

The Auditor-General
Audit Report No.42 2003-04
Business Support Process Audit

Financial Delegations for the Expenditure of Public Monies in FMA Agencies

Australian National Audit Office

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of Australia 2004

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Canberra ACT
16 April 2004

Dear Mr President
Dear Mr Speaker

The Australian National Audit Office has undertaken a business support process audit in accordance with the authority contained in the *Auditor-General Act 1997*. Pursuant to Senate Standing Order 166 relating to the presentation of documents when the Senate is not sitting, I present the report of this audit and the accompanying brochure. The report is titled *Financial Delegations for the Expenditure of Public Monies in FMA Agencies*.

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

Yours sincerely

A handwritten signature in black ink, appearing to read 'Pat Barrett'.

Pat Barrett
Auditor-General

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

AUDITING FOR AUSTRALIA

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

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Abbreviations/Glossary

AGS	Australian Government Solicitor
ANAO	Australian National Audit Office
APS Commission	Australian Public Service Commission
BSP Audit	Business Support Process Audit
CE	Chief Executive of an organisation - this audit used the acronym CE to represent Chief Executives, Chief Executive Officers, Directors, Director-Generals, and Departmental Secretaries.
CEIs	Chief Executive's Instructions
Control structure	Control structures are a corner stone of good governance. They should contribute to program outcomes, align with an acceptable level or risk and fit the nature of the agency. Control structures consist of the interrelated components of risk assessment, control environment, control activities, information and communication, and monitoring and review.
CPGs	Commonwealth Procurement Guidelines
Finance	Department of Finance and Administration
FMIS	Financial Management Information System
FMA Act	<i>Financial Management and Accountability Act 1997</i>
FMA Regulations	<i>Financial Management and Accountability Regulations 1997</i>
GST	Goods and Services Tax
Internal audit	An independent, objective assurance and advisory activity designed to add value and improve an entity's operations. It helps an entity accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.
Public money	Public money is money in the custody or control of the Commonwealth.
Sound and better practices	Business practices, which, if adopted, would strengthen the internal control framework and lead to improved effectiveness and efficiency of outputs and outcomes.

Summary and Recommendations

Summary

Background

1. Changes to financial legislation¹ for the public sector adopted at the start of 1998 have seen a shift from central agency control to a framework of devolved authority with enhanced responsibility and accountability being demanded of public sector agencies and statutory bodies.²
2. The *Financial Management and Accountability Act 1997* (FMA Act) makes the Chief Executive (CE) responsible for managing the affairs of the agency in a way that promotes proper use of Commonwealth resources. In order for CEs to uphold their accountability and governance obligations in the devolved environment, an effective control structure must be designed and maintained.
3. The payment of accounts for goods and services is a significant business process that requires an effective control structure to achieve the required outcomes. A key component of an effective control structure in the payment of accounts process is a formalised system for the delegation of authority. The latter must also be complemented by clear guidance, instructions and awareness raising of attendant responsibilities.

The audit

Audit objectives

4. The objectives of the audit were to:
 - assess whether financial delegations associated with the expenditure of public monies were determined, applied and managed in accordance with applicable legislation, Government policy and applicable internal controls; and

¹ From 1 January 1998, the former *Audit Act 1901* was replaced by three Acts which together provide a robust framework for the financial management of the Commonwealth public sector as follows:

(a) the *Auditor-General Act 1997* 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) the *Financial Management and Accountability Act 1997* sets down the financial regulatory, accountability and accounting framework for Commonwealth bodies such as departments that have no separate legal financial existence of their own (i.e. they are simply agents of the Commonwealth); and

(c) the *Commonwealth Authorities and Companies Act 1997* provides standardised accountability, ethical and reporting provisions for Commonwealth bodies that have a separate legal existence of their own (e.g. Commonwealth-controlled companies and their subsidiaries and those statutory authorities whose enabling legislation gives them legal power to own money and assets).

² Presentation by Pat Barrett, AM, Auditor-General for Australia, *What's new in Corporate Governance*, CPA Australia, Annual Congress, Adelaide, 17 November 2000.

- identify better practices and recommend improvements as necessary to current practices.

Audit focus and scope

5. The audit focused on financial delegations for the expenditure of public monies. It assessed relevant aspects of the audited agencies' control structures and sample tested individual expenditure transactions.

6. Audit testing of a statistically selected sample of transactions included examination of financial delegations used for spending proposals, supplier invoices and payments during 2002–2003. Expenditure transactions were reviewed to determine whether financial delegations had been applied in accordance with the relevant policies, procedures, financial delegation schedules, and legislation. Sample testing did not extend to purchasing procedures such as requests for quotations and the evaluation of tenders.

The agencies included in this audit

7. The audit was conducted in five medium sized³ FMA Act agencies, as follows:

- Australian Agency for International Development (AusAID);
- Australian Competition and Consumer Commission (ACCC);
- Commonwealth Superannuation Administration (ComSuper);
- Department of the Treasury (Treasury); and
- Office of the Director of Public Prosecutions (DPP).

Audit conclusion

8. The ANAO concluded that, generally, agencies had developed adequate control structures for the application of financial delegations for the expenditure of public monies. However, the ANAO noted that financial delegations were not always being managed in accordance with relevant legislation. In particular, the requirement to document the approval of a spending proposal was not being adhered to in the majority of instances. As well, the statutory power for entering into contracts, agreements and arrangements was incorrectly referenced in some organisations.

9. In addition, during its testing of a sample of transactions, the ANAO found that the number of approvals being granted by inappropriate delegates was higher than the ANAO expected, given that financial delegations are a routine and well established control. However, it is up to CEs to determine the

³ Medium sized agencies (in terms of staffing levels) have been defined by the Australian Public Service Commission (APS Commission) in the Commission's *State of the Service Report 2002–2003* to include those with 251 to 1000 ongoing staff.

acceptable level of error and to implement controls, guidance and training commensurate with the nature of the business and the acceptable level of risk. Nevertheless such controls should be complemented by adequate guidance and training.

10. The ANAO identified a number of opportunities for marked improvement in the control structures in most agencies, including the need for:

- policy documents to be amended to provide an interpretation of the legislation relevant to the agency;
- the nature and monetary limits of the delegation to be detailed in the instruments of delegation;
- the relevant risks and controls in the fraud risk assessment to be identified and assessed; and
- Financial Management and Information Systems’ controls to be reviewed so that they support the overall control structure.

Sound and better practices

11. The ANAO identified examples of sound and better practices in several agencies, which are listed at Table 1.

Table 1

Examples of sound and better practices

Control environment	<p>Policies and Procedures</p> <ul style="list-style-type: none"> ▪ Policies and procedures were comprehensive and contained easy to understand flowcharts, checklists and quick reference guides. [TREASURY] ▪ The CEIs were reviewed on a quarterly basis by a dedicated team. [TREASURY] ▪ The processes and procedures to be followed when updating, issuing and maintaining the financial delegations schedules were documented. [COMSUPER] <p>Financial delegations schedules</p> <ul style="list-style-type: none"> ▪ The financial delegations schedules had been drafted to identify clearly the delegate, the section of the legislation that permits the delegation, the power or function being delegated, and limitations applying to delegates. [DPP, TREASURY] ▪ Financial delegations were described in terms of the position number/name and not the name of the staff member occupying the position. [ALL] ▪ The financial delegations schedules were maintained in the Human Resources systems, which provided an up-to-date listing of the current incumbent for all delegations at any point in time. [COMSUPER] ▪ Financial delegations schedules were viewed on a quarterly basis by a dedicated team. [TREASURY]
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	<ul style="list-style-type: none"> ▪ When amendments were made to delegations, any updated pages were signed and approved by the CE, and included in the current set of the financial delegations schedules. [TREASURY] ▪ The monetary limit of delegations was represented by symbols against delegates. The symbols were explained by use of legend table. [TREASURY] <p>Fraud risk assessment</p> <ul style="list-style-type: none"> ▪ Risks and mitigating controls relevant to financial delegations, purchasing and payments were comprehensively identified in the Fraud Control Plan. [TREASURY] <p>Awareness</p> <ul style="list-style-type: none"> ▪ Changes to the financial delegations policy, procedures and schedules were communicated to relevant staff through a variety of mediums. [DPP, AUSAID, ACCC, TREASURY] <p>Technology</p> <ul style="list-style-type: none"> ▪ An independent FMIS administrator granted, and documented, user access requests. [TREASURY] ▪ FMIS Administrators, independent of the accounts processing function, were the only staff able to create and update supplier master files. [TREASURY] ▪ A senior finance staff member monitored changes made to supplier master files. [COMSUPER] ▪ Automatic payments were made through ReserveLink using the generation of an encrypted payment run report. [AUSAID, TREASURY]
<p>Monitoring and review</p>	<ul style="list-style-type: none"> ▪ Internal audit reports, as well as minutes of the audit committee meetings, were accessible to all staff through the intranet. [ALL] ▪ The detailed findings flowing from the internal audits were communicated to relevant staff. [ALL]

Recommendations

The summary of recommendations below are based on the findings from the agencies reviewed but are likely to have relevance to other Commonwealth organisations, in particular, other FMA Act agencies.

Control environment

Recommendation

No.1

Para 3.20

The ANAO recommends that agencies' CEIs:

- specify the responsibility and timeframe for review and updates;
- include specific details of the FMA legislative framework that are to be adhered to and how they are to be applied;
- are accurately reflected in other procedural documents; and
- are updated regularly so that only references to current Commonwealth and agency practices are included.

Recommendation

No.2

Para 3.32

The ANAO recommends that agencies' policy and procedural documents, and financial delegations schedules should refer to section 44 of the FMA Act as the source of the authority for CEs, and their delegates, to enter the Commonwealth into contracts, agreements and arrangements, and make payments using an organisational credit card.

Recommendation

No.3

Para 3.35

The ANAO recommends that:

- financial delegations schedules should clearly specify the nature of the delegation and the monetary limits that apply by type of expenditure and delegate; and
- copies of the financial delegations schedules used by staff as part of daily operations are consistent with the CE approved financial delegation schedules.

**Recommendation
No.4
Para 3.42**

The ANAO recommends that agencies' fraud risk assessments comprehensively identify, and assess risks and mitigating controls associated with purchasing and payments functions, and financial delegations.

**Recommendation
No.5
Para 3.52**

The ANAO recommends that agencies:

- provide staff with ongoing training and guidance on financial delegations and fraud awareness; and
- develop mechanisms to effectively disseminate amendments to the CEIs and the financial delegation schedules to staff.

Control activities

**Recommendation
No.6
Para 4.9**

The ANAO recommends that agencies have control mechanisms in place to enable accounts processing staff to confirm that the appropriate delegate has approved the transaction.

**Recommendation
No.7
Para 4.13**

The ANAO recommends that agencies conduct regular reviews aimed at providing assurance that all credit card holders hold an appropriate delegation and a credit card limit consistent with the financial delegations schedules.

**Recommendation
No.8
Para 4.23**

The ANAO recommends that agencies:

- implement detective controls in circumstances where preventative controls such as, a FMIS administrator independent of accounting functions cannot be appointed; and
- regularly monitor the activity of FMIS 'super users' to confirm the appropriateness of their activity.

**Recommendation
No.9**

Para 4.33

The ANAO recommends that agency procedures provide for:

- requests for supplier master file changes and user access to be accompanied by supporting documentation; and
- changes to supplier master file data and user access to be reviewed on a periodic basis so that inappropriate changes can be detected.

**Recommendation
No.10**

Para 4.39

The ANAO recommends that agencies implement controls that:

- prohibit the administrators of electronic payments systems from being able to transfer payment information; and
- provide for data contained in payment run reports to be encrypted.

Monitoring and review

**Recommendation
No.11**

Para 5.12

The ANAO recommends that executive management and audit committees of agencies follow up the implementation of recommendations flowing from internal audits and other review mechanisms in a timely manner, particularly where they relate to areas of significant risk.

Responses to the recommendations and general comments provided by agencies

12. Agencies' responses to the recommendations are provided following each recommendation in the main body of the report. General comments provided by the audited agencies and the Department of Finance and Administration have been included at Appendix 4.

Audit Findings and Conclusions

1. Introduction

Background

1.1 Changes to financial legislation⁴ for the public sector adopted at the start of 1998 have seen a shift from central agency control to a framework of devolved authority with enhanced responsibility and accountability being demanded of public sector agencies and statutory bodies.⁵

1.2 In order for the Chief Executive (CE) or governing body of a public sector organisation to uphold their accountability and governance obligations in the devolved environment, an effective control structure must be designed and maintained.

1.3 The payment of accounts for goods and services is a significant business process that requires an effective control structure to achieve the required outcomes. A key component of an effective control structure in the payment of accounts process is a formalised system for the delegation of authority. The latter must also be complemented by clear guidance, instructions and awareness raising of attendant responsibilities.

1.4 Delegation is a commonly used term to describe a range of methods of conferring authority, powers or functions upon people. Legislation may provide a statutory procedure permitting a person (the delegator) to designate to another person (the delegate) the ability to exercise their power⁶. For example, section 53 of the *Financial Management and Accountability Act 1997* (FMA Act) provides that a Chief Executive may delegate their powers and functions under the FMA Act to an official. Delegates are personally

⁴ From 1 January 1998, the former *Audit Act 1901* was replaced by three Acts which together provide a robust framework for the financial management of the Commonwealth public sector as follows:

(a) the *Auditor-General Act 1997* 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) the *Financial Management and Accountability Act 1997* sets down the financial regulatory, accountability and accounting framework for Commonwealth bodies such as departments that have no separate legal financial existence of their own (i.e. they are simply agents of the Commonwealth); and

(c) the *Commonwealth Authorities and Companies Act 1997* provides standardised accountability, ethical and reporting provisions for Commonwealth bodies that have a separate legal existence of their own (e.g. Commonwealth-controlled companies and their subsidiaries and those statutory authorities whose enabling legislation gives them legal power to own money and assets).

⁵ Presentation by Pat Barrett, AM, Auditor-General for Australia, *What's new in Corporate Governance*, CPA Australia, Annual Congress, Adelaide, 17 November 2000.

⁶ Australian Government Solicitor, *Legal Briefing Number 24*, April 1996.

accountable for their decisions and actions, as they possess the powers and functions that have been delegated to them.

1.5 Effective delegation of authority provides the linkage between the governing body, management and the individual employees who are responsible for the basic operation of control processes and procedures. However, effectiveness is also very dependent on awareness, guidance and clear instructions as necessary, backed up by regular training and review.

FMA Act agencies' legislative framework

1.6 The agencies, covered by this audit report, operate within the legislative framework provided by the FMA Act and *Financial Management and Accountability Regulations 1997* (FMA Regulations). This framework focuses on the fundamental principles underpinning public sector management, and places significant importance on the formalised delegation of authority.

FMA Act

1.7 The FMA Act specifies the responsibilities and powers of the Finance Minister, CEs and officials⁷, including the responsibilities associated with the expenditure of public monies.

1.8 Section 44(1)⁸ of the FMA Act requires CEs to manage the affairs of their agencies in a way that promotes the proper use of Commonwealth resources and provides CEs with the inherent power to approve proposals to spend public money and enter into contracts, agreements and arrangements. Appendix 1 shows a summary, provided by the Department of Finance and Administration (Finance), of the legislative power to enter into contracts on behalf of the Commonwealth.

1.9 Under section 53(1) of the FMA Act, CEs may subsequently delegate their powers and functions, including the power to approve proposals to spend public money and enter into contracts, agreements and arrangements, to agency officials.

FMA Regulations

1.10 The FMA Regulations support the FMA Act by '...prescribing matters necessary or convenient for carrying out or giving effect to the Act'⁹. In particular, regulations may make provision for a number of matters, including

⁷ Official is defined in section 5 of the FMA Act as 'a person who is in an Agency or is part of an Agency'.

⁸ Provided in full at Appendix 2 of this report.

⁹ Department of Finance and Administration website, FMA Regulations.

the handling, spending and accounting for, and the proper use and associated accountability, of public money.

1.11 Specifically, FMA Regulations 9–13, impose constraints on the exercise of the power to approve proposals to spend public money and enter into contracts, agreements and arrangements. These regulations can be summarised as follows.

- FMA Regulation 9 requires that an approver of a proposal to spend public money must be satisfied that the proposed expenditure is in accordance with the policies of the Commonwealth, will make efficient and effective use of the money and, if the proposal is one to spend special public money, is consistent with the terms under which the money is held.
- FMA Regulation 10 requires authorisation from the Finance Minister or his delegate, prior to the approval of a proposal to spend public money, where expenditure under the proposal is not fully supported by an appropriation.
- FMA Regulation 11 provides that an ‘official must not approve a proposal to spend public money unless authorised by a Minister or Chief Executive, or by or under an Act, to approve the proposal’.
- FMA Regulation 12 requires that, where approval of a spending proposal is not given in writing, the approver must record the terms of the approval in a document as soon as practicable after the approval is given.
- FMA Regulation 13 requires that ‘a person must not enter into a contract, agreement or arrangement under which public money is, or may become, payable unless a spending proposal for the proposed contract, agreement or arrangement has been approved under regulation 9 and, if necessary, in accordance with regulation 10’.

1.12 FMA Regulations 9–13 have been included in full at Appendix 2.

Chief Executive Instructions

1.13 Section 52(1) of the FMA Act and FMA Regulation 6 allows CEs to issue instructions to officials in their agencies known as Chief Executive Instructions (CEIs). In relation to financial delegations, FMA Regulation 6(1)(b) discusses the role of CEIs which includes:

... ensuring or promoting:

- (i) the proper use and management of public money, public property and other resources of the Commonwealth; and
- (ii) proper accountability for the use and management of public money, public property and other resources of the Commonwealth.

The Audit

Audit objectives

1.14 The objectives of the audit were to:

- assess whether financial delegations associated with the expenditure of public monies were determined, applied and managed in accordance with applicable legislation, Government policy and applicable internal controls; and
- identify better practices and recommend improvements as necessary to current practices.

Audit scope and focus

1.15 The audit focused on financial delegations for the expenditure of public monies in five FMA Act agencies. It covered relevant aspects of the audited agencies' control structures, and specifically tested individual expenditure transactions.

1.16 Audit testing included examination of financial delegations used for spending proposals, supplier invoices and payments in 2002–2003. Expenditure transactions were reviewed to determine whether financial delegations had been applied in accordance with the relevant policies, procedures, financial delegation schedules, and legislation. Audit testing did not extend to purchasing procedures, such as requests for quotations and the evaluation of tenders.

The agencies included in this audit

1.17 The audit was undertaken in five medium sized¹⁰ FMA Act agencies, as follows:

- Australian Agency for International Development (AusAID);
- Australian Competition and Consumer Commission (ACCC);
- Commonwealth Superannuation Administration (ComSuper);
- Department of the Treasury (Treasury); and
- Office of the Director of Public Prosecutions (DPP).

1.18 Details of the audited agencies' staffing levels and supplier expenditure are shown in Table 2.

Table 2

Audited agencies' financial information 2002–2003

Agency	Average staffing level ¹¹	Suppliers expenditure (\$ million)	Supplier expenditure as a percentage of total operating expenditure
AusAID	511	24.7 ¹²	35
ACCC	469	36.0	49
ComSuper	356	11.5	27
Treasury	732	66.1	45
DPP	435	21.4	34

Source: Agencies' financial statements for the year ended 30 June 2003

Audit Evaluation Criteria

1.19 The audit is one in a series of business support process audits (BSP audits) designed to examine business and financial processes in the Commonwealth. The criteria for these audits have been based on the internal

¹⁰ Medium sized agencies (in terms of staffing levels) have been defined by the Australian Public Service Commission (APS Commission) in the Commission's *State of the Service Report 2002-2003* to include those with 251 to 1000 ongoing staff.

¹¹ Average staffing level for the year ended 30 June 2003 from the agencies' financial statements.

¹² The sample included transactions from the administered expenditure of \$1.7 billion.

control framework detailed in the ANAO's *Better Practice Guide to Effective Control*¹³ which consists of:

- risk assessment¹⁴;
- control environment;
- control activities;
- information and communication¹⁵; and
- monitoring and review.

1.20 The internal control framework can be described as follows:

The control environment is the foundation for the effectiveness of all the other components. It reflects management's commitment and attitude to establishing an effective control structure. It is sometimes referred to as the 'tone at the top' and is dependent on firm leadership and clarity of direction from the governing body.

Risk assessment and control activities include the identification, analysis and assessment of risks to achieving objectives and the design of control policies and procedures to manage those risks, focussing on those that have potential for more significant exposures and are critical to the business.

Regular and relevant information needs to be collected and communicated to enable performance to be monitored and reviewed. The effectiveness of the control structure also requires on-going monitoring and review.¹⁶

Detailed audit criteria

1.21 The above criteria have been adapted to take account of the varied risks, operations and processes in relation to financial delegations for the expenditure of public monies. Development of the criteria also incorporated consideration of sound and better practice in financial delegations.

1.22 The audit criteria for each element of the control structure are shown at the relevant section of the report and are summarised in Table 3 below.

¹³ Australian National Audit Office, *Controlling Performance and Outcomes, Better Practice Guide to Effective Control*, Canberra, 1997.

¹⁴ For reporting purposes, risk assessment has been addressed as part of the Control Environment.

¹⁵ For reporting purposes, information and communication has been addressed as part of the Control Environment and Monitoring and Review.

¹⁶ Australian National Audit Office, *Controlling Performance and Outcomes, Better Practice Guide to Effective Control*, op. cit., p.6.

Audit approach

1.23 The audit methodology involved interviews with selected officers, sample testing, the examination of documentation and records supporting financial delegations, and general observation and inspection.

1.24 The ANAO provided each agency reviewed with a management report on the audit, which included a number of detailed and specific recommendations relevant to the particular agency. However, individual agencies performance is only identified when it exemplifies better practice.

1.25 The audit was undertaken in accordance with ANAO Auditing Standards at an approximate cost of \$280 000.

Audit report structure

1.26 The results of the audit sample testing are set out in Chapter 2. Chapters 3–5 outline the findings against the audit criteria (as detailed in Table 3) and provide recommendations, which in the ANAO’s opinion, would assist agencies, generally, in improving their administrative processes for financial delegations.

Table 3

Detailed Audit Criteria

Control Environment
<p>Policy and Procedures</p> <p>The agency has issued policies on, and procedures for managing, financial delegations. The policies and procedures address the review, use and process of financial delegations. The policies and procedures also address the communication of information relating to the financial delegations system to relevant staff.</p>
<p>Financial Delegations Schedules</p> <p>The agency has a current instrument of delegation. Instruments of delegation are set and reviewed according to relevant policy and procedures. Further, in developing the instruments of delegation, each agency has conducted a risk assessment to identify, assess and manage risks relating to financial delegations.</p>
<p>Awareness of Financial Delegations</p> <p>The key personnel in the agency are aware of their responsibilities for setting, reviewing, using or processing financial delegations. Management effectively communicates the outcomes flowing from the periodic review of the financial delegations policy, procedures and instruments of delegation to relevant staff.</p>

Control Activities

Application of financial delegations

Transactions are authorised in compliance with the instruments of delegation and relevant agency policies and procedures and legislation.

Technology

Information system design and functionality effectively and efficiently supports financial delegation processing and obligations.

Monitoring and review of the financial delegations system

The agency conducts periodic internal monitoring of its financial delegations system to gain assurance that the instruments of delegation and policies and procedures relating to financial delegations are adhered to and properly applied. The agency also communicates the outcomes of periodic internal reviews of the financial delegations system to relevant staff.

The agency regularly reviews financial delegation guidance and/or instructions, and the training provided to staff.

2. Audit Testing Results

Sample methodology

2.1 The audit methodology included testing a statistically based sample of expenditure transactions processed within each agency's Financial Management Information System (FMIS). The sample was tested to determine whether financial delegations had been applied in accordance with: relevant agency policies; procedures; financial delegation schedules; and the relevant legislation.

2.2 In each of the audited agencies, a sample of 150 transactions was drawn from the population of supplier expense transactions¹⁷ for the 2002-2003 financial year¹⁸. As the sample was selected on a statistical basis, conclusions from the results can be used to make valid inferences about the population of transactions.

2.3 In determining the size of the sample, the ANAO expected a low error rate of between zero and 5% because financial delegations are a routine and established control within processes used by all agencies. Additionally, the requirements of the FMA Act and Regulations are clear in providing a framework for the application of financial delegations.

Audit findings

Types of errors

2.4 The errors identified during testing were classified into two categories, as follows.

- **Inappropriate approval of a proposal to spend public money or invoice/claim for payment.** The ANAO assessed whether delegations were applied in accordance with agencies' CEIs and procedures for each expenditure transaction. As part of this testing, the ANAO also verified the delegate's signature.
- **Lack of a documented approved proposal to spend public money.** The ANAO reviewed the supporting documentation for each expenditure transaction to identify if a proposal to spend public money had been approved by an approver prior to entering into a contract, agreement or arrangement to spend public money, in accordance with

¹⁷ Excluded travel expenses.

¹⁸ The Australian Bureau of Statistics (ABS) provided the audit's statistical methodology for the sample selection and the estimation techniques implemented in this testing. The methodology used by the ABS is included at Appendix 3 of this report.

agencies' CEIs and relevant legislation. Purchase orders were a commonly used form of a proposal to spend public money identified.

Approval of a proposal to spend public money or invoice/claim for payment

2.5 The ANAO identified 27 transactions in the agencies audited where delegations were not applied in accordance with the agencies' policies and financial delegations schedules¹⁹.

2.6 Table 4 shows that there were observed error rates, in the agencies, of between 2.07% and 7.47%. The table also shows the extrapolation of the error rate across the entire population of transactions. This means, for example, that in Agency 5, it can be concluded that, based on the sample of transactions tested, there was a 95% chance of the true error rate being between 0.94% and 7.34% in the population of transactions. Put another way, there is a 95% chance that the true number of errors was between 527 and 4117 out of a population of 56 084.

Table 4
High level results of sample testing²⁰

Agency	Actual sample size ²¹	No. of errors	Observed error rate across sample %	Total pop'n	95% Confidence Interval for the true population error rate (%)		95% Confidence Interval for the true population error rate (numbers)	
					Lower bound	Upper bound	Lower bound	Upper bound
1	148	4	2.71	23 321	0.22	5.20	51	1 213
2	146	3	2.07	4 976	0.00	4.35	0	216
3	145	3	2.08	16 395	0.53	3.62	87	593
4	149	11	7.47	24 574	3.28	11.66	806	2 865
5	142	6	4.14	56 084	0.94	7.34	527	4 117
TOTAL	730	27	4.18	125 350	2.42	5.93	3 033	7 433

Source: ANAO fieldwork results

¹⁹ Additionally, there were seven transactions in Agency 3, where the ANAO was unable to verify the delegates' signature with an independent sample signature because the relevant staff had left their positions. The ANAO did not classify these transactions as errors as the audit test could not be completed.

²⁰ There is no relationship between the order of the agencies listed in Table 2 and the order of the identifying numbers in Tables 4 and 5.

²¹ Although the ANAO selected 150 transactions in each agency for testing, not all transactions could be tested. This was mainly because the supporting documents could not be located or the transactions related to accrual journals for which the supporting documents had not been received at the time of the audit. The number of transactions, within the agencies, that could not be tested ranged from 1 to 8. The ABS advised that, given that the extent of non-responses was minimal, it could be assumed that the impact would be small.

2.7 As discussed earlier, the ANAO developed its sampling methodology based on an expected error rate of between zero and 5%. Table 4 shows that one agency had an error rate that was greater than expected by the ANAO. However, it is the responsibility of CEs to determine and specify the acceptable level of error and to implement controls commensurate with the nature of the business and the acceptable level of risk.

Documented approval of a proposal to spend public money

2.8 Consistent with FMA Regulation 12, all five agencies' CEIs required the approval of proposals to spend public money to be recorded either at the time of granting or as soon as practicable after approval. However, as Table 5 demonstrates, the audit results revealed that FMA Regulation 12 had not been complied with in the majority of agencies and transactions tested.

Table 5

Compliance with FMA Regulation 12²²

Agency	Number of transactions tested ²³	Instances of non compliance with FMA Regulation 12	Percentage of total instances of non compliance with FMA Regulation 12
1	148	116	78
2	146	109	75
3	145	76	52
4	149	126	85
5	142	19	13

Source: ANAO fieldwork results

2.9 Because of the relatively high level of non-compliance with FMA Regulation 12, the ANAO sought legal advice from the Australian Government Solicitor (AGS), on the interpretation of FMA Regulation 12. The AGS advised that a spending proposal can be constituted by both formal and informal type arrangements, as well as proposals for single purchases not made under an existing contract, agreement or arrangement. Essentially, any approval to enter into a contract, arrangement or agreement under which public money will, or might, become payable should be recorded in writing in accordance with FMA Regulation 12.

2.10 Table 5 above shows that Agency 5 had results significantly better than the other four agencies. The agency had documented the approval of a

²² There is no relationship between the order of the agencies listed in Table 2 and the order of the identifying numbers in Tables 4 and 5.

²³ Refer Table 4.

spending proposal and/or the decision to enter into a Commonwealth contract, agreement or arrangement, in accordance with its CEIs and FMA Regulations 9, 12 and 13, for the majority of transactions tested. Where approval was documented it was in a variety of forms, including purchase orders, proposals, contracts and emails.

2.11 Given the observed results, the ANAO could not obtain assurance that most agencies had complied with FMA Regulations 9 and 13, that is, based on evidence that spending proposals had been approved.

Conclusion

2.12 Generally, the level of errors was higher than the ANAO had expected when it developed the audit testing methodology. However, CEs should assess the level of error that they are willing to tolerate and establish the appropriate controls to mitigate the risks. In that regard, CEs must direct staff accordingly. Also, CEs should put in place a regime that reviews the controls to confirm that they are effective.

3. Control Environment

Background

3.1 Agencies should establish a control environment that reflects sound management principles by clearly setting out the responsibilities for determining, applying and managing financial delegations.

Risk assessment

3.2 In order for the CE to determine whether to delegate a power or function and to whom a power or function should be delegated, an assessment should be made of the risks associated with the exercise of the power or function by the delegate. Risks will vary depending on the power or function that is being considered for delegation. The risks will include fraud, failure by the delegate to comply with relevant directions issued by the delegator and poor performance of the delegated functions.

3.3 In relation to the payment of accounts functions, the analysis of risks should include those associated with the lack of segregation of duties of incompatible functions and fraud risks, such as manipulation of the supplier master file in the FMIS for personal gain, submission of fictitious invoices, acquisition of goods or services for unauthorised use, and diversion of valid payments to unauthorised recipients.

3.4 The decision as to whether to delegate should be based on an assessment of whether the control structure mitigates the risk. Following the assessment of risks, the CE may decide to avoid the risk associated with the delegation of a power or function by choosing not to delegate it.

Control structures

3.5 Agencies' control structures should have a basic level of preventative control over the expenditure of public monies by the proper application of the FMA legislative framework as described earlier.

3.6 Preventative controls in the long run are less expensive and less disruptive to daily operations as they attempt to deter or prevent undesirable events, such as the unauthorised purchase of goods and services, from occurring. The preventative controls prescribed in the FMA legislative framework, such as requiring approval of spending proposals prior to entering into contracts, agreements and arrangements, have an additional benefit of allowing agencies to record their financial commitments as they arise.

3.7 Conversely, detective controls provide evidence that an error or irregularity has occurred and, therefore, requires correction. While

preventative controls are preferred, detective controls are also important to provide evidence that the preventative controls are functioning as intended. Detective controls over the payment of public monies would confirm whether delegated functions are being appropriately performed, and comply with the FMA legislative framework and relevant directions issued by the delegator.

3.8 Agencies should develop and subsequently review strategies and controls to minimise the risks associated with the delegation of a power or function. The Australian Public Service Commission (APS Commission) advised that controls to minimise risks may include ensuring that:

- delegations are within the scope permitted by the legislative framework;
- instruments of delegation are drafted in accordance with an established agency-wide standard;
- both the delegator and delegate are familiar with their responsibilities;
- delegates possess the necessary skills and attributes to exercise the delegated powers and functions;
- effective performance management and accountability mechanisms are in place;
- appropriate internal audit, review and monitoring is undertaken;
- delegates receive relevant training; and
- all delegations are regularly reviewed for appropriateness and accuracy²⁴.

3.9 Financial delegations should be reflected in comprehensive and up-to-date policies such as CEIs, administrative procedures and instruments of delegation. Staff should receive ongoing training to promote awareness of their responsibilities. There should also be readily available guidance and/or instructions, which should be regularly reviewed. It would also be expected that financial delegations have been appropriately identified and documented as a mitigating control for risks identified in agency's risk assessment.

Audit findings and comments

3.10 The control environment was audited against three elements, as follows:

- policy and procedures;
- instruments of delegation; and
- awareness of financial delegations.

²⁴ Australian Public Service Commission, *Delegations*, June 2002, p.5.

Policies and procedures

3.11 The following table summarises the criteria that was used to assess an agency's policy and procedural framework.

Table 6

Audit criteria

Audit evaluation criteria

The agency has issued policies on, and procedures for managing, financial delegations.

The policies and procedures address the review, use and process of financial delegations. The policies and procedures also address the communication of information relating to the financial delegations system to relevant staff.

Policy

3.12 Agency's policies are promulgated through Chief Executive Instructions (CEIs). CEIs play an important role in the control framework for the payment of accounts process. The purpose of the CEIs is to interpret the requirements of the FMA legislative framework into policies that apply to the agency involved. As a matter of better practice, CEIs should provide comprehensive guidance and/or instructions to staff for the exercise of their delegations, and be reviewed periodically to determine whether they reflect current financial practices and the agency's operating environment. CEIs also assist agencies minimise the loss of corporate memory and knowledge caused by staff movements.

3.13 All the audited agencies had documented CEIs that specifically addressed financial delegations. The CEIs were maintained on the agencies' intranet site. However, three agencies could not provide evidence that the copy of the CEIs on the intranet were the latest version approved by the CE.

3.14 The ANAO considered that Treasury's CEIs, and the agency's management of them, was better practice because they:

- provided comprehensive guidelines for using and processing financial delegations;
- contained flowcharts and process checklists, including those for granting approvals for expenditure proposals; and
- were reviewed on a quarterly basis.

3.15 The ANAO also identified the following weaknesses in the agencies' CEIs.

- In two agencies, the CEIs contained information that was irrelevant to the agency. Sections of the CEIs had been replicated from the

*Department of Finance and Administration's CEIs Model Set 1997*²⁵ (*Finance CEIs Model Set*) without consideration of the agencies' specific requirements.

- Three agencies' CEIs had not been updated to reflect changes in financial practices.
- Most of the audited agencies' CEIs referred delegates to the FMA legislative framework for guidance when exercising their authority rather than providing an interpretation of the legislative framework as it applied to the agency.
- In three agencies, the CEIs provided guidance on using and processing financial delegations but did not address the responsibility or timing for the review of financial delegations.

Procedures

3.16 Agency procedures are expected to include detailed instructions on how transactions should be processed, including where and how control mechanisms such as delegations are to be applied. Only three of the agencies had procedures that were linked to the CEIs.

3.17 ComSuper's procedures had included the requirements of how to maintain its financial delegations schedules, including allocating responsibility for the maintenance of the schedules.

3.18 Treasury's procedures contained easy to understand flowcharts outlining the processes to follow. For instance, the agency's *Purchasing Handbook* contained a flowchart of the payment process, which indicated the responsibilities of its operational finance branches. The agency's quick reference guides for purchasing and credit cards contained a summarised version of the same information as the relevant CEI and the handbook, as well as a detailed flowchart of the payment process, and broader descriptions of what to do during each stage of the payment process.

3.19 The ANAO, at the time of the audit, however, identified a number of areas where agencies' procedures could be improved:

- one of the agencies did not have any procedures detailing the payment process and regular functions of accounts processing staff;
- two agencies' procedures referred to outdated information;

²⁵ Finance issued the *Chief Executive Instructions Model Set* in 1997 as part of the change in the legislative framework. The model set is no longer actively promulgated by Finance but the ANAO used them as a basis for comparison as part of the audit.

- in one agency, the procedures did not contain any information relevant to the agency as they had been directly copied from a section of the *Finance CEIs Model Set*; and
- two agencies' procedures were inconsistent with, and contained a number of differences to, the financial delegation schedules.

Recommendation No.1

3.20 The ANAO recommends that agencies' CEIs:

- specify the responsibility and timeframe for review and updates;
- include specific details of the FMA legislative framework that are to be adhered to and how they are to be applied;
- are accurately reflected in other procedural documents; and
- are updated regularly so that only references to current Commonwealth and agency practices are included.

Agencies' responses

3.21 All of the agencies agreed with the recommendation. Specific comments provided by Treasury and ComSuper were as follows.

- Treasury is fully compliant with this recommendation.
- ComSuper is currently conducting a review of its CEIs. ComSuper's CEIs have been updated to reflect the FMA legislative framework and financial changes (eg GST). The review will be completed by April 2004.

Instruments of delegation

3.22 The following table summarises the criteria that were used to assess the development and structure of an agency's instruments of delegation.

Table 7

Audit criteria

Audit evaluation criteria

The agency has a current instrument of delegation.

Instruments of delegation are set and reviewed according to relevant policy and procedures. Further, in developing the instruments of delegation, each agency has conducted a risk assessment to identify, assess and manage risks relating to financial delegations.

Instruments of delegation

3.23 As a matter of better practice, the CEIs should contain a section on delegations and authorisations. This section should specify how delegations

are set and reviewed, as well as identifying the instrument by which a delegation is granted. Agencies in this audit referred to these instruments as financial delegations schedules.

3.24 The APS Commission recommends that:

a delegation instrument should be carefully drafted to ensure that it clearly identifies:

- the delegate;
- the section of the legislation that permits the delegation; and
- the power or function being delegated²⁶.

3.25 The APS Commission also provides advice on a number of options by which a CE can specify delegates.

The options are to:

- name the relevant employee or employees to whom the powers or functions are delegated; or
- specify that the power or function is delegated to the person or persons nominated from time to time to occupy a specified position created under section 77 of the *Public Service Act 1999* (PS Act); or
- specify that the power or function is delegated to the person or persons performing from time to time the duties specified in the instrument²⁷.

3.26 Where either of the two latter options is adopted, the delegation is described in terms of the office, or position, and not the person occupying the position. This allows the delegation to continue to operate where there is a change in the person occupying a position or performing the specified duties as it automatically transfers to any person formally given the functional responsibility for the position.

3.27 DPP and Treasury's financial delegations schedules had been drafted to clearly identify: the delegate; the section of the legislation that permits the delegation; the power or function being delegated; and limitations applying to delegates.

3.28 In all agencies, financial delegations were described in terms of the position number/name and not the name of the staff member occupying the position. This practice provides administrative flexibility as new delegations are not needed when the staff member who occupies the position is replaced.

²⁶ Australian Public Service Commission, op. cit., p.4.

²⁷ *ibid.*

3.29 All agencies' financial delegations schedules had provided delegates the authority to:

- approve proposals to spend public monies;
- enter into Commonwealth contracts/liabilities;
- approve Official Hospitality; and
- make a payment using an organisational credit card.

Source of statutory authority to enter into a contract, agreement or arrangement

3.30 Only three agencies correctly identified that section 44 of the FMA Act was the source of authority to enter into Commonwealth contracts/liabilities and make a payment using an organisational credit card. Of the other two agencies, one did not specify the authority being delegated or refer to the relevant part of the FMA legislative framework in their financial delegations schedules.

3.31 The other agency had recognised FMA Regulation 13 as the source of authority for delegates to make a payment using an organisational credit card rather than section 44 of the FMA Act being the source of the authority to do this.

Recommendation No.2

3.32 The ANAO recommends that agencies' policy and procedural documents, and financial delegations schedules should refer to section 44 of the FMA Act as the source of the authority for CEs, and their delegates, to enter the Commonwealth into contracts, agreements and arrangements, and make payments using an organisational credit card.

Agencies' responses

3.33 All of the agencies agreed with the recommendation. Specific comments provided by Treasury and ComSuper were as follows.

- Treasury is fully compliant with this recommendation.
- ComSuper considered that an understanding of the source of the authority and reference to section 44 of the FMA Act should be incorporated in the policy and procedural documents and financial delegations schedules.

Other issues

3.34 The ANAO found other areas where agencies' financial delegations schedules could be improved as follows.

- One agency could not provide evidence that the financial delegations schedules being used were the latest schedules to be approved by the CE²⁸. In another agency, authorisation forms signed by the CE for each of the delegates listed in the financial delegations schedules could not be located for twenty of the thirty-four delegates.
- In one agency, nine of the fourteen delegates had been authorised by the delegator (CE) for a monetary limit that was different to that in the current financial delegations schedules.
- All agencies had provided a number of ‘unlimited’ delegations for certain staff for all or certain types of expenditure. The ANAO considers that the financial delegations schedule should specify that the delegated amount is ‘limited by the budget’ or other similar words considered appropriate by the agency. The provision of an unlimited delegation in one agency, led to the misinterpretation of the powers or functions delegated by the CE. The staff member in question, mistakenly assumed that the unlimited nature of the delegation included the power to sub-delegate.
- All agencies’ CEIs required official hospitality expenditures to be approved by designated ‘official hospitality approvers’ as opposed to ‘approvers’. In two agencies, the financial delegations schedules did not identify ‘official hospitality approvers’, while two other agencies’ financial delegations schedules did not limit the authority of ‘approvers’ by stating that official hospitality expenditure required a separate delegation.

Recommendation No.3

3.35 The ANAO recommends that:

- financial delegations schedules should clearly specify the nature of the delegation and the monetary limits that apply by type of expenditure and delegate; and
- copies of the financial delegations schedules used by staff as part of daily operations are consistent with the CE approved financial delegation schedules.

Agencies’ responses

3.36 All of the agencies agreed with the recommendation. Specific comments provided by ComSuper were as follows.

²⁸ This is similar to the issue raised earlier in regards to CEIs.

- ComSuper's financial delegations clearly specify the nature of the delegations and type of expenditure. Copies of the updated financial delegations schedule are provided to the accounts payable staff and posted on the intranet each fortnight.

Sound and better practices

3.37 Treasury displayed a number of sound practices with its management of the financial delegations schedules, as follows.

- a dedicated team reviewed delegations on a quarterly basis.
- when amendments were made to delegations, any updated pages were approved by the CE and included in the current set of the financial delegations schedules.
- the monetary limit of delegations was represented by symbols against delegates. The symbols were explained by use of legend table.

Fraud Risk Assessment

3.38 Risks relevant to delegations and the associated payment of accounts process, and the mitigating controls in place within an agency, should be identified in fraud risk assessments.

3.39 In one of the audited agencies, Treasury, the ANAO considered that the risks relevant to financial delegations, purchasing and payments functions were comprehensively identified. In turn, the controls addressed the risks and were comprehensively documented.

3.40 Conversely, in two agencies, risks relevant to the delegations, purchasing and payments, had not been comprehensively identified in the fraud risk assessment. Further, in the ANAO's opinion, the controls identified, did not fully address the risks and were not comprehensively documented.

3.41 One of these agency's fraud risk assessment also did not take into account the risk exposures identified in an internal audit.

Recommendation No.4

3.42 The ANAO recommends that agencies' fraud risk assessments comprehensively identify, and assess risks and mitigating controls associated with purchasing and payments functions, and financial delegations.

Agencies' responses

3.43 All of the agencies agreed with the recommendation. Specific comments provided by Treasury and ComSuper were as follows.

- Treasury is fully compliant with this recommendation.

- ComSuper’s fraud risk assessment already identifies risks and mitigating controls associated with purchases and payments. The fraud risk assessment will be updated to include financial delegations.

Awareness of Financial Delegations

3.44 The following table summarises the criteria that were used to assess the level of training including awareness raising, guidance and/or instructions provided on financial delegations.

Table 8

Audit criteria

Audit evaluation criteria

The key personnel in the agency are aware of their responsibilities for setting, reviewing, using or processing financial delegations.

Management effectively communicates the outcomes flowing from the periodic review of the financial delegations policy and procedures and instruments of delegation to relevant staff.

3.45 Training and ongoing guidance on financial delegations and fraud awareness is an effective and practical step that assists agencies in mitigating risks associated with the delegation of authority. This is particularly important where new staff are appointed or in organisations where there is a high staff turnover.

Financial delegations and fraud awareness training

Raising awareness of financial delegations related information

3.46 Four agencies communicated changes flowing from the periodic reviews of the financial delegations’ policy, procedures and schedules to relevant staff through the intranet as well as an ‘all staff’ email detailing the areas of change.

3.47 One agency’s only mechanism for informing staff, including accounts processing staff, that CEIs and financial delegations schedules were updated, was to post the revised information on the intranet.

3.48 Across the five agencies audited, training in financial delegations and the associated requirements was generally limited to on-the-job training for new and ongoing Finance branch staff.

3.49 While the on-the-job training appeared to be adequate in four of the agencies, the ANAO noted that one agency’s internal audit had reported that in certain operational areas, knowledge of the application of CEIs and Commonwealth Procurement Guidelines (CPGs) was inadequate. Where weaknesses are identified, agencies should provide specific training to staff on these matters.

Fraud awareness training

3.50 Formal fraud awareness training had been conducted in two agencies. In two agencies, the lack of fraud awareness by staff was highlighted as a risk in their Fraud Control Plans. These plans had recommended that the agencies should carry out fraud awareness training.

3.51 Where agencies assess that a lack of fraud awareness is a risk to the agency, the ANAO considers that fraud awareness training should be provided to all staff and delegates.

Recommendation No.5

3.52 The ANAO recommends that agencies:

- provide staff with ongoing training and guidance on financial delegations and fraud awareness; and
- develop mechanisms to effectively disseminate amendments to the CEIs and the financial delegation schedules to staff.

Agencies' responses

3.53 All of the agencies agreed with the recommendation. Specific comments provided by Treasury and ComSuper were as follows.

- Treasury is fully compliant with this recommendation.
- ComSuper will undertake a comprehensive communication and training programme as part of the CEI review. Ongoing training and updates of amendments to the CEIs will be provided twice-yearly.

Conclusion

3.54 The ANAO concluded that agencies' CEIs and procedural documents could be improved by providing interpretations of the legislative framework as they applied to the agency, and by being kept up-to-date and consistent with instruments of delegation. Instruments of delegation could be improved by specifying the nature of extent of the delegation along with identifying the appropriate source of statutory power to enter into a contract, agreement or arrangement.

4. Control Activities

Background

4.1 Control activities are an important element of a control structure. In relation to financial delegations, control activities are the specific practices, processes and methodologies that help an agency to:

- reduce risks while identifying opportunities for improvement;
- prevent and/or detect and address irregularities; and
- maintain complete and accurate financial records and relevant data.

Audit findings and comments

Application of financial delegations

4.2 The criterion that was used to assess an agency's application of financial delegations is shown in the following table.

Table 9

Audit criterion

Audit evaluation criterion

Transactions are authorised in compliance with the instruments of delegation and relevant agency policies and procedures.

4.3 As reported in Chapter 2, the ANAO tested a number of transactions within the audited agencies, and identified errors in two categories – an inappropriate expenditure approval and a lack of a documented approved expenditure proposal. The ANAO also identified a number of other issues in the application of financial delegations within agencies, as discussed below.

Verifying authorised delegate

4.4 Accounts processing functions should include verification that the appropriate delegate had given approval for the expenditure of public monies. These functions should be carried out in sufficient detail to satisfy management and external scrutiny.

4.5 In two agencies, it was difficult to ascertain whether the appropriate delegate had approved the transaction, as the name and position number/name of the delegate was not documented.

4.6 In one of these two agencies, the ANAO noted that in 21 per cent of transactions tested, the position names of staff were either not stated on the accounts processing forms, or when they were stated, did not agree with the

position names of delegates listed in the financial delegations schedules. Also, the agency did not maintain a list of the names of the staff occupying the delegated positions and/or their signatures to enable accounts processing staff to confirm that the appropriate delegate had approved the transaction.

4.7 This may not be considered a significant risk in agencies with a small number of delegates. However, in agencies where there are a large number of delegates there is a risk that accounts processing staff will not identify transactions that have been inappropriately authorised. For example, in this agency, there were 129 different delegates for the transactions tested, which the ANAO considered too large a number for the accounts processing staff to be sure that an appropriate delegate had approved the payment.

4.8 ComSuper managed this risk by maintaining its financial delegations schedules within the Human Resources (HR) Information System. As financial delegations were assigned to position numbers, the HR system provided an up-to-date listing of the current incumbents for all delegations.

Recommendation No.6

4.9 The ANAO recommends that agencies have control mechanisms in place to enable accounts processing staff to confirm that the appropriate delegate has approved the transaction.

Agencies' responses

4.10 All of the agencies agreed with the recommendation. Specific comments provided by Treasury and ComSuper were as follows.

- Treasury has implemented an electronic delegations spreadsheet as an additional control mechanism. The electronic delegations spreadsheet identifies the delegate's name, title, work unit and dollar limits and is located on the Department's shared drive for easy access and quick reference by accounts processing staff. In addition, Treasury has updated the relevant forms requiring approvers' signatures to ensure that delegates utilise titles that are consistent with the financial delegation schedules.
- ComSuper is introducing a work-flow strategy to provide efficiencies in the accounts payable process for the organisation. The implementation of an electronic data management system will ensure that the name and position number of the delegate is provided when authorising the payment.

Application of credit card delegations

4.11 The ANAO also reviewed delegations relating to credit cards by verifying that all credit card holders held an appropriate delegation and a credit card limit consistent with the financial delegations schedules.

4.12 The ANAO identified some instances where agencies' practices were not in accordance with their CEIs and procedures.

- In one agency, one staff member had *two* credit cards with a combined limit of \$25 000 although the financial delegations schedules only provided the staff member with a delegation to hold *one* credit card with a \$20 000 limit.
- One agency's credit card procedures required transaction limits for credit cards to be equal to or less than the credit card holder's delegation limit. However, in one instance, this agency's Chief Finance Officer had increased a credit card holder's transaction limit to a higher level than that delegated by the CE.
- In accordance with legislative requirements (discussed in Chapter 3), all the agencies' CEIs required credit card holders to have a delegation to enter into a Commonwealth contract, agreement or arrangement and have credit card limits that mirrored their delegation limits. However, in one agency, only one of the total forty-six credit cardholders, had a delegation to enter into a Commonwealth contract, agreement or arrangement.

Recommendation No.7

4.13 The ANAO recommends that agencies conduct regular reviews aimed at providing assurance that all credit card holders hold an appropriate delegation and a credit card limit consistent with the financial delegations schedules.

Agencies' responses

4.14 All of the agencies agreed with the recommendation. Specific comments provided by Treasury and ComSuper were as follows.

- Treasury reviews the delegation and limits of all credit card holders as part of the Department's quarterly review of financial delegation schedules.
- ComSuper is conducting regular reviews of credit card holders to ensure that credit limits are consistent with the financial delegations schedule.

Technology

4.15 The criterion that was used to assess an agency's information system design and functionality is shown in the following table.

Table 10

Audit criterion

Audit evaluation criterion

Information system design and functionality effectively and efficiently supports financial delegation processing and obligations.

4.16 Agencies' FMISs provide application software required to support various business processes of the organisation. The software should be designed to reflect and support the control environment implemented by management.

4.17 The ANAO reviewed the design of the agencies' FMISs, in particular;

- the role of administrators;
- 'super users'²⁹;
- review of supplier master file changes;
- access to the FMIS; and
- encryption of payment run reports;

to determine whether the above audit criterion had been achieved.

FMIS administrators

4.18 A FMIS administrator is responsible for managing the configuration, operation, security and integrity of the FMIS, and the information stored within it. The administrator level of access provides powerful system administration functions along with wide ranging system access rights. Better practice requires that systems 'administration staff should not be authorised to enter transaction data or update master files'.³⁰

4.19 In three agencies, the FMIS administrators were not independent of the accounts processing function, as they were involved in processing payments. Further, the ANAO noted that activities performed by the FMIS administrators were not reviewed in two of these agencies.

²⁹ User profile that generally permits complete access to application data, activity logs and operating privileges, and allows all forms of operation (including read, write, delete and modify rights).

³⁰ Australian National Audit Office, *Security and control for SAP R/3 Better Practice Guide*, 1998, p.147.

4.20 The ANAO recognised that these agencies had limited staff resources to create a FMIS administrator position separate to accounts processing functions. However, the risk of having a FMIS administrator who is also able to enter transaction data needs to be mitigated. The ANAO considered that agencies must determine whether preventative or detective controls are preferable. For example, a preventative control could include a senior member of staff, who is unable to enter data, being appointed the system administrator. Detective controls could include ongoing monitoring and review of user activity, including that of the administrator and master data changes.

Super users

4.21 Agency FMISs have the ability to create user profiles known as ‘super users’. ‘Super users’ generally have powerful system access rights that permit complete access to application data, activity logs and operating privileges, and which allow all forms of operation (including read, write, delete and modify rights). Access to ‘super users’ should be adequately restricted to minimise the risk of: unauthorised transactions being processed; and the integrity of system data being compromised. However, even if access is restricted, the activities of those staff members with these access rights need to be monitored to confirm the appropriateness of actions taken.

4.22 The ANAO found that none of the agencies reviewed the activity of their ‘super users’. The ANAO considers that the activity of ‘super users’ should be monitored by a staff member, independent of the accounts processing function, with the skills and seniority to determine the appropriateness of the actions taken.

Recommendation No.8

4.23 The ANAO recommends that agencies:

- implement detective controls in circumstances where preventative controls such as, a FMIS administrator independent of accounting functions cannot be appointed; and
- regularly monitor the activity of FMIS ‘super users’ to confirm the appropriateness of their activity.

Agencies’ responses

4.24 All of the agencies agreed with the recommendation. Specific comments provided by ComSuper were as follows.

- ComSuper reported that detective controls are in place. Due to the operational requirements of the area, a separate Systems Administrator position for processing functions cannot be managed. An audit tracking report from the organisation’s FMIS is now provided each

month highlighting any functions in the accounts payable processing where the same person has completed both tasks. This report is reviewed and signed off by the Manager of the area.

Supplier master files

4.25 Finance managers need to be confident that the controls over supplier master files, which provide payment details including suppliers' bank account details, are adequate to prevent inadvertent or intentional errors in payments.³¹ Ideally, managers should segregate supplier master file setup from processing payments. However, if this is not possible, other control mechanisms such as review of master file changes must be implemented to ensure that errors in payment transactions are detected. The ANAO *SAP Better Practice Guide* supports this by stating 'an independent review should be performed of audit trails for changes to vendor master records'³².

4.26 The ANAO identified that three agencies had controls over supplier master files, including restricted access to the supplier master file maintenance functions in the FMIS and the requirement that requests for supplier master file changes be accompanied by supporting documentation. In one of these agencies, the FMIS administrators were the only staff with access to create and update supplier master files, and were not involved with accounts processing. In another agency, a senior member of the Finance branch periodically monitored supplier master file changes made by the FMIS administrator.

4.27 In the third agency, the FMIS administrator and another manager were the only staff members with access to create and update supplier master files. However, the manager was able to process payments. Moreover, the ANAO was advised that, in practice, the manager was not involved with processing functions.

4.28 In relation to whether agencies had standard periodic processes in place to review changes to supplier master file data, the ANAO noted three agencies did not have these processes in place. Further, two of these agencies did not have independent FMIS administrators.

Access to the FMIS

4.29 The ANAO *SAP Better Practice Guide* provides guidance on user access, which is applicable to all FMISs. It recommends that security administration procedures be documented and address the: authorisation and approval of user access; addition, change and deletion of user access privileges; and the

³¹ ANAO Audit Report No.22, *Payment of Accounts and Goods and Services Tax Administration by Small Commonwealth Organisations*, 2002–2003.

³² Australian National Audit Office, op. cit., p.22.

removal of user access. It also recommends that periodic reviews be performed of the access rights assigned to each user, so that an adequate level of segregation of duties can be maintained.

4.30 Three agencies did not have a formal process for granting FMIS user access requests. The general practice in two of these agencies was for the relevant managers to send an email to the FMIS administrator requesting access for their staff. Whilst the FMIS administrator had recorded the email electronically, it was not maintained as an official record³³ of the agency. Another agency had recently implemented a new FMIS and, at the time of the audit, had not formalised procedures and forms for granting access to the FMIS.

4.31 The remaining two audited agencies had formalised processes for granting access to the FMIS. In one of the agencies, Treasury, the process for granting user access demonstrated sound practice as it was performed by an independent FMIS administrator and documented to record:

- all users and their access requirements;
- the reasons for the level of access granted to users; and
- the original request by the relevant manager for user access.

4.32 The ANAO also identified instances that highlighted weaknesses in the controls over user access:

- one agency had a FMIS Administrator with two user IDs;
- two agencies had user IDs (a FMIS administrator and a 'super user'), which were not allocated to specific individuals; and
- one agency's user access had not been updated to reflect staff movements.

Recommendation No.9

4.33 The ANAO recommends that agency procedures provide for:

- requests for supplier master file changes and user access to be accompanied by supporting documentation; and
- changes to supplier master file data and user access to be reviewed on a periodic basis so that inappropriate changes can be detected.

³³ An official record, in this context, refers to the document being maintained in a formal recordkeeping system.

Agencies' responses

4.34 All of the agencies agreed with the recommendation. Specific comments provided by Treasury and ComSuper were as follows.

- Treasury is fully compliant with this recommendation.
- ComSuper considers that this procedure reduces the risk of fraud to the Commonwealth.

Electronic payments

4.35 All agencies made payments electronically and used a specific system to enable payment of transactions by transferring payment information from the FMIS to the relevant bank.

4.36 As a general principle, the administrator of these systems should not have the ability to process transactions such as transmitting payment files to the relevant bank. The ANAO noted however, that the administrators in three agencies did have the ability to transmit files to the bank.

Encryption of payment run report

4.37 To use the electronic payments system, a payment run report is usually generated to initiate the transfer of payment information. The ANAO considers that payment information (including details of supplier bank account numbers) should be encrypted to minimise the risks associated with processing staff having access to information, which can be manipulated.

4.38 In one agency, an internal audit review³⁴ had identified that un-encrypted payment run reports were being placed on a floppy disk prior to processing through the system. The agency, therefore, ran the risk that payment data could be manipulated. The ANAO found that this risk still existed.

Recommendation No.10

4.39 The ANAO recommends that agencies implement controls that:

- prohibit the administrators of electronic payments systems from being able to transfer payment information; and
- provide for data contained in payment run reports to be encrypted.

Agencies' responses

4.40 All of the agencies agreed with the recommendation. Specific comments provided by Treasury and ComSuper were as follows.

³⁴ Reported in May 2002.

- Treasury updated access to the electronic payments system in November 2003 to ensure that the administrator role was prohibited from transferring payment information. Treasury has encrypted the data contained in payment files since August 2002.
- ComSuper commented that transmission of payment files generated by the FMIS, can only be transferred to the bank by the IT area. For ReserveLink transmissions, the connect function has been removed from the Administrator.

Conclusion

4.41 All agencies, to varying degrees, needed to make improvements to the controls surrounding the verification of the authorising delegate and applying credit card delegations. Additionally, agencies need to review the design of their FMISs to assure themselves that controls relating to inappropriate access are adequate.

5. Monitoring and Review

Background

5.1 Monitoring and review is the final component of an effective control structure. The monitoring and review of the components of the control structure in place such as the financial delegations schedules and FMIS controls provide feedback and assurance to management on the effectiveness of the controls supporting the payment of accounts process and contributes to the continuous improvement of these controls.

5.2 Monitoring and review of the control structure can be undertaken in various ways, including:

- on-going monitoring which is an inherent part of the payment of accounts process, and by encouraging staff to identify breakdowns, redundancies, duplications and gaps in control procedures which in turn enhances ownership of controls by staff; and
- separate periodic reviews and evaluations, such as internal audit or process reviews. These reviews look at the effectiveness of control structures from another perspective and often provide the opportunity for continuous improvement.

5.3 The scope and frequency of monitoring and review activities will depend primarily on an assessment of risks and the effectiveness of on-going monitoring. The greater the on-going monitoring, the less need there will be for separate periodic reviews and evaluations. It is also important to note that the effectiveness and appropriateness of the control structure can change as the operational environment changes.

Audit findings and comments

5.4 The following table summarises the criteria that was used to assess an agency's monitoring and review activities.

Table 11

Audit criteria

Audit evaluation criteria

The agency conducts periodic internal monitoring of its financial delegations system to gain assurance that the instruments of delegation and policies and procedures relating to financial delegations are adhered to and properly applied. The agency also communicates the outcomes of periodic internal reviews of the financial delegations system to relevant staff.

The agency regularly reviews financial delegation guidance and/or instructions, and the training provided to staff.

5.5 The ANAO found that all agencies had conducted periodic reviews of relevance to financial delegations. For instance, two of the agencies had recently completed an internal review of financial delegations. The reviews resulted in the identification of a number of improvements designed to make the application of financial delegations easier to understand.

5.6 Another agency conducted bi-annual internal audits of its administrative processes, which included ensuring that the financial delegations schedules, CEIs and procedures relating to financial delegations are complied with. The remaining two agencies had reviewed financial delegations as a component of overall corporate governance or payment framework reviews.

5.7 The ANAO considers that, by conducting internal audits on agency's high risk areas, as well as areas of a low risk compliance nature, management gains assurance of the effectiveness and efficiency of business processes, management systems, control structures and the management of risks.

5.8 Further, outcomes flowing from the periodic internal reviews should be communicated to relevant staff. In all five audited agencies, internal audit reports and minutes of the audit committee meetings were accessible to all staff through the agency's intranet. In addition, the agencies communicated the detailed findings flowing from the internal audits to relevant staff.

5.9 However, the ANAO noted that in two of the five agencies, executive management had not followed up on the implementation of recommendations made in internal audit reports. For instance, in one of the two agencies, a recommendation relevant to financial delegations contained in an internal audit report, issued in February 2001, had not been implemented at the time of this audit. In the second agency, some of the proposed recommendations from an internal audit, conducted in early 2002, had not been implemented at the time of this audit. Neither management nor the audit committee had followed up on the recommendations.

5.10 The ANAO considers that audit committees should receive reports of action taken by the agency on the implementation of recommendations made in its internal audit reports, external audit reports and the Fraud Control Plan as a standard agenda item. This provides the audit committee with an opportunity to follow up on the implementation of recommendations made in its review processes. Better practice suggests that audit committees responsibilities should include 'monitoring and critiquing management's responsiveness to internal audit's findings and recommendations'³⁵.

³⁵ The Auditing and Assurance Standards Board of the Australian Accounting Research Foundation, The Australian Institute of Company Directors and The Institute of Internal Auditors—Australia, *Audit Committees Best Practice Guide*, 2001, pp.22–25.

5.11 As discussed in Chapter 3, one agency's CEIs were regularly reviewed so that they remained current, while the other agencies CEIs were either not up-to date or did not address the responsibility or timings for reviews of financial delegations.

Recommendation No.11

5.12 The ANAO recommends that executive management and audit committees of agencies follow up the implementation of recommendations flowing from internal audits and other review mechanisms in a timely manner, particularly where they relate to areas of significant risk.

Agencies' responses

5.13 All of the agencies agreed with the recommendation. Specific comments provided by Treasury and ComSuper were as follows.

- Treasury is fully compliant with this recommendation.
- ComSuper commented that all external and internal audit recommendations are provided at each meeting with the status towards implementation. The recommendations from this performance audit will be included and monitored by the Audit Committee until all recommendations have been addressed.

Conclusion

5.14 The agencies had established internal monitoring and review arrangements to gain assurance that policies surrounding financial delegations systems were adhered to and properly applied. However, these arrangements would be enhanced if recommendations flowing from internal audits and other review mechanisms were implemented in a timely manner and effectively followed up by management and audit committees. Internal and external audit recommendations should be regularly listed on audit committee agendas, so that the committee can review action taken, or proposed to be taken, to implement the recommendations.

Canberra ACT
16 April 2004



Pat Barrett
Auditor-General

Appendices

Appendix 1: Summary of Legislative Power to enter into contracts on behalf of the Commonwealth

Exercise of executive power of the Commonwealth	Delegation or authorisation of executive power to officials	Legislative constraints on the exercise of executive power to enter arrangements to spend public money
<p>Executive power of the Commonwealth exercisable by the Governor-General</p> <p>Section 61 of the Constitution.</p> <p>The Governor-General may appoint Ministers of State for the Commonwealth</p> <p>Section 64 of the Constitution.</p> <p><i>Ministers may exercise executive power on behalf of the Commonwealth.</i></p> <p>Chief Executives are responsible for promoting the proper use of Commonwealth resources.</p> <p>Section 44 of the FMA Act</p> <p><i>The power to enter into contracts is an inherent power of Chief Executives under section 44 of the FMA Act.</i></p>	<p>The Minister may <i>authorise</i> a person, under general legal principles, to act in his or her name for the purposes of exercising executive power under s.64 of the Constitution, including to enter an agreement on behalf of the Commonwealth.</p> <p>Typically the authorisation, and its specific scope, would be made in writing, although this is not mandatory.</p> <p>The power of the Chief Executive to enter an agreement on behalf of the Commonwealth can be <i>delegated</i> to officials under s.53 of the FMA Act.</p> <p>As with a Minister, Chief Executives can also <i>authorise</i> another person to act on behalf of the Chief Executive. This may also be done through an agency's Chief Executive's Instructions issued under s.52 of the FMA Act.</p>	<p>A person must not enter into an arrangement under which public money is or may become payable unless a proposal to spend public money has been approved (Reg 9) and, if necessary, authorised (Reg 10).</p> <p>FMA Regulation 13</p> <p>An approver must not approve a spending proposal without being satisfied that the expenditure:</p> <p>(a) accords with Commonwealth policies, (b) is efficient and effective, and (c) if related to special public money, is consistent with any terms applying to that money.*</p> <p>FMA Regulation 9</p> <p>Approvers must not approve spending proposals that are not covered by sufficient appropriation unless authorised in writing by the Finance Minister.</p> <p>FMA Regulation 10</p> <p>An official must not approve a proposal to spend public money unless authorised by a Minister, a Chief Executive, or by or under an Act to approve the proposal.</p> <p>FMA Regulation 11</p> <p>Approval of spending proposals must be recorded in writing as soon as practicable.</p> <p>FMA Regulation 12</p> <p>Approvers includes a Minister, a Chief Executive, the Auditor-General and the Presiding Officer(s).</p> <p>FMA Regulation 3</p> <p>Section 51 of the <i>Auditor-General Act 1997</i> Section 36 of the FMA Act</p>

Source: Department of Finance and Administration

***Note:** Special public money, as with all public money, forms part of the Consolidated Revenue Fund under section 81 of the Constitution, and can only be spent under an appropriation: see Finance Circular 2003/10 *Special Instruction regarding Special Public Money*.

Appendix 2: Relevant Legislation

FMA Act

44 Promoting efficient, effective and ethical use of Commonwealth resources

- (1) A Chief Executive must manage the affairs of the Agency in a way that promotes proper use of the Commonwealth resources for which the Chief Executive is responsible.
- (2) If compliance with the requirements of the regulations, Finance Minister's Orders, Special Instructions or any other law would hinder or prevent the proper use of those resources, the Chief Executive must manage so as to promote proper use of those resources to the greatest extent practicable while complying with those requirements.
- (3) In this section:
proper use means efficient, effective and ethical use

FMA Regulations 9–13

9 Approval of spending proposals—principles

- (1) An approver must not approve a proposal to spend public money (including a notional payment within the meaning of section 6 of the Act) unless the approver is satisfied, after making such inquiries as are reasonable, that the proposed expenditure:
 - (a) is in accordance with the policies of the Commonwealth; and
 - (b) will make efficient and effective use of the public money; and
 - (c) if the proposal is one to spend special public money, is consistent with the terms under which the money is held by the Commonwealth.
- (2) Subregulation (1) does not apply to a proposal by an intelligence or security agency to spend operational money within the meaning of section 5 of the Act as modified in accordance with Schedule 2.

10 Approval of future spending proposals

If any of the expenditure under a spending proposal is expenditure for which an appropriation of money is not authorised by the provisions of an existing law or a proposed law that is before the

Parliament, an approver must not approve the proposal unless the Finance Minister has given written authorisation for the approval.

11 Approval of spending proposals—officials

An official must not approve a proposal to spend public money unless authorised by a Minister or Chief Executive, or by or under an Act, to approve the proposal.

12 Approval to be recorded

If approval of a proposal to spend public money is not given in writing, the approver must record the terms of the approval in a document as soon as practicable after giving the approval.

Note Document is not limited to paper documents: *Acts Interpretation Act 1901*, s 25.

13 Entering into contracts etc

A person must not enter into a contract, agreement or arrangement under which public money is, or may become, payable (including a notional payment within the meaning of section 6 of the Act) unless a proposal to spend public money for the proposed contract, agreement or arrangement has been approved under regulation 9 and, if necessary, in accordance with regulation 10.

Appendix 3: ABS Statistical Testing

The ANAO consulted the Australian Bureau of Statistics (ABS) on the audit sampling approach to statistical sampling. The ABS confirmed that:

- a sample size of 150 transactions for each agency allowed the audit to support conclusions about estimates of the population; and
- stratified random sampling was a preferred methodology in the circumstances as it provided a random sample with reasonable coverage of different types of transactions and allowed the audit to make valid inferences about the population.

The design of the sample was based on the assumption that the expected error rate in the population was likely to lie between the range 0% and 5% (2.5% error rate—the midpoint of the range).

A 95% confidence interval that spans between 0% and 5% error rate, was used as the accuracy constraint.

Transactions for each agency were stratified, with the sample allocated to strata proportional to population size.

Appendix 4: Agency comments

The comments provided by each of the audited organisations and the Department of Finance and Administration in response to the audit report are shown below.

AusAID

AusAID welcomes the ANAO report, in particular the highlighting of sound and better practice and considers the recommendations of the report a useful basis for further strengthening of its financial control framework. Some of the findings and better practices have already been adopted within the agency's CEIs, delegations and processes while others will be considered over the coming months.

ACCC

The Australian Competition and Consumer Commission notes the proposed report and agrees with the recommendations in it.

One particular point that was identified by ANAO, and, is an issue for the smaller agencies is the limited staff resources available to implement best practice control environments. The ACCC has a limited number of staff in its Accounts unit and therefore has to manage the operational risks associated with the payments system and determine the most appropriate balance between preventative and detective controls. This will no doubt be the case for most of the smaller agencies. However it is agreed that ultimately the agency must be satisfied that any identified risks are being adequately addressed.

ComSuper

As a result of financial delegations process our agency fully understands the need to review its CEIs and financial delegations. The review of the CEIs has already commenced, with new guidelines complementing existing CEIs. Participation in the review highlighted areas of improvement and gave us the opportunity to make permanent changes for a more proficient workplace. A regular review of financial delegations is supported as a measure across the Commonwealth to ensure expenditure of public monies operates with effectiveness and efficiency.

Department of the Treasury

Treasury values the work undertaken by the Australian National Audit Office in relation to their audit on *Financial Delegations for the Expenditure of Public Monies*. The Department agrees with the recommendations contained in the report and is pleased that the ANAO has identified a number of Treasury's processes as sound and better practices.

Office of the Director of Public Prosecutions

We agree with all the recommendations made.

We thank the ANAO for the constructive manner in which the audit was undertaken; we will take steps to lift our standard. We see merit in the ANAO, together with the Department of Finance and Administration, preparing a Better Practice Guide on Chief Executive Instructions and Chief Executive Delegations, include a model set of the Instructions and the Delegations. Such a guide would be very useful for small agencies that do not necessarily have the resources available to review these items on a regular basis.

Department of Finance and Administration

Finance considered that the proposed report extracts provide an appropriate summary of the financial framework legislative requirements and the policy that supports its implementation.

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