board in the context of an applicable standard.

The move towards both accrual budgeting and reporting is an important element in assisting departments and agencies to develop useful performance information. It will help agencies to become more outcomes-focussed in reporting; providing improved information to both agency management and the Parliament; and encouraging the formation of an effective corporate governance framework.

The adoption of accrual budgeting also opens the possibility for another interesting comparison at the whole-of-government reporting level, namely the scope to have the statements include a review of budget estimates and actuals for each financial year. Until now, the former were in cash and the latter were accrual-based and accordingly, meaningful comparisons could not be made. In future, however, with budget estimates and actual figures both being accrual based, there is the potential for comparisons to be made to between the two to provide useful indications of the Government's financial management performance at the whole-of-government level.

Performance Audits

Performance audits evaluate the economy, efficiency and effectiveness of the management of public sector entities by examining and assessing resource use; related information systems; outputs and outcomes, including performance targets, indicators, assessments and measures; monitoring systems; and legal compliance. The Auditor-General's performance audit functions do not extend to auditing the performance of Ministers nor to examining or reporting on the appropriateness of government policy. However, our performance audits can, and do, evaluate how effectively and efficiently government policy has been implemented.

Performance audits can take a number of forms: as an audit of a selected function within an agency, such as the management of a contract; or an audit of a selected function across several agencies, such as approaches to dealing with the Year 2000 computing problem; or management of a program within, or across, agencies. There are also broader performance audits which evaluate the performance of a large number of agencies in regard to a specific issue, for example management of assets or the internal audit function, with the results summarised as a general report card on the performance of the agencies concerned.

GBEs are not subject to performance audits as a matter of course. However, I can be requested to conduct a performance audit of these bodies by the responsible portfolio Minister, the Finance Minister or the JCPAA. I may suggest to the responsible Minister, the Finance Minister or the JCPAA that there could be good reasons for requesting me to conduct a particular performance audit of one or more of these bodies. This is a new initiative embodied in the Auditor-General Act but which has not yet been used (Section 17(2)).

As part of our integrated audit service approach which I have just outlined, performance audit topics are selected on two grounds: firstly, to focus on audits expected to have the greatest value-added in terms of improved accountability, economy, efficiency and effectiveness; and, secondly, to ensure appropriate coverage of entity operations within the limitations of available audit resources.

The views of the JCPAA and other parliamentary and public sector entities are sought when audits are being planned, and suggestions from individual members and senators are welcomed. In this latter context, we receive, on occasions, requests from Ministers and Parliamentarians to undertake particular audits. Examples include audits conducted at the request of the Prime Minister on ministerial travel claims and the then Minister for Education, Employment, Training and Youth Affairs relating to a contract with a shipping cruise line. Preliminary inquiries into the National Heritage Trust were made as a result of issues raised by the Leader of the Opposition and other members of Parliament.

More recently, I conducted an audit of the Government's community education and information programme (CEIP) for a new taxation system, including a goods and services tax (GST), after a number of issues had been raised by the Leader of the Opposition in the Senate, as well as by newspaper editorials and by some members of the public. It became clear that these issues had a considerable public interest component and, on that basis, I decided to go ahead with a limited scope performance audit addressing just those issues.

I would suggest that these various requests to conduct audits highlight the point that the Office of the Auditor-General is recognised by the Parliament, the Government and the public alike, as playing a unique accountability role focussed mainly on the independence of the Office and being a fundamental element of our system of democratic government in Australia.

Better Practice Guides

Depending on the subject and nature of information collected during an audit, we might produce a Better Practice Guide (BPG). Such guides aim to assist agencies and other bodies to test their own systems and, where applicable, improve their practices and performance. As well, these guides may be used by the ANAO as a checklist for review of management action, or lack of action, in later audits. In part, this check was instituted to provide assurance to the JCPAA and Parliament of appropriate follow-up action on audits of financial control and administration.

BPGs are very important outputs in the achievement of our outcome of 'Improvement in Public Administration' or, more descriptively, achieving 'a more efficient Australian Commonwealth public sector implementing better practices in public administration'. The Guides seek to belie the misconception that auditors have a mindset of just looking for 'gotchas', as noted earlier. It is generally easy to be critical and, although we may deliver some hard truths at times, it is incumbent on us to make constructive contributions to the improvement of public administration as resources and circumstances allow. On many occasions we are borrowing on the wisdom of others, whether it be in the public or private sectors, in Australia or overseas. Our particular skills are to identify, assess and articulate deficiencies as well as good practice based on our knowledge and understanding of the public sector.

Allied to our BPGs are the range of advisory services we provide to entities. For example, we are currently undertaking a benchmarking study of finance function operations²⁷ in a number of Commonwealth agencies. Research from the private sector indicates that financial operations can be a relatively costly function in organisations with significant scope for performance improvement. Therefore, benchmarking the finance function in APS agencies both offers an opportunity to learn from other Commonwealth agencies and from private sector practices as well as providing a degree of assurance about its relative performance in the home agency.

Participants in the study will receive a customised benchmarking report, which will compare their agency's performance against other Commonwealth agencies and the

private sector. The results of this report will be distributed only to the agency concerned.

We will also produce for Parliament a “global” benchmarking report. This report will include common findings across all benchmarked agencies and the findings will not be attributed to any organisation except where a better practice is identified. The purpose of identifying agencies with better practice is to facilitate sharing of the knowledge within the broader APS community. Such an exercise contributes significantly to both the outcomes we have identified for the ANAO.

BPGs and similar publications are becoming increasingly important source documents for managers operating in an environment of devolved authority and responsibility where the role of central agencies has become increasingly a ‘hands-off’ one. These documents are especially of value to small agencies which have always found it difficult, due to their size and resource endowment, to develop and maintain in-house expertise on the wide range of public sector management issues and have tended to rely heavily on detailed legislative and policy frameworks and guidance from central agencies.

I would hasten to add that we are not trying to supplant the role of central agencies or even to fill a perceived gap as a business strategy. Indeed, on a number of our Guides, we have worked positively with other interested agencies. For example, we worked with the former Department of Finance on a Guide outlining the principles of performance information²⁸; with Comcare on a package of materials designed to assist APS staff, and senior managers in particular, in the management of occupational stress²⁹; and with the former Department of Industry, Science and Tourism and the Management Advisory Board in 1997 to produce a guide and tool kit on Quality in Customer Service³⁰ aimed at the broad public sector as providing assistance in the implementation of a client focus in our operations.

Nevertheless, it should be recognised that in a devolved environment and with the vacation of the traditional monitoring review and oversighting roles by central agencies, gaps have emerged in the information available to managers to assist them to make sound and informed decisions. Given our across-the-service perspective, we are well placed to help fill those gaps as part of our contribution to improving public administration.

As an example of such gaps, the Parliament has, in recent times, expressed particular concerns about the effectiveness of accountability arrangements in the changing reform environment in regard to issues such as purchasing, outsourcing and contract management. Such concerns, which are often about compliance assurance matters, will influence not only the kinds of audits we undertake in the future, but also the direction of the subject matter and content of our better practice guides.

Having indicated who we are, where we fit into the public sector, what we do and how we do it, I thought it might be of interest to canvass some of the specific issues that we are encountering in our audits in the current environment.

V. SOME ISSUES FOR AUDITING IN CONTEMPORARY PUBLIC ADMINISTRATION

Convergence of the Public and Private Sectors

As I mentioned earlier, the introduction of the notion of contestable service delivery has led to the outsourcing of a growing proportion of public sector activity, even in so-called 'traditional' public services such as policy advising and delivery of social welfare. That is, not only is the private sector providing more goods and services to the public sector but it is also delivering an increasing range of public services direct to citizens, often in competition with the private sector. The public sector is shifting from being a provider of services to a purchasing role. Such 'privatisation' of the public sector has also been accompanied by a growing 'commercialisation' of public sector organisations in both their structures and ways in which they operate.

The provision of government services by contractors is one of the most significant issues in contemporary public sector administration. It represents a major challenge for public service managers and Auditors-General to establish an appropriate balance between achieving cost effective outcomes and accountability for the manner in which public sector resources are used. In a recent paper dealing with accountability issues, Professor Richard Mulgan from the Australian National University commented:

*'Contracting out inevitably involves some reduction in accountability through the removal of direct departmental and Ministerial control over the day-to-day actions of contractors and their staff. Indeed, the removal of such control is essential to the rationale for contracting out because the main increases in efficiency come from the greater freedom allowed to contracting providers. Accountability is also likely to be reduced through the reduced availability of citizen redress under such instruments as the Ombudsman and FOI. At the same time, accountability may on occasion be increased through improved departmental and Ministerial control following from greater clarification of objectives and specification of standards. Providers may also become more responsive to public needs through the forces of market competition. Potential losses (and gains) in accountability need to be balanced against potential efficiency gains in each case.'*³¹

The trade-offs referred to by Professor Mulgan that have to be considered are not likely to be simply resolved but are profound and complex, involving consideration of many facets of, inter alia, cost effective service delivery to citizens, administrative and privacy legislation and the various accountability requirements of the Parliament. The issue for resolution is often likely to be about possible trade-offs in those requirements rather than just between efficiency and accountability. Nevertheless, Mr Ruddock, in his opening speech in this Public Seminar Series made reference to the following obligation to the Australian community:

'... to achieve an appropriate and workable balance between accountability, which ensures justice and protection for individuals

*affected by Government decision-making and actions on one hand, and practical, efficient and lawful administration on the other.*³²

Interestingly, in relation to the much discussed Job Network arrangements, a recently released exposure draft of a request for tender is intended to make Intensive Assistance providers more accountable and be required to detail the activities and assistance they will provide for each job seeker they sign up.³³

As the reform of government service delivery continues to evolve, so has the focus of the debate on these accountability issues, with commercial confidentiality and public interest issues (particularly involving ‘sensitive’ information) becoming of increasing concern. The debate has not been limited to Parliamentarians and Parliamentary Committees, Auditors-General, and academics. For example, an editorial in the Australian newspaper last November commenting on the High Court judgement in relation to the tabling of documents before the NSW Legislative Council stated that:

*‘This defence (that papers were commercially sensitive and should not be released) is over-used by governments trying to avoid scrutiny and embarrassment and often represents arrogance of the first order; a democracy elects its representatives to act on behalf of the electorate as a whole, not of vested interests. The system requires the utmost transparency and direct accountability from its Parliamentary representatives. Lack of transparency and limiting the capacity of Parliament to review government decisions weakens our democracy.’*³⁴

The Australasian Council of Auditors-General has put out a statement of Principles for Commercial Confidentiality and the Public Interest. As an example, one of the Principles concludes that:

*‘Some private and public sector bodies are instinctively apprehensive and protective about the disclosure of any commercial information. But such views often overstate the implied risks to an entity that might be occasioned by the release of commercial data. After-the-event commercial information has significantly less value than commercial information concerning events that have yet to occur. But even where commercial information might have commercial value to others, there are often overriding obligations that require it to be released. This is so for commercial information held in the private sector and, a fortiori, it applies to the public sector.’*³⁵

The issues indicated in the above conclusion reflect a number of considerations which have exercised fellow Auditors-General in addressing commercial in confidence material. A particular concern has been the insertion of confidentiality clauses in agreements/contracts which can impact adversely on Parliament’s ‘right to know’ even if they do not limit a legislatively protected capacity of an Auditor-General to report to Parliament.

For example, as another indicator of public concern about this issue, in an ABC Background Briefing recently addressing the “Shrinking Democracy” Tony Harris, Auditor-General of New South Wales, stated that:

*'... it appears to me that governments just don't want to be accountable and are using private sector participation and so are reducing the amount of information that's available.'*³⁶

Tony also raised this issue in the context of his performance audit report reviewing the estimates for the Sydney 2000 Olympic and Paralympic Games. In the preface to the report he stated:

*'In responding to the draft of this report, the government agencies most closely associated with the Games criticised the level of detail of revenue and expense estimates included in this report. That detail was said to involve commercially sensitive information because, if published, it would require government agencies to answer a large number of queries from the public. It is true accountability has costs. It is also true that avoiding accountability has potentially much larger costs.'*³⁷

Ches Baragwanath, Auditor-General of Victoria, has had to consider whether it is in the public interest to disclose the value of a commercial in confidence contract to outsource the State Revenue Office's information technology services. Under the terms of the commercial in confidence contract, the service provider had not consented to such disclosure as this information was regarded as proprietary and its public release could place the contractor at a competitive advantage. After analysing the various arguments he concluded that:

'While I am aware of the importance of promoting practices that enable the benefits of competition to flow from the operation of a fully competitive market, it is my view that the introduction of contestability and the involvement of contractors in the provision of government services should not provide public sector agencies with an avenue for not disclosing the cost of publicly-funded services. The Parliament has the power to make these decisions and where it has seen a need to protect commercial confidentiality, as in the case of the Grand Prix, it has passed legislation to this effect.'

*Accordingly, I have elected to disclose the value of the contract to outsource the Office's information technology services in order to enhance accountability and preserve the public's interest in the right to know how their taxes have been spent. It is my view that the same level of disclosure in annual reports of agencies as applies to consultancies should also apply to outsourcing contracts.'*³⁸

In South Australia, the Auditor-General, Ken McPherson, has produced a substantial report dealing with contract management but which also analyses the issues of claims of commercial confidentiality with respect to government contracts and the role of the Auditor General. The report is almost a seminal contribution to the debate about contracting/outsourcing issues which will have to be carefully considered by parliaments and governments as well as by both public and private sector managers. In the report Ken states that:

‘... the issue of confidentiality is of central importance in matters associated with government contracting.’³⁹

Des Pearson, the Western Australian Auditor-General, is reported as backing calls for contracts to be made available for Parliamentary and public scrutiny after they are signed as happens in Britain, New Zealand and the United States.⁴⁰ On the other hand, the views of some engaged in private sector delivery of government services are reflected, for example, in the comments reportedly attributed to Mark Paterson of the Australian Chamber of Commerce and Industry on the ABC 7.30 Report as follows:

‘I think that the sanctity of contract and the certainty of contract are fundamental pillars of our legal system, and if private businesses enter into contracts with government that specify confidentiality, then that ought to be respected.’⁴¹

Against such comments and the growing concern about use of commercial in confidence claims to prevent or limit any disclosure, it is interesting to note the recent paper by Tom Brennan, of Corrs, Chambers Westgarth. Building his argument on a series of High Court decisions including Lange’s Case, he concludes, inter alia, that:

‘The Commonwealth’s capacity to enter into binding obligations of confidence most likely is limited’.

and

‘Parties dealing with the Federal Government or agencies cannot rely on maintenance of confidentiality of information provided to government instrumentalities except to the extent that it can be demonstrated that it would be contrary to the public interest for that confidentiality to be breached.’⁴²

In a more recent radio interview with Tom Brennan and Alan Rose (President of the Australian Law Reform Commission and previously Secretary of the Federal Attorney-General’s Department) both parties made a distinction between Parliamentary requests for information and formal resolutions seeking its presentation. Reference was made to past stand-offs between the Executive and the Senate on the latter and the issue of the right of Parliaments to require access under the Constitution. Resolution of any differences would be a matter for the High Court.

As a statement of general principle, Alan Rose said:

‘... There are quite obviously important reasons for both Members of the Parliament and the public community at large to know the basis on which certain government decisions were taken and certain government contracts were entered into.’⁴³

At the heart of this debate is the on-going problem of clearly defining the ‘public interest’. The public interest is, of course, fundamental to democratic governance and

is an issue that public officials, including auditors, continually grapple with. Again, the challenge is about striking the right balance between public and private interests. Section 37(1)(a) of the Auditor-General Act precludes publication by the Auditor-General of information whose disclosure would be contrary to the public interest for any of the reasons set out in sub-section (2) which includes unfair prejudicing of commercial interests of any body or person. The former also applies where the Attorney-General has issued a certificate to the Auditor-General along the same lines and is also subject to the same reasons. Not surprisingly, these provisions have been subject to considerable Parliamentary debate.

Contract Management

While the public and private sectors could be said to be re-converging, there remain (necessary) differences which are exemplified in the area of contract management (by which I mean the whole process from the initial release of tenders through to ongoing contract performance monitoring). The nub of these differences is that the taxpayers' dollars are at stake. For instance, the awarding of contracts must of necessity follow a process which has ensured open and effective competition and the realisation of value for money. The reasons for a particular source selection need to be written up and be able to withstand scrutiny, including from the Parliament. Contracts have to be put in place with performance standards clearly specified including appropriate arrangements for monitoring and reviewing contractors' performance.

However, the more rigorous the selection process is, the more protracted the contract negotiation process is likely to be; the more clear and quantifiable the performance standards are, the less likely that there will be an unsatisfactory outcome. In essence, the issue is a trade-off between administrative and accountability processes (or simply 'bureaucratic red tape' in the eyes of some) and their impact on costs and prices. Put another way, the challenge of contract management is to maintain accountability and transparency throughout the process, with the ultimate end of achieving cost efficiencies and value for money outcomes. What also needs to be kept in mind is the cost associated with contract management which partially at least offsets the latter, as many studies of outsourcing have shown.

Crucial to meeting the challenge is the contract itself and how it is subsequently managed. Contracts should not be a daunting process for either party. The ideal contracts are the ones that you can leave in the bottom drawer but at the same time you are confident that, if a challenge were to arise, the Commonwealth's interests are well protected. Such an ideal reflects the establishment of a genuine partnership between the public and private sectors. It is an arrangement whereby the parties operate in tandem rather than at arm's length and where there is room for some give and take. But the boundaries have to be clear enough that each request for a service or product does not result in either or both of the parties scrambling for the contract to settle differences.

For a number of years, our performance audits have addressed contract management issues. And quite frankly, the results have been mixed, as indicated in recent audit reports as follows:

- In relation to the shipping cruise contract audit I mentioned earlier, the former Department of Employment, Education, Training and Youth Affairs (DEETYA) selected a service provider and provided advanced funding of 80 per cent of the contract fee to a contractor without undertaking any financial viability checks on the contractor. The contractor later abandoned the project before it was fully completed because of the withdrawal of its financial backers. As a result the department terminated the contract and has taken legal action in an endeavour to protect any remaining Commonwealth funds held by the contractor.⁴⁴
- Similarly, the audit of the \$5 billion project for six new submarines found that, although only two submarines had been provisionally accepted by the Navy, the department had paid over 95 per cent of the construction contract funds. This was compounded by the finding that the contract only provides modest recourse by the Commonwealth by way of financial guarantees and liquidated damages for late delivery and under-performance.⁴⁵

Equally, we have undertaken a number of audits where agencies have effectively achieved the outputs and outcomes required as a result of sound project and contract management skills. For instance, we found that DEETYA had followed key principles of good project management in implementing the new Employment Services Market arrangements; that each of the project planning criteria had been met; and that risks had been managed in line with good practice. My office identified a range of good practices implemented by the Department and examples are highlighted throughout the report.⁴⁶

We are in the process of conducting an audit of Management of Contracts which is evaluating agency processes in relation to key better practice principles for managing contracts, dealing with:

- provider performance monitoring frameworks;
- management information for tracking expenditure, milestones and outputs; and
- implementation of purchaser, provider and other contract stakeholder feedback mechanisms.

We are also expecting to complete a Financial Control and Administration Audit on Contract Management, limited to common business requirements such as cleaning, and a complementary Better Practice Guide this financial year. Such audit activity is indicative of the significance of the topic now and for the foreseeable future. That significance was highlighted in a recent seminar on Commonwealth Sector legal issues⁴⁷ which discussed, among other things, the convergence of legal and commercial risks and the need for planning and sound systems for contract management, particularly over the whole life of the contract. These are areas where audit experience should assist to minimise risk and maximise performance.

As a result of increased outsourcing, the Commonwealth is, in many cases, no longer directly responsible for program outputs being reliant on a private sector contractor for the provision of particular services or products. Nevertheless, the relevant

agency/body is still accountable for those outputs. This is also Parliament's expectation. The Senate Finance and Public Administration References Committee reinforced this concern in the following terms:

*'The Committee believes strongly that contracting-out of services should not diminish public accountability through the Parliament, the Auditor-General and what can be summarised as the administrative law - the role of statutory officers such as the Commonwealth Ombudsman, the operations of agencies such as the Administrative Appeals Tribunal and legislation such as the Administrative Decision (Judicial Review) Act. It has been suggested that contracting-out may improve accountability by requiring services to be defined more precisely and imposing service agreements on providers. That should be seen as a bonus not an alternative.'*⁴⁸

Transparency of the processes involved is therefore paramount. One of the central concerns, which has received much attention in recent times, is access to contractors' records and, on occasions, to their premises particularly where Commonwealth assets are involved. This issue was also addressed by the above Senate Committee in its 1997 Inquiry into Contracting Out of Government Services.⁴⁹ My submission to that Inquiry noted that:

*'For agencies to be in a position to support the accountability obligations of their Minister and ensure adequate performance monitoring of contracted services, it is essential there be, at least, specified minimum levels of performance information to be supplied by the contractor to the agency, and agreed arrangements which provide for access by the agency to contract-related records and information.'*⁵⁰

I am not suggesting that agencies should have unfettered access to contractors' records, and/or premises, but contractual arrangements must enable agencies to have sufficient information to enable their managerial and accountability responsibilities and obligations to be fully met. This issue is particularly important because the ANAO needs to have access to records and information relating to contractor performance in order to fulfil its statutory duty to the Parliament. That is a shared responsibility with the agencies concerned. In the main, the audit requirements are really no different to those of managers in order to be able to meet their accountability obligations. In that respect regular contract monitoring and review of milestones is essential. As the New South Wales Ombudsman has observed:

*'The consequences of a failure to properly monitor the performance of a contract range from private contractors failing to deliver what they promise, through to corruption.'*⁵¹

The Auditor-General Act provides a range of powers for access by the Auditor-General to records (including contracts) which are relevant to an audit, including records and information held by third parties so long as any access is for the purposes of undertaking an Auditor-General function. Commercial-in-confidence claims do not limit my right of access to relevant records. However, I do not have access to

contractors' premises under that Act. There is provision for me to exclude 'sensitive' material from public reports if I consider that its disclosure is not in the public interest. The latter has to be a primary concern of any Auditor-General.

I have proposed a set of standard clauses for inclusion into contracts with the public sector. These clauses provide for me to access records (including premises) relating to the contract that are in the possession of a private sector contractor. These clauses are not necessary to provide me with access to information as such but they are important in flagging to contractors that they are required to give full access to the Auditor-General for proper accountability. In my view it is a matter of educating both parties that is, in the private and the public sectors, to the relationship or contract. Vague relationships do not assist either party nor lend confidence to the partnership or use of contractual arrangements. This is another aspect of the public sector environment with which the private sector is becoming more familiar as the trend towards outsourcing continues.

Corporate Governance

Improving organisation performance is a primary focus of both the private and public sectors. Management in both those sectors has increasingly recognised that appropriate corporate governance arrangements are a key element in corporate success. They form the basis of a robust, credible and responsive framework necessary to deliver the required accountability and 'bottom line' performance in whatever way that is measured or assessed.

For some time, corporate governance has been a theme, or a specific issue, addressed in a number of our performance audits. In short, corporate governance is about how an organisation is managed, its corporate and other structures, its culture, its policies and the ways in which it deals with its various stakeholders.⁵² While good corporate governance structures have been evident in GBEs, such as Telstra and Australia Post, for some time, a useful Handbook on Corporate Governance and Resource Management has recently been produced by the Department of Communications, Information Technology and the Arts for Members of Councils and Authorities, Directors of Boards and Commissioners in the Portfolio.⁵³

A corporate governance framework, particularly where it involves sound values, cost structures and risk management processes, provides the necessary foundation on which we should be building a cost effective, transparent and accountable public sector. The principles involved are important to any business in whatever manner they have to be implemented to suit the nature and extent of that business.

Effective corporate governance requires leadership from the executive management of agencies and a strong commitment to personal values, quality control and client service. Corporate governance is basically concerned with structures and processes for decision-making and with the controls and behaviour that support effective accountability for performance outcomes. Major elements are strategic planning, risk management, performance monitoring and accountability mechanisms. The framework requires clear identification and articulation of responsibility and a real understanding and appreciation of the various relationships between the

organisation's stakeholders and those who are entrusted to manage resources and deliver required outputs and outcomes.

An integral player in an entity's corporate governance arrangements is its audit committee. With the implementation of the new financial legislation in January 1998, all Commonwealth bodies are now legally required to establish an audit committee. An effective audit committee can improve communication and coordination between management and internal as well as external audit, and strengthen internal control frameworks and structures to assist CEOs and governing bodies meet their statutory and fiduciary duties.

ANAO officers often participate in the meetings of entities' audit committees which provide a useful avenue for building strong client relationships with those entities. An especially important element of our approach is the Audit Strategy Document which is prepared for each Commonwealth entity in the case of financial statement audits, and for each portfolio and some major agencies (eg. Australian Taxation Office) in the case of performance audits. These will be better integrated in the future. These documents are the starting point for the audit cycle each year and provide an overview of the business of the entity subject to audit, a description of the entity risks and an outline of the overall audit approach.

Individual Audit Strategy Documents are presented to audit committees and senior management of public sector entities to foreshadow the areas of audit interest. Copies are also provided to the JCPAA and to relevant Ministers. The strategies provide a basis for discussion of significant audit and other related issues facing the entity. In a number of situations there is a shared interest in such issues with entity management. This creates the opportunity to achieve value added outcomes for both the entity and the ANAO.

My Office has released a publication entitled *'Principles for Core Public Sector Corporate Governance'*⁵⁴ which provides an outline of a corporate governance framework for the 'core' public sector as well as principles for the operation of a public sector Executive Board. The framework is very much people-oriented and reinforces the importance of better communication; a more systematic approach to corporate management; a greater emphasis on corporate values and ethical conduct; a higher profile for audit committees and their strategic and operational relationship with internal and external audit; risk assessment, priorities, monitoring and review; skills development; relationship with the general public as citizens and clients; development of government service charters; quality service delivery; and published performance indicators and/or measures.

I am currently preparing a related discussion paper on the principles and practices of corporate governance applying to Commonwealth Authorities and Companies. This paper focuses on the practical application of the principles of corporate governance covered by the Commonwealth Authorities and Companies Act.⁵⁵ We aim to provide constructive guidance on how to develop a robust corporate governance framework in the complex operating environment of government organisations.

The pressure on the Commonwealth government to provide more services with less has led, in part, to the introduction of private sector approaches to the structuring of government businesses including, for example, the appointment of Boards of Directors. This has also focused attention on good corporate governance but, I hasten to add, not just for commercially oriented government organisations. Accountability structures such as those used in the private sector are increasingly important in all government agencies. Accountability is not the only benefit of corporate governance. An effective corporate governance framework also assists an agency to identify and manage risks in a more systematic and effective manner. The public sector is learning just what the latter involves in a more risky environment as I will now discuss.

Risk Management and Control

Risk management is an important element of corporate governance underlying many of the reforms which have taken place in the public sector. It is not a separate activity within management but an integral part of good management process, particularly as an adjunct to the control environment.

Risk management requires the identification of all risks, determining their priorities and an evaluation of such risks for their potential impacts on the resources required and outputs/outcomes achieved in accordance with the risk assessments made. Further evaluation and reporting of results follows at a later date to ensure that appropriate decisions were made and, where applicable, revised decisions are made and timely action taken, including effective 'damage control'.

As I have mentioned, the overall aim of my office is to improve public administration and the accountability framework. Managing risk efficiently and effectively is a key way that this can be achieved. It is a major challenge for public sector managers, particularly as the culture under which they have operated has traditionally been risk averse. Parliament itself, and its Committees, are still coming to grips with the implications of managing risks instead of minimising them, almost without regard to the costs involved, particularly where better results are achieved.

The concept of risk management is fundamental to our own auditing activities. Professional accounting standards require us to identify and assess the risks which exist in the agency being audited. We base our audit programs on an assessment and prioritisation of the risks of various programs, to ensure that our resources are applied to the areas of greatest risk. For example, my office has adopted risk management techniques in the selection of performance audit topics. We apply an analytical framework to identify the risks that a program or function will be poorly managed. This way we can apply our available resources to auditing those programs which will provide the greatest returns in terms of improved accountability, economy, efficiency and administrative effectiveness.

At the same time, we have in place a number of internal risk management structures which ensure that we are not exposed to unnecessary risks internally. These include, for example, the risk of issuing an incorrect audit opinion. Concerns with the latter have been heightened by the privatisation program discussed next. Another example is the increasing expenditure on legal advice as a means of containing risk exposure in

a more litigious environment. Legal expenses for the ANAO have more than doubled in the last two years.

Risk management is thus important both in the conduct of our work and in the operation of our organisation. We emphasise in our audit reports the importance of effective corporate governance including risk management frameworks in agencies. I consider that the implementation of these two concepts has been markedly instrumental in changing the culture of the public sector including a more outcomes focus. Strengthening the internal framework of agencies allows management attention to be directed at the core business of the agency reflected in its outputs and outcomes.

Complementary to a sound risk management approach is a robust system of administrative control. Late in 1997, the ANAO released a publication entitled *'Control Structures in the Commonwealth Public Sector - Controlling Performance and Outcomes : A Better Practice Guide to Effective Control'*⁵⁶. Control was broadly defined as 'a process effected by the governing body of an agency, senior management and other employees, designed to provide reasonable assurance that risks are managed to ensure the achievement of the agency's objectives.'⁵⁷ The emphasis is on a more systematic approach to decision-making to manage, rather than avoid, risk. A good example is the growing use of computer-oriented rulebase (or expert) systems, particularly to administer 'complex legislative and policy material'.⁵⁸

In the better practice guide, we indicated that a framework for effective control can only be achieved if, within its capacity to do so, an agency is able to:

- control its environment;
- control its risk;
- control its activities;
- control its information and communication; and
- monitor and review its control arrangements.

The purpose of the Guide is to assist public sector managers assess the appropriateness and effectiveness of their organisation's control structures. It also can be used as a tool to encourage the review, design and implementation of a control structure which fits the nature, assessed risks and required performance outcomes of the agency or entity. Not surprisingly, increasing attention is being given to the computing and communications environments where audits over recent years have shown particular weaknesses and risks in areas such as privacy, security and adequate audit trails. Additional pressures are being experienced from Year 2000 compliance, impact of, and exposure to, the Internet and IT outsourcing. A recent report of the Australian Institute of Criminology indicates that the increased usage of information technology will lead to a major rise in white collar crime against governments⁵⁹. These are issues that warrant attention and comment on their own account but are beyond the scope of this address.

The notion of a control environment has to start from the top of an agency. To be effective it requires clear leadership and commitment. This imperative is reinforced by the interrelationship of risk management strategies with the various elements of the control culture. The control environment of the agency will strongly influence the design and operation of control processes and procedures to mitigate risks and achieve the agency's objectives. The clear intent and message to staff should be that such processes and procedures should be designed to facilitate rather than to inhibit performance. This approach should be promoted as good management. In short, the control environment is a reflection of management's attitude and commitment to ensuring well controlled business operations that can demonstrate accountability for performance.

The key to developing an effective control framework lies in achieving an appropriate balance so that the control environment is not unnecessarily restrictive nor encourages risk averse behaviour and indeed can promote sound risk management and the systematic approach that goes with it. Agencies need to concentrate on the potential of an effective control framework to enhance their operations in the context of the more contestable environment that is being created as part of government reform policy.

Privatisation

In the last ten years there has been an increased focus on privatisation of government business entities, with more than \$32 billion raised by the Commonwealth over this time.⁶⁰ Privatisation also provides an opportunity to transfer risks formerly carried by the Commonwealth to the private sector and has been argued to offer the potential for improved business efficiency.

Privatisation, whether by trade sale or public share offer, has always impacted on our financial statement business through our participation in the activities associated with the due diligence program, which ensures the accuracy and completeness of information provided to prospective purchasers by the Commonwealth. Information disclosed to potential purchasers typically includes the most recent audited financial statements, which emphasises the importance of comprehensive and sound financial statement auditing practices.

Privatisation also impacts more broadly on our audit practice because the *Auditor-General Act 1997* and *Commonwealth Authorities and Companies Act 1997* provide that my mandate includes wholly owned Commonwealth companies or companies in which the Commonwealth has a controlling interest. Partial privatisation that does not involve such an interest presents risks to management/Boards and to Government and the budget but, where there is a Commonwealth controlling interest, there is also potential for conflicts of interests and audit risk. The latter is reflected in attendance at annual general meetings where there are normal audit responsibilities to respond to questions as auditor as well as some expectation of the broader responsibilities of an Auditor-General.

We also have undertaken a program of performance audits to examine the extent to which Government sale objectives have been achieved, the effectiveness of the management of the sale and the Commonwealth's ongoing risk exposure. To ensure their effectiveness, our privatisation audits (such as the recent audits of the Telstra share offer⁶¹, the leasehold sales of Federal airports⁶², and third tranche sale of the Commonwealth Bank⁶³) undertaken by a team of experienced officers who understand the financial markets, the commercial nature of the transactions and the overlaying public accountability issues. In addition, we engage appropriately qualified professionals to provide specific technical advice.

The Commonwealth privatisation process itself is now subject to extensive outsourcing under multi-million dollar advisory contracts. This places considerable emphasis on contract management and balancing commercial interests with the overlaying public accountability required of the public service. One of the key outcomes from our privatisation audits has been the identification of opportunities for significant improvement to the process of tendering and managing these advisory contracts, which would improve overall value for money and project management quality in future sales.

The purpose of a contract is to make a legally enforceable agreement. Our audits have clearly illustrated the value of written consultancy contracts that reflect the understanding of all parties to the contract, and which constitute the entire agreement between the parties. Otherwise, the documentary trail supporting the authority for the payment of Commonwealth money and contractual performance requirements, incentives and sanctions may not be clear. It is recognised that contractual performance is maximised by a cooperative, trusting relationship between the parties. But it should never be forgotten that such relationships are founded on a business relationship in which the parties do not necessarily have common objectives.

Making a Difference to the Bottom Line

Under the current public sector reforms, the public sector is subject to increased levels of scrutiny of its performance and effectiveness. A culture of ongoing performance assessment is important in maintaining Parliamentary and public confidence in the public sector.

Despite the greater involvement of the private sector, performance assessment in the APS continues to be more than just about a financial bottom line. It covers a range of measures, both quantitative and qualitative. As well, the agency has to be accountable, for example, for the implementation of the Government's requirements with respect to public sector reforms and for meeting legislative, community service and international obligations; for equity in service delivery; and for high standards of ethical behaviour. This point has been recently emphasised by Max Moore-Wilton, Secretary, Department of the Prime Minister and Cabinet, as follows:

'Ministers and Departments do have an obligation not just to achieve the bottom line that is often the key outcome sought by private companies. We owe it to the community to establish public trust that we work with integrity and put public interest ahead of personal gain. Ensuring the

*transparency of our processes can focus our minds on the need for each individual decision we take to be justifiable in terms of strict propriety.*⁶⁴

In many of its performance audits, my Office provides an assurance to Parliament that agencies are fulfilling their requirements to maintain effective control structures for assurance purposes as well as providing access to key information about their performance. As with most other public sectors, there is still some way to go in establishing credible, reliable and useful performance targets, indicators and assessments. Our focus is primarily on a limited number of high quality indicators that will be used both by managers to manage and by stakeholders to assess how well they have succeeded. All parties must have confidence in the results being achieved.

The accrual-based outputs and outcomes reporting framework will require a cultural change in the APS if it is to focus effectively on the above aspects of an agency's performance in delivering the identified outcomes sought by Government. My office has an important role in assisting agencies to implement that framework effectively, and in assuring Parliament that the required framework is in place and operating effectively. We aim to execute this role with a broad client focus. By working closely with agencies to implement the changes to their reporting, we can make a difference to the way this important initiative is taken up and provide assurance of a better outcome to Parliament.

VI. MANAGING OURSELVES

My Office is funded through budget appropriations and, like any other entity that is budget funded, we are expected to ensure that value for money is achieved for each taxpayer dollar spent. Indeed, under the Financial Management and Accountability Act, I and the heads of other Commonwealth agencies subject to the Act, are required to promote the efficient, effective and ethical use of the Commonwealth resources for which we are responsible (section 44 of the Act).

Our budget and resources are determined in consultation with the JCPAA which has the responsibility to examine the draft budget estimates of the ANAO and to make recommendations to the Parliament and the Prime Minister on those estimates. Through this process, which does not involve the Executive Government, independent judgements are made as to whether the ANAO is adequately funded to meet its statutory obligations. While ultimately it is the Executive's prerogative to decide the level of funds earmarked for the ANAO in the Appropriation Bills that are presented for Parliamentary approval, clearly, any proposed funding which departed in any significant way from that recommended by the JCPAA, would be likely to be questioned by the Parliament.

While the ANAO must remain independent of the bodies it audits, the Office is, nevertheless, a part of the public sector as a statutory body. Consequently, we have a responsibility to contribute to the overall performance and development of the public sector.

For our products to remain credible and relevant, we also need to demonstrate we are meeting the challenges of the changing public sector environment and, within our capacity, are contributing to the implementation of the Government's reform agenda. Over a number of years, we have placed increased emphasis on ensuring that our services are contestable; outsourcing non-core business functions where the private sector can provide better value for money; and ensuring commitment to the processes of benchmarking, quality assurance, peer review and continuous improvement.

The capacity to monitor performance is a prerequisite to being able to improve performance and we have expended a good deal of effort on developing our performance monitoring framework. We measure the quality and impact of our products through a range of quantitative and qualitative measures, including surveys of Parliamentarians and our audit clients. Our audits are regularly subjected to formal quality assurance review processes and we conduct peer review and benchmarking activities with State Audit Offices and relevant private sector organisations. We do not see our independence as meaning we are under no obligation to be accountable for the use of our resources which was a concern expressed by Mr Ruddock, in an earlier address in this Series, about some (independent) members of review tribunals.⁶⁵

We have paid particular attention to our corporate governance arrangements, not just to cope positively with our changing workload, in terms of its nature and scope, but also to pursue a better directed operational effort to meet the strategic requirements of a more integrated public audit approach both across the APS and for individual agencies and bodies.

In January 1998, a private sector review concluded that the ANAO has an appropriate corporate governance framework and systems to give effect to that framework. The review observed that there appeared to be a good level of understanding within the ANAO of the principles and elements of good corporate governance. The review also made several recommendations for further improving our corporate governance arrangements. Action has been taken to do so.

An important element of our corporate governance framework is the external audit function carried out by the Independent Auditor who is appointed under the Auditor-General Act with the approval of the JCPAA. The Independent Auditor is responsible for undertaking the audit of the financial statements of the ANAO, and performance audits of the operations of the Office. In the conduct of performance audits, the Auditor-General Act requires the Independent Auditor to have regard to the audit priorities of the Parliament as determined by the JCPAA.

As I mentioned at the outset, as the Auditor-General, I am not able to achieve very much without the professionalism, skill and commitment of the staff in the ANAO. Accordingly, we pay particular attention to our personal development and leadership

programs to enhance the skills and capabilities of our people and to maintain a productive and supportive working environment. Of course, it is important to recruit the right people in the first place and we devote considerable time to the recruitment and development of our graduates who are expected to be key contributors to the future of the ANAO.

Central to having highly performing people delivering quality audit services is the performance management framework contained in the ANAO Certified Agreement. The Agreement which came into place in June last year, introduced a broadbanded classification structure and innovative and flexible working arrangements, with advancement based on performance (that is, merit). We have introduced a generally accepted performance management system which is not only recognition of dependence on our staff and responsibility for their personal development but also our professional duty of care to our audit clients.

A measure of success in the way we manage our people is the extent to which people want to work for the ANAO. Overwhelming staff acceptance of the Certified Agreement and strong responses to recent recruitment campaigns indicate that we are travelling fairly well in this regard. Nevertheless we are conscious of the increasing demand for accounting and systems skills in the developing accrual-based financial framework and the increased competition for those skills in a more flexible 'remuneration package' employment climate.

Our capacity to deliver quality auditing services is also enhanced through maintaining strong relationships with our public sector peer groups in Australia and overseas and with the various professional accounting and auditing bodies. We have close links with several national and international auditing organisations through which we assist with the development of auditing standards, professional practices and exchanges of experience. The ANAO also works closely with major accounting firms and professional accounting bodies to set and maintain professional and ethical standards internally, the importance of which I underlined earlier. Outsourcing of selected activities and the contracting-in of specialist expertise to assist on particular audits have also provided us with opportunities to extend and develop our knowledge and skill base.

The foregoing indicates that, in managing ourselves, we are continually looking to the future and the medium to long term issues and challenges that face auditing and the ANAO, and consequently developing strategies to successfully meet those issues and challenges. A major strategy is to create and maintain the breadth, and particularly the depth, of public sector knowledge and skills, complemented by outside expertise and information systems, that will be capable of delivering the required outputs and outcomes efficiently, effectively and ethically. In essence, we want to ensure that our comparative advantage as a public sector auditor is demonstrated through our performance and valued by all our stakeholders.

The contemporary trend has been towards the notion of continuous auditing. In the past auditing has been a largely retrospective activity where opinions and advice produced after the event have met fundamental assurance obligations to Parliament but have not necessarily contributed markedly to improving public sector

performance. Rather, auditors have often told managers what they should have done in hindsight. However, as public administration has changed, auditing has had to take a more pro-active approach to ensure audit services are timely and relevant and can also make 'real-time' contributions to enhancing public administration.

In recent times, our approach has been to add value wherever possible by working closely with entities to identify and solve problems now, not later, by making constructive recommendations for change and by promoting and disseminating better management practice. Advances in information technology and the widespread availability of different information sources mean we cannot be complacent about our audit products and services, particularly about how we deliver them to our audit clients, notably the Parliament.

The following extracts from a recent speech by Des Pearson, Auditor-General Western Australia, provide some useful insights into the future of auditing and its role in assisting managers to improve entity performance:

'... I believe we are starting to see the audit deliverable as more than just the opinion on the financial statements, controls and performance indicators of an entity. We are expanding our view of the deliverable to that set of continuous communications that exploit all the knowledge we have gained during the audit.

... Of all the professions, auditors are in the best position to be able to assist managers and executives in interpreting and analysing performance information. Our work is such that it requires a good grasp of the entire range of activities and operations of an entity and ensures we maintain a level of professional scepticism and a critical eye for facts and details. In short our level of knowledge is often on a par with the most senior executives in the organisation, but with the added advantage of objectivity and independence.

*It is important that we exploit this position in a positive way and take a proactive interest in assisting managers to improve the agency's performance. An agency's ability to be seen as a going concern in the future will depend on how well it manages its performance. Why shouldn't the auditor also ensure their own audit business is a 'going concern' by acting now to advise and assist managers on how to use performance information to their best advantage?'*⁶⁶

I consider that my Office is well down the track in terms of the scenario described by Des Pearson. The management challenge for us is to keep moving forward and to continue to look over the horizon in order to maintain our comparative advantage.

VII. CONCLUDING REMARKS

The public sector is operating in an environment of considerable change accentuated by a range of reforms aimed both at the adoption, or adaptation, of private sector approaches and its greater involvement in delivering goods and services to agencies and citizens.

As well, there is an increasing emphasis on finding more innovative and cost effective ways of delivering government programs. The public sector is also becoming increasingly characterised by greater management flexibility and more personal responsibility, underpinned by largely principles-based legislation. At the same time, there is a strong focus on performance at both the entity and individual officer levels.

Equally, the relaxation of central controls, increased devolution of authority, greater involvement of the private sector, growing dependence on communications and information technology, and reduced corporate knowledge, have all led to the creation of an environment characterised by greater uncertainty and greater risk. The risks that today's public servant needs to manage and control have increased not only in their range and complexity, but also in terms of the severity of the consequences should a risk event actually occur.

Contributing to the greater uncertainty and risk are the lines of accountability which have become more blurred and/or complicated. Yet the imperative for appropriate and robust accountability mechanisms has been heightened, especially in the eyes of the Parliament which has expressed concerns on several occasions about the lack of clarity in contemporary accountability arrangements.

Correspondingly, the role of the Auditor-General and the place of auditing in democratic governance has also changed. To provide a somewhat quaint example of the functions of previous Auditors-General, until the late seventies, under the *Audit Act 1901*, the Auditor-General was required to:

*'... transmit to the Treasurer the name of any person failing to comply with any of the provisions of this [Audit] Act or the regulations and thereupon and until such failure shall have been made good to the satisfaction of the Treasurer all salary and moneys that may be or become due or payable to such person may be withheld'*⁶⁷.

The assurance role we perform is no longer simply confined to auditing financial statements nor to, say compliance with legislation, as exemplified by the following tongue in cheek comment by a former Auditor-General:

'Once upon a time there was a government auditor whose only duty was to make sure no-one fiddled the till'.⁶⁸

In today's environment, our role includes providing independent assurance to Parliament on the overall performance and accountability of the public sector in delivering the Government's programs and services and implementing effectively a

wide range of public sector reforms. And I cannot overstate the importance of the independence of the Auditor-General. As the public and private sectors converge; as the management environment becomes inherently riskier; and as concerns for public accountability heighten; it is vital that the Auditor-General has all the professional and functional freedom required to fulfil, fearlessly and independently, the role demanded by Parliament on behalf of the Australian people.

The four national audit agencies making up the Public Audit Forum in the United Kingdom believe that:

'... there are three fundamental principles which underpin public audit:

- *the independence of public sector auditors from the organisations being audited;*
- *the wide scope of public audit that is covering the audit of financial statements, legislatively (or legality), propriety (or probity) and value for money; and*
- *the ability of public auditors to make the results of these audits available to the public, and to democratically elected representatives.'*⁶⁹

One particular challenge in this environment of change is the increasing pressure for accountability to match the more flexible, results oriented culture with the seemingly inevitable trade-offs between requirements for accountability and greater efficiency. This is most apparent in contract management with the private sector, which demands different accountabilities and skills than required in the past. The issue of any trade-off is one for the Government and Parliament to resolve. I would expect our audit reports both to contribute to any resolution of that issue as well as indicating whether contract management meets the terms of that resolution (that is, providing assurance and/or identifying shortfalls in, or lack of, proper accountability). I note that the Hon. Bob McMullan, MP, made a similar analogy in his address to this Series in March when he talked about the relative importance of governability and accountability and the need to strike 'a balance in the resolution of the democracy/efficiency dilemma'.⁷⁰

At the same time, we know that we are well placed to fulfil a broader role (beyond our continually expanding assurance role) based on our across-the-service perspectives and virtual day-to-day involvement with agencies and statutory bodies, including GBEs. Such exposure carries with it a responsibility to share with the public sector the better practices of agencies and bodies that we identify in our work. That is, we have to contribute to achievement of better accountability for performance and required results. The latter 'bottom line' is more than just about cost effectiveness. There is also concern about 'how' government objectives are met which includes questions of values and ethics and the rights (and responsibilities) of citizens.

Whether it is by identifying and disseminating better practices; facilitating the implementation of government reforms; or by helping to change cultures and attitudes, which is often the fundamental action required to make administration

changes effective; we aim to add value and be recognised for the excellence of our audit products and services.

In summary, I would argue that the role of the Auditor-General and the ANAO, are more important to effective, accountable and democratic governance today, than at any time in the past. I would also suggest that, as we move into the future, and as the pace of change remains unabated, this trend will not decline, rather it is likely to increase as the roles and responsibilities of the public and private sectors converge and, perhaps, become more apparent than real. As the British Prime Minister, Tony Blair, has observed in the current environment:

*‘Distinctions between services delivered by the public and private sectors are breaking down in many areas, opening the way to new ideas, partnerships and opportunities for devising and delivering what the public wants’.*⁷¹

and

*‘People want effective government.’*⁷²

That is a challenge to all of us who operate in the public sector and highlights the requirement for ‘public accountability’ where the Auditor-General and the ANAO have particular responsibilities and commitments to our major client, the Parliament. That is my primary focus.

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- ³ Uhr, John 1999. '*Institutions of Integrity - Balancing Values and Verification in Democratic Governance*'. Public Integrity, Winter (page 98).
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The Commission has adopted a framework of principles, cognisant of the broad economic and social goals of government to guide its analysis and recommendations for improvements. This framework includes the following decision sequence:

- Assess whether or not there is a role for government.
- Where there is, decide which level of government, and assess whether or not government objectives are clearly specified and effectively provided.
- Assess whether or not effective activities are being conducted on a 'best practice' basis. (page vii)

In relation to the last mentioned issue, the Committee found that service delivery systems should be market tested against other systems to fully test their efficiency. This involves public sector managers benchmarking their service delivery methods against best practice, re-engineering the way they do their business and contracting-out functions where it is cost effective to do so. (page 83)

The Committee recommended that agencies should be required to market test all activities over the next 3 to 5 years unless there is a good reason not to do so (page 84). This is now government policy.

- ⁹ National Commission of Audit 1996. '*Report to the Commonwealth Government*', AGPS, Canberra, June.
- ¹⁰ Commonwealth Ombudsman 1999. '*Annual Report on activities, 1997-98*'. Canberra, February (page 2).
- ¹¹ Op.cit., Uhr, John 1998. '*Deliberative Democracy in Australia: The Changing Place of Parliament*', (page 182).
- ¹² The three Acts are:
 - (a) The Auditor-General Act which provides for the appointment, independence, status, powers and responsibilities of the Auditor-General; the establishment of the ANAO, and for the audit of the ANAO by the Independent Auditor.
 - (b) Financial Management and Accountability Act (FMA) which sets down the financial regulatory/accountability/accounting framework for Commonwealth bodies that have no separate financial legal existence of their own (ie they are simply agents of the Commonwealth)

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- (c) Commonwealth Authorities and Companies Act (CAC) which provides standardised accountability, ethical and reporting provisions for Commonwealth bodies that have a separate legal existence of their own (eg Commonwealth controlled companies and their subsidiaries and those statutory authorities whose enabling legislation gives them legal power to own money and assets).
- ¹³ *Report of the Auditor-General on the Financial Statements prepared by the Minister for Finance for the year ended 30 June 1984*, AGPS, Canberra.
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- ¹⁶ Op.cit., Uhr, John. 'Institutions of Integrity - Balancing Values and Verification in Democratic Governance', (page 99).
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- ¹⁹ JCPAA 1999. 'Inquiry into Community Education and Information Programme'. Hansard evidence given on 17 March. (pages 7 and 8).
- ²⁰ One example is ANAO Report No.49 1997-98. 'Evaluation Processes for the Selection of Hearing Devices', Canberra, June. (pages xi to xiv).
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- ²² ANAO Report No. 33, 1998-99, 'Audit Activity Report: July to December 1998 - Summary of Outcomes', Canberra.
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- ²⁵ Commonwealth Government of Australia, 1999. 'Consolidated Financial Statements for the year ended 30 June 1998'. Canberra, March (pages 5 to 16).
- ²⁶ Ibid., (pages 22 to 24).
- ²⁷ For now, the Finance function operations benchmarking definition broadly covers all financial transactions processing, financial control mechanisms and financial systems, including forecasting and reporting. The audit activity is not included as it was covered in our Better Practice Guide 'New Directions for Internal Audit' Canberra, July 1998. The Treasury/Financing operation and costing function are also being excluded until agencies generally get more involved and experienced in these areas.
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- ²⁹ ANAO/Comcare, December 1997. 'The Management of Occupational Stress in Commonwealth Agencies: A Better Practice Guide for Senior Managers', Canberra.
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