

publicfinance inVictoria

PRACTICES & LEGISLATION

discussion paper

october 2008

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Foreword

There are three 'pillars' of public administration in Victoria – the *Constitution Act 1975*, the *Public Administration Act 2004* and the *Financial Management Act 1994*.

In the fourteen years that have followed the introduction of the Financial Management Act, public financial management has evolved significantly in Victoria and in many other jurisdictions throughout the world.

The Victorian Government recognises that this evolution presents new challenges for providing transparent and accountable government. Since its election in 1999, the government has been a leader in reforming public administration and improving government transparency and accountability. Independent economic consultancy Access Economics has recently upgraded the Victorian Government's fiscal transparency rating to the highest ranking of A+. This makes Victoria the most transparent Australian state in terms of financial reporting.

The government has already thoroughly reviewed the Constitution Act and introduced the Public Administration Act. Now, as part of our 2006 election commitment to modernise fundamental legislation in Victoria, we are reviewing the state's public finance legislation. This review was foreshadowed in the 2008 Annual Statement of Government Intentions.

This review will play an important role in determining the relationship between parliament and executive government for the next generation and in ensuring that government in Victoria is even more accountable, accessible and transparent.

As part of this review, this discussion paper is designed to canvass the views of the community and stakeholders about how new public finance legislation can meet contemporary needs, and be responsive to the needs of future generations.

We will consult widely in this review and consider all perspectives.

In reading and responding to the issues raised in this discussion paper, you will be contributing directly to reforming public finance in Victoria.

TIM HOLDING MP

Minister for Finance, WorkCover
and the Transport Accident Commission.

October 2008

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Introduction

The key legislation for Victoria's public financial management, the Financial Management Act, was enacted in 1994. Since then public financial management, and the public sector more broadly, have changed considerably.

Today, the Victorian public sector comprises ten government departments and numerous other entities, often working in partnership with the private sector and non-government organisations. These institutions work closely together in an environment with fewer boundaries and more emphasis on personalised service delivery, citizen engagement and participation. In addition, citizens now expect to be able to find out, with minimal effort, how their government has performed in delivering a range of key policies and initiatives. Advances in information and communication technology mean that governments can interact with citizens in a greater range of ways, and citizens can be more easily informed about the workings of government.

Victoria's financial management framework has evolved to reflect these broader public sector changes. With these changes, new opportunities and responsibilities have evolved for both the parliament and executive government. This has resulted in a dramatic shift in accountability. For its part, government has been granted greater flexibility to pursue its objectives whereas parliament, which traditionally relied on a rudimentary test of whether appropriated funds had been spent, now queries whether those funds have been spent efficiently and effectively.

Some of the specific financial reforms over the past fourteen years include:

- introduction of an accrual-based output management framework
- enshrining in the Constitution the position of the Auditor-General as an independent officer of the Parliament and requiring that any changes to that officer's powers be approved in a referendum
- establishment of a comprehensive financial management compliance framework
- institutionalisation of the Auditor-General's annual review of the assumptions and methodology underpinning the government's estimated financial statements included in budget papers – a world first
- development of a comprehensive and transparent financial reporting framework, including the requirement for the Department of Treasury and Finance to publish a Pre-Election Budget Update (PEBU) once a general election is called
- enshrining in legislation the basic principles of sound financial management to which the government must adhere.

More broadly, the Victorian Government has a strong record of achievement in public sector reform. Since it was elected in 1999, the government has reformed the state's Constitution Act and introduced the Public Administration Act.

Now, to ensure that Victoria remains a leader in public sector management for the next generation, the government is comprehensively reviewing its public finance legislation and practices.

Scope and process of the review

The goal of the review is to introduce a new Bill to replace the Financial Management Act. The review is considering the following matters.

- What represents best contemporary management practice for the key elements of financial management, including planning, governance, resource allocation, resource management and accountability?
- What would be best practice for Victoria's public finance legislative framework?
- What financial management structure would best support the Westminster system of government in Victoria?

In addition to the Financial Management Act, the review is considering a number of related Acts with the aim of building a more cohesive legislative framework for public finance. These include the *Borrowing and Investment Powers Act 1987*, the *Administrative Arrangements Act 1983*, the *Monetary Units Act 2004* and the *Public Authorities (Dividends) Act 1983*.

The review focuses on expenditure and governance rather than taxation and other sources of revenue.

The premise of the review is that legislative reform will enable Victoria's public finance system to better meet the needs of the community, parliament and government.

To inform this process, consultation is essential. The government is seeking community and stakeholder views on what arrangements might enable Victoria to have the best public finance system.

This discussion paper outlines the key issues and a range of options identified in the review. It poses a number of questions that interested parties might consider when making their comments.

1. Victoria's current public finance system

This chapter describes the key participants in Victoria's public finance system and its current legislative, policy and management frameworks. It also provides a high-level overview of the history of financial reform in Victoria.

1.1 Key participants in the public finance system

Any system of public finance features a range of participants with specific roles, responsibilities and relationships. An overview of these roles in Victoria is provided below.

Parliament

Parliament is central to Victoria's system of government, which is based on the Westminster system.

In this system, people elect members of parliament to represent them and the government is formed by the political party or parties who form a majority in the lower House of parliament, the Assembly. The government is accountable, through its ministers, to parliament.

Parliament acts as a primary forum for public debate about matters of public importance generally, and about the programs and priorities of the government. In addition, parliament makes rules for financial governance and administration, and authorises the appropriation of funds to the executive.

Parliament puts the government's performance on the public record. The Victorian Parliament generally applies this scrutiny through the Public Accounts and Estimates Committee (PAEC) and the Auditor-General.

Public Accounts and Estimates Committee

The PAEC is a joint House investigatory committee of the Victorian Parliament. The committee is responsible for scrutinising both the public accounts and the budget estimates. The committee has a range of functions. These include inquiring into, considering and reporting to parliament on matters of public administration or public sector finances, the annual estimates or receipts and payments, and other budget papers.

Auditor-General

The principal role of the Auditor-General is to provide assurance to parliament on the accountability and performance of the government. As an independent officer of the Victorian Parliament, established under Victoria's Constitution Act, the Auditor-General is responsible for the audit of around 650 public sector organisations. Audit findings and recommendations address, among other things:

- the degree to which value-for-money has been achieved
- the effectiveness of organisations in meeting government objectives
- the fair presentation of annual financial statements.

Department of Treasury & Finance

Executive government

The Victorian Constitution states that the role of executive government is 'to govern for and on behalf of the people of Victoria'. In the context of this review, this role includes achieving outcomes through the delivery of goods and services, and ensuring that all parts of the public sector follow sound governance and financial management principles. The relationship of executive government and parliament is embodied in rules relating to taxation, appropriation, reporting and broader accountability.

Public finance ministers

The Treasurer and the Minister for Finance have specific roles in relation to the management of the state's finances. Together, they are responsible for:

- the preparation and delivery of the annual state Budget
- revenue collection, borrowing, investment and financial arrangements to hedge, protect or manage the state's financial interests
- promoting economic growth across the State of Victoria
- providing investment and fund management services to the state and its statutory authorities
- overseeing the net assets, total revenues and expenses of consolidated reporting entities
- the state's financial reporting and accountability framework
- administering and coordinating certain Victorian Government land and property
- purchasing and procurement arrangements for the Victorian Government
- overseeing policy in relation to statutory insurance and public sector superannuation.

Departments

Department is the term used in Victoria to describe the administrative units allocated to the operations of government. Departments differ in the type of functions and activities they undertake. For example, some departments deliver programs and services, others are more administrative in nature, while some perform a central coordinating role across the whole of government.

Entities

For the purpose of this paper, entity refers to all units of the state government in Victoria that are not departments. The consistency of definitions for entities across Victorian legislation is a key issue discussed later in this paper.

1.2 Legislative framework

Victoria's public finances are founded on a number of key pieces of legislation – the Constitution Act, appropriation Acts, the Public Administration Act, the Administrative Arrangements Act, the Financial Management Act and the *Audit Act 1994*. Each of these Acts, in the context of financial management, is detailed below.

Constitution Act 1975

The Constitution Act establishes democratic government in Victoria and defines many of the roles and responsibilities of parliament and executive government. It sets out the broad powers for government to use public money and collect revenue. Parliament appropriates this revenue for specific purposes, but only on the initiative of executive government (see annual appropriation Acts below).

The Constitution Act also sets out a requirement for 'warrants'. A warrant is a written authority to spend specified sums during the financial year from the consolidated fund, the government's bank account. A warrant must be signed by the Treasurer, the Auditor-General and the Governor. Conceptually, a warrant is similar to an approval to draw cheques on a bank account.

Appropriation Acts

The annual appropriation Acts are one of the instruments through which the Parliament authorises executive government to disburse public money. They provide the legal authority for the government to make payments from the consolidated fund.

In Victoria, all appropriation Bills must originate in the Legislative Assembly (lower House) and annual appropriation Bills may become law without the support of the Legislative Council (upper House).

The Financial Management Act requires the annual appropriation Bills to be accompanied and supported by supplementary information in the budget papers.

In addition to the authority provided under annual appropriation Acts, parliament authorises various special (standing) appropriations. Special appropriations represent a standing authority and do not lapse each year as annual appropriations do. They may be established in any legislation and remain in force until the legislation is amended or repealed by parliament. Special appropriations are generally used for ongoing payments which need to be made independently of the government's annual resource allocation process, such as the salaries of the judiciary and the costs of parliament. They can also be used for one-off payments.

Public Administration Act 2004

The Public Administration Act provides a framework for good governance in the Victorian public sector and in public administration generally in Victoria. The Public Administration Act defines the organisations that comprise the Victorian public sector: public service bodies, special bodies and public entities. The Act also dictates the responsibilities of department and administrative heads, duties of public entities and accountability requirements.

Administrative Arrangements Act 1983

The Administrative Arrangements Act provides for the transfer of the administration of an Act or of a function of government between ministers and departments. This is called an administrative or a machinery of government change.

Financial Management Act 1994

The Financial Management Act is the primary focus of this review. It governs the use of public money, and the accountability processes and subordinate legislation with which government is obliged to comply. Specifically, it:

- prescribes the collection, expenditure and management of public money and other public resources (including public and other property)
- sets out the subsequent accounting and reporting for this public money and resources
- establishes and defines the scope of the consolidated fund and the trust fund
- establishes financial responsibility and budget management provisions associated with these functions.

The Financial Management Act authorises the Governor in Council (through regulation) or the Minister for Finance (through ministerial directions) to set and administer detailed rules for public financial management.

Audit Act 1994

The Audit Act prescribes the auditing and reporting powers of the Auditor-General. The Act empowers the Auditor-General to audit the state's consolidated financial report, and the financial reports of individual departments and other public sector organisations. The Act also authorises the Auditor-General to conduct performance audits and review the government's estimated financial statements published in the budget papers.

1.3 Management frameworks

In addition to the legislative framework set out above, there are a number of management frameworks that operate in Victoria.

Integrated Management Cycle

The Victorian Government follows an annual cycle, the Integrated Management Cycle (IMC), which aligns its resource management, planning, decision making, monitoring and reporting processes. In essence the IMC comprises four elements which, taken together, form a continuous cycle of planning, resource allocation, service delivery and accountability.

- **Planning** processes articulate the government's desired outcomes and strategic priorities, and provide the foundation for planning by departments and entities.
- **Resource allocation** matches resources to the goods and services that will contribute to the government's desired outcomes. These should be consistent with the strategic priorities that were formulated and agreed during the planning phase. At the whole-of-government level, this phase mainly occurs through the annual budget process.
- **Service delivery** by departments delivers agreed goods and services, to agreed performance standards, consistent with decisions made in the planning and resource allocation phases.
- **Accountability** processes evaluate, review and report on performance at the whole-of-government, department and entity level. They include both internal and external evaluation and reporting processes.

Output Management Framework

Victoria's public finance system is based on an 'output' management framework. Outputs are goods or services produced or delivered by, or on behalf of, a department or entity. Under this model, resource allocation decisions about the nature and mix of outputs should be based on each output's expected contribution to government outcomes.

The delivery of outputs is a key indicator of Victorian Government performance. Output performance measures (stated in terms of quality, quantity, timeliness and cost) describe each department's agreed service delivery performance. Performance against these measures is reported annually in the budget papers and in departmental annual reports. Reporting results against performance measures demonstrates the extent to which the goods and services paid for by government have been delivered.

Asset Management Framework

The Asset Management Framework aims to ensure Victoria's asset base best supports the government's service delivery requirements. The framework includes a series of strategies and planning tools that assist government to manage the state's assets over the longer term. The framework allows government to agree with departments on the services they need to deliver in the medium-to-long term. They then develop strategies to make sure the necessary assets are available to support the delivery of these services.

Financial Management Compliance Framework

The Financial Management Compliance Framework is a mechanism to satisfy the government that departments and entities have fulfilled their financial management obligations under the Financial Management Act, and ministerial directions. The framework is based on best practice in financial management such as the requirement for each entity to establish an audit committee and an internal audit function. The central assurance mechanism is an annual certification process. Entities must provide their relevant minister with letters certifying that they are complying with the standing directions, and departments provide to the Minister for Finance corresponding portfolio summaries.

Victorian Government Risk Management Framework

The Victorian Government Risk Management Framework supports good public sector risk management by providing information on governance policies, accountabilities and role and responsibilities for all those involved in risk management. The framework also provides for a minimum standard of risk management for public sector entities. This requirement is built into annual corporate planning and reporting processes: each accountable officer must attest in their annual report that the standards have been met. It also promotes awareness of risk management not only for a specific department or entity, but at inter-agency and whole-of-government levels.

Other rules and guidance material

The government also issues rules and various guidance materials including budget and financial management guidances, Treasury management guidelines and investment lifecycle guidelines.

As required by the Financial Management Act, financial reports are prepared using the latest, relevant accounting standards issued by the Australian Accounting Standards Board.

1.4 History of financial reform in Victoria

The evolution of Victoria's financial management practices should be considered in the broader context of wide-ranging reforms in public management, the most significant taking place over the last thirty years.

The 1980s and 1990s was a period of reflection about the effectiveness of the public service in carrying out its core functions. Reforms of this period aimed to make the public service more flexible and efficient, and more responsive to government direction.

Modern public service became characterised by a stronger focus on objectives, with performance being assessed on the basis of results. Private sector management and employment practices were commonly adopted in the public sector; for example, the concept of contestability was introduced.

These broader reforms gave rise to new forms of financial management and planning. In Victoria, program budgeting was introduced in the 1980s. However, program budgeting continued to focus on inputs (such as staffing requirements) rather than outputs.

The Financial Management Act and Audit Act were introduced in 1994, following a Victorian Commission of Audit review of Victoria's public sector finances. This review recommended fundamental changes to governance structures, and transformed public sector accounting and accountability techniques. Consequential changes included the introduction of three-year forward estimates, and budget flexibility measures (including global appropriations), and corresponding accountability measures, such as more timely reporting, and auditing of departments and entities.

Reform continued throughout the 1990s, aiming to more closely align departmental activities and services with government priorities, and to improve value for money. This resulted in amendments to the Financial Management Act in 1998, including:

- a shift in focus from inputs to output budgeting and reporting for performance
- a shift in focus from cash-based accounting to a mix of cash and accrual accounting
- allocation of funds based on the full cost of services agreed to be delivered.

These reforms provided a framework for longer term thinking and planning about resource allocation issues. Although the framework maintained an annual financial focus, it anticipated that longer term considerations such as the role of assets in service delivery, modes of service delivery and desired outcomes would evolve over time. Unlike some other jurisdictions, the Victorian model did not emphasise outcomes. In the first instance, the framework concentrated on outputs. This was part of a deliberate incremental strategy to emphasise outcomes once the output management framework was in place.

Further amendments to the Financial Management Act in 2000 were founded on a platform of sound economic management, transparency and accountability. The *Financial Management (Financial Responsibility) Act 2000* introduced principles of sound financial management and required the government to publish longer term financial policies and objectives. The amendments also enhanced accountability by incorporating a detailed and consistent whole-of-government reporting framework.

While the legislation does not require the specification of outcomes, in 2001 the Victorian Government released *Growing Victoria Together*, its ten-year vision for Victoria. *Growing Victoria Together* sets out long-term goals (or outcomes), including performance measures, for social, environmental and economic progress. Progress against these performance measures is reported annually in the *Growing Victoria Together* Progress Report published in the budget papers. *Growing Victoria Together* was revised in 2005.

2. The case for change

The previous chapter described the evolution of the current framework and key participants in Victoria's public finance system. This chapter considers the case for reform.

Expectations and demands on government are increasing. With improvements in technology people expect more streamlined and simpler interactions with government, and information on performance that is clear and accessible. People want more flexible and adaptable services, and they expect these services to be delivered seamlessly, regardless of the diversity of entities that may be involved. The public also expects government to respond to increasingly complex policy issues and deliver optimum outcomes. Finally, the public wants to know what outcomes the government plans to achieve and how it plans to achieve them.

Worldwide trends show that governments are evolving in a number of different ways to meet these demands. The case for change in Victoria now is substantially informed by those trends in thinking and practice.

An important part of modernising Victoria's public administration is to simplify the public finance system. All participants should clearly understand their functions, what they are accountable for and to whom they are accountable.

2.1 Emerging thinking and trends

Outcomes

There are many benefits to focusing on outcomes. First, it provides a more strategic focus for government to ensure that its policies and programs are directly connected to things that matter to citizens: it shifts the focus of government away from inputs and outputs, towards benefits and results. Further, it is more likely to ensure that funds are allocated where they are most likely to maximise the achievement of outcomes. It also provides a potential framework for joined-up government where more than one department or entity is expected to make a contribution to a government outcome.¹

Victoria is in a strong position to formally add an outcomes focus to the management framework. As a leader in the adoption of output-based management in Australia, Victoria has developed a solid foundation in output planning, budgeting, delivery and reporting. Already, the Victorian public sector has been aligning plans and performance measures with desired government outcomes. It has put in place outcomes-focused reporting arrangements such as the *Growing Victoria Together* Progress Report, sustainability reporting and triple bottom line reporting. These have evolved beyond traditional reporting on financial performance to incorporate environmental and social objectives.

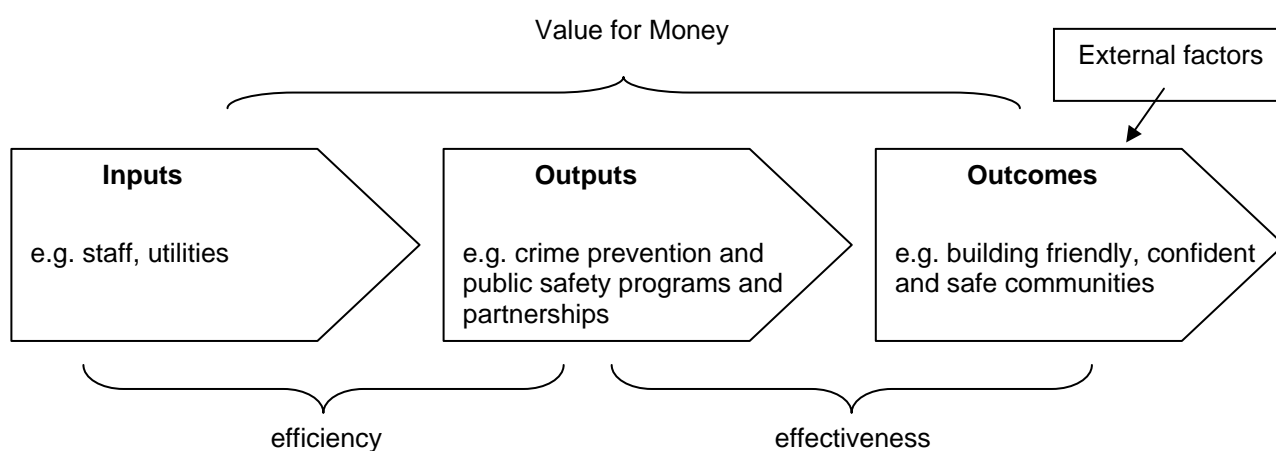
With this strong foundation in place, Victoria has an opportunity to be a leader in the design of the next generation of outcomes-orientated systems. This could involve embedding the use of outputs and outcomes performance information more deeply in the strategic allocation of government resources.

A focus on outcomes can make an important contribution to improving government transparency and accountability. A heightened focus on outcomes is a prominent worldwide trend in public finance. This approach emphasises how outputs contribute to desired outcomes and provides more meaningful information for parliament and the general public on government outcome performance. Jurisdictions that have adopted an outcomes-focused approach include New Zealand, the United Kingdom, Canada (British Columbia and Alberta), the Netherlands, Sweden, and Scotland.

Under an outcomes-focused management system, the achievement of outcomes, together with the delivery of outputs becomes the key indicator of government performance for which government is accountable. It enables citizens to assess whether government has achieved its objectives, rather than how much money has been allocated and spent on a particular good or service. Parliament and the general public can hold the government accountable for delivering the mix of services that makes the greatest contribution to the achievement of desired outcomes.

In practice, an outcomes approach demands clearer connections between inputs and outputs, and in turn, outcomes (see Diagram 1). Creating these links requires financial and non-financial information to show how goods and services are contributing to broader government outcomes. To implement an outcomes-based management approach the public finance system needs to integrate outputs and outcomes including government planning, resource allocation, performance measurement and reporting functions.

Diagram 1: Linkage between inputs, outputs and outcomes



Source: Victorian Department of Treasury and Finance (adapted from Z Noman, 'Performance Budgeting in the United Kingdom', *OECD Journal on Budgeting*, vol. 8, no. 1, 2008, p. 78).

To further strengthen accountability, some jurisdictions have adopted formal mechanisms for their outcomes planning, performance measurement and reporting. For example, in the United Kingdom, public service agreements set out the priority outcomes the government wants to achieve over the next spending period, including aims, objectives and outcome targets. The departments report annual progress against these public service agreements and departmental objectives.

It is important to recognise that a focus on outcomes is not without its challenges, particularly in the area of performance measurement. Ensuring timely, reliable and valid information is a key challenge for all jurisdictions, along with the development of good data systems, clear objectives and accurate performance measures.² A strengthened focus on non-financial reporting may also require a re-balancing of financial and non-financial reporting requirements to minimise the reporting burden on government.

Outcomes may also require a longer term outlook when compared with outputs. Such a longer term approach has also been implemented by some jurisdictions in the area of expenditure and appropriation reforms. These reforms have included the introduction of multi-year appropriations or appropriations of unlimited duration. Certain expenditures, such as investment projects that require long-term planning horizons, are approved on a multi-year basis. In some jurisdictions, including the United Kingdom, Sweden, and Finland, multi-year expenditure planning and budgeting has led to the setting of firm expenditure ceilings. In some instances, these ceilings cover a large proportion of central government spending and are reviewed periodically.

Outcomes in the Australian context

An Australian example of focusing on outcomes is the new Commonwealth-state financial framework being negotiated by the Council of Australian Governments (COAG).

This reform seeks to increase the flexibility of states in their use of Commonwealth tied grants, while increasing the accountability of all governments to their citizens for achieving planned outcomes.

This approach recognises the benefit of a partnership between Commonwealth and state governments in delivering shared objectives and outcomes. It also recognises that both levels of government are first and foremost accountable to their electorates for their performance, rather than to other levels of government.

Key changes which have been agreed by COAG include:

- greater focus on outputs and outcomes to replace prescriptive controls on the use of Commonwealth or state resources to achieve agreed outcomes
- rationalisation of a number of existing specific purpose payments (SPPs) into a smaller number of broad, flexible funding agreements focused on shared objectives and aspirational outcomes
- provision of national partnership agreements to support the delivery of specified projects or to drive reforms of national importance
- new performance reporting framework, focusing on providing meaningful, publicly available information on the progress of all governments towards stated objectives
- central payments to each state treasury, which will then distribute the funding within its jurisdiction according to its resource allocation processes.

Most of the new arrangements are due to commence in the first half of 2009.

'Joined-up' government

Improved collaboration and integration across government is a priority for jurisdictions across the globe. Traditionally, governments have been organised with vertical, confined structures, aligned to the delivery of particular services such as hospitals or schools. This structure can provide efficiency, clear lines of accountability and concentration of specialist knowledge. However, vertical structures are not always well equipped to deal with many contemporary public policy issues, such as climate change or social disadvantage, which require action across many portfolios.

The move to horizontal, joined-up arrangements (also known as 'networked government') recognises that no one organisation has sufficient knowledge or resources to effectively address commonly encountered public issues on its own.

Victoria is already well down the path of operating joined-up government. For example, the approaches to reducing family violence and improving road safety are jointly administered by several departments and entities, with clear particular and common responsibilities. However, Victorian Government systems and processes could be improved to further encourage and enhance this approach to service delivery. This will affect all elements of the framework: planning, resource allocation, service delivery and accountability.

Engaging citizens

Another new focus of public administration is the relationship between the citizen and the state, and the growing desire for strengthened community and individual engagement with government.

Many governments worldwide have identified a trend of citizens expecting and demanding improved service from government. Specifically, they expect:

- higher levels of transparency and accountability for results
- services that are more flexible and adaptable, more holistic and tailored to their needs, and delivered in a way that best meets their needs
- cohesive policy responses from all levels of government that address the growing complexity of cultural, social, environmental and economic issues.

For Victoria, there is an opportunity to continue to strengthen citizen engagement, in areas such as planning and reporting. This approach would build on recent developments such as the Annual Statement of Government Intentions, which aims to engage the public in the legislative program, increase government accountability and build trust. It would better equip the public and parliament to assess government progress against its objectives and would likely involve increased web-based and short-form reporting.

A related recent development is a body of work concerning 'public value'.³ While there are different approaches to the subject, the consensus is that public value is determined by the value that citizens place on services, or infrastructure, or general government efficiency. The quality of services (outputs), as well as the broader outcomes achieved and the trust generated, are all central to public value. Although the concept is still developing and there is some debate as to its applicability in some jurisdictions, it is increasingly being used in management frameworks or service delivery objectives.⁴

2.2 Modernisation and simplification

Since its introduction in 1994, the Financial Management Act has been amended on a number of occasions to deal with issues as they arise. This has led to inconsistencies in the language and application of the Act, and inconsistencies with other legislation. Various requirements set out in different but related legislation give rise to even more complexity.

Further, more sophisticated and flexible approaches to appropriation and procurement have developed since the Act's inception and should arguably be incorporated into Victoria's public financial management legislation.

2.2.1 Entities

A key example of the Financial Management Act's complexity is its lack of clarity about which entities are a 'public body' for the purpose of public finance legislation. Public sector entities are defined and categorised under several state Acts, and different aspects of the governance of entities are regulated by different pieces of legislation. These include, for example, the Financial Management Act, the Public Administration Act, *Victorian Managed Insurance Authority Act 1996* and various establishing legislation. This has led to a degree of ambiguity and inconsistency in applying the terms defined across the various Acts and the corresponding requirements of entities. There is a need to provide a clear and consistent definition for public entities, and to establish a consistent reporting and governance framework for them.

The categorisation of entities is further complicated by the different functions they undertake, and the way in which they are held accountable.

Some of the requirements of the Financial Management Act are also 'one-size-fits-all' in nature; they fail to tailor requirements or needs to match the varying size, complexity and function of entities.

2.2.2 Accrual-based appropriations and flexibility

In 1998-99, the Victorian Government adopted an accrual-based budgeting and appropriation framework. Despite these changes, there are some elements of Victoria's appropriation mechanism that date back to a time when it focused solely on cash. At the time of these reforms, it was thought that a strong focus on accrual reporting might detract from the management of cash flows. Administrative tools and the utilisation of accounting formats such as cash-flow statements continue to recognise the essential nature of cash, both in the context of government's operations and in explaining a more complex and integrated financial picture. However, some residual elements of the cash system, such as warrants and special appropriations, could be reassessed, given that the adequacy of controls in the accrual environment has now been established.

There are also some highly detailed and prescriptive legislative provisions in the Financial Management Act which constrain executive government's management flexibility while delivering very little additional information or control of executive government to parliament. Examples of these provisions include restrictions on shifting or augmenting appropriations.

2.2.3 Reporting

The Financial Management Act requires the tabling in parliament of:

- the Annual Financial Report
- the Mid-year Financial Report
- quarterly financial reports
- the estimated financial statements as part of the annual Budget
- the estimated financial statements as part of the Budget Update.

Victorian Government financial reports are presented in a format that complies with both prescribed Australian Accounting Standards Board and Uniform Presentation Framework standards.

Increasingly, public sector reporting standards have become more closely aligned with those in the private sector.

The current level and type of financial reporting in Victoria should be evaluated to ensure it is achieving the appropriate balance between transparency and reporting burden.

2.2.4 Other public finance legislation

Consistent with the Victorian Government's election commitment to modernise all legislation and reduce the number of Acts, this review provides an opportunity to do this for public finance legislation. The Acts and provisions being considered are:

- *Borrowing and Investment Powers Act 1987*
- *Monetary Units Act 2004*

Department of Treasury & Finance

- *Public Authorities (Dividends) Act 1983*
- existing property and land functions currently contained in the Financial Management Act.

The above Acts all deal with elements of public finance. To this end, consolidating the Acts would provide a more consistent and comprehensive financial management framework for Victoria. Further, since the introduction of several of the Acts, there have been changes to the number of entities to which these Acts apply, particularly the *Borrowing and Investment Powers Act 1987* and the *Public Authorities (Dividends) Act 1983*. This raises the question as to whether a more appropriate structure could administer the relevant provisions in these Acts, rather than maintaining separate Acts.

2.2.5 Procurement

An effective governance framework for procurement is an important element of public financial administration. In the mid 1990s, in order to achieve greater value for money in government purchases, the centralised purchasing body, the State Tender Board, was replaced with accredited purchasing units within individual departments. At the same time, the Victorian Government Purchasing Board (VGPB) was established under the Financial Management Act to:

- develop, implement and review policies and practices pertaining to the supply of goods and services to departments and the management and disposal of goods by departments, and to provide advice, staff training and consultancy services
- monitor departmental compliance with supply policies and ministerial directions, and to report irregularities to the Minister for Finance and the relevant portfolio minister
- foster improvements in the use and application of purchasing systems and electronic trading
- establish and maintain a comprehensive database of purchasing data of departments and supply markets for access by departments.

Over the past decade, a rigorous process has been developed to ensure a high level of probity and accountability in Victorian Government procurement. The elements include probity advisors, probity auditors, requirements for probity plans, the contract publishing system and a requirement to report policy breaches. The *Whistleblowers Protection Act 2001* was introduced to encourage and facilitate disclosures of improper conduct by public officers and public bodies. More broadly, scrutinising bodies such as the State Services Authority, the Auditor-General and the Ombudsman now play a greater role in ensuring probity and accountability.

Beyond the probity aspects, some of the key activities ascribed to the VGPB have been transferred to specialist teams in government departments. At the same time, functions such as policy development and implementation, and the focus on improvements and adoption of purchasing systems have been undertaken centrally.

Given these developments, it is worth considering how these procurement issues should be addressed in the development of a modern public finance system.

3. Possible directions for reform

The previous chapter discussed the various developments and considerations informing this review. These covered the trends and emerging developments in public sector financial management towards a greater focus on outcomes and the need to reduce complexity and ambiguity.

3.1 An outcomes framework

A more outcomes-focused approach to public finance would change planning, resource allocation and accountability aspects of the management framework.

A focus on outcomes will enhance the strategic focus of government, and facilitate joined-up government, because we now recognise that many desired outcomes can only be achieved through the collaborative effort of multiple departments and entities. It is also consistent with evolving citizens' demands of government for efficient delivery of flexible, personalised services; bureaucratic arrangements for their delivery are of little interest to citizens.

3.1.1 Planning

Plans establish a benchmark against which actual performance can be measured and reviewed. It is appropriate for government to set short, medium and long-term goals for the overall direction of the state, with appropriate milestones for assessing intermediate performance.

The Financial Management Act includes a range of provisions relating to sound financial and budget management but it does not explicitly require the development of outcome plans or the presentation of progress against the outcomes to parliament. A key consideration for this review is to determine whether whole-of-government and departmental strategic plans should be an obligation under legislation, in addition to existing fiscal plans and budget policy statements that are presented annually.

A strengthened strategic and integrated planning framework, with stronger linkages between outputs and outcomes would be consistent with the direction of current practice, and with the perceived benefits of an outcomes-orientated approach.

Departments and entities could be required to develop strategic and operational plans that outline how their outputs will help create public value and contribute to government outcomes, and how each of these will be measured. Entities could prepare plans independently of departments, or their contribution could be included in departmental plans.

Strategic plans could include a mix of quantitative and qualitative measures, accompanied by explanatory narrative. Such plans could also cover the full range of time frames from the short term through to the inter-generational.

Given the discussion above, you may wish to respond to the following questions.

Should a requirement to develop strategic plans be embedded in legislation?

If so, should strategic plans be at the level of:

- **whole-of-government**
- **departments**
- **entities?**

What form should these strategic plans take?

3.1.2 Providing and allocating resources

Strategic plans should inform priorities in deciding resource allocations (the budget process). A stronger alignment between government priorities and the allocation of resources is likely to enhance efficiency and provide a better mechanism for creating and measuring public value.

With an increased focus on outcomes, a modern public finance system should ensure that clearly identified outcomes drive the budget process. The resultant decisions are then presented to parliament for approval in the form of appropriation Bills.

At present, the purpose of appropriations is for parliament to authorise the payment of funds from consolidated revenue to departments to use for particular purposes in the following year. This practice dates from well before the establishment of responsible government in Victoria. It originated when government had fewer departments, and was responsible for fewer services and activities. For several decades these practices have been augmented in Westminster jurisdictions around the world, through such means as forward estimates budgeting and global output appropriations. The review is considering whether they can be further built on, in a formal legislative arrangement, without diminishing traditional parliamentary oversight of the performance of executive government.

Appropriations could be authorised at the outcomes level in a number of ways. One option might involve parliament authorising specific dollar amounts against each desired outcome. It would then be the responsibility of the Treasurer, on behalf of the government, to purchase the outputs necessary to achieve the outcomes. Another form might involve parliament authorising the draw down of funds to the level deemed necessary for the government to achieve its desired outcomes.

Under both options, departments would continue to report output performance in the budget papers, with an additional requirement to report on their performance against strategic goals, that is, their contribution to the government's desired outcomes. Appropriating at the outcomes level would provide greater transparency to parliament and the public about the resources allocated in the pursuit of those outcomes.

While the appropriations are currently presented to parliament on an annual basis, a move to a multi-year approach could be considered. This would be based on the existing budget and forward estimates (three years) process. Multi-year appropriations would provide a legal basis for multi-year spending or investment, especially for those items that require a longer term planning horizon. Such changes would ideally be supported by enhanced reporting on the achievement of strategic objectives.

In any new framework, an important consideration would be how much flexibility the executive government should have to adjust the application of funds to address unforeseen circumstances.

Depending on the extent of change pursued for appropriations, consequential changes to the Administrative Arrangements Act are likely to be required.

Given the discussion above, you may wish to respond to the following questions.

Does the current Victorian parliamentary appropriation system serve any continuing purpose?

Should appropriations authorise:

- **payments from the consolidated fund at the departmental / output level**
- **payments from the consolidated fund against each outcome**
- **drawing down of the consolidated fund to the level deemed necessary to achieve the government's desired outcomes?**

Should appropriations be annual or multi-year, or a mix of both?

3.1.3 Accountability

A stronger strategic planning framework, particularly one that includes outcomes, provides an opportunity to strengthen accountability mechanisms, particularly those that link outputs and outcomes. Clear plans with clearly defined goals and measures would allow parliament and the public to more meaningfully assess executive government performance.

In recent times, parliament has granted additional flexibility to the executive government in return for greater reporting. It is expected that this trade-off will continue. If a more flexible approach to resource allocation is adopted (through appropriations to outcomes or multi-year appropriations), an increase in accountability would be required.

Improving performance (non-financial) reporting

Parliament has an important role in ensuring that government uses public resources effectively and efficiently. Meaningful performance information should tell parliament and the public what government is planning to do and what it has achieved.

It is important that a performance management framework be based on robust performance measures and monitoring processes, and clear accountability, whether at the input, output or outcome level. The new legislation should define the level and type of performance information that is required, and should ensure that performance information remains relevant over time and open to scrutiny.

The current government produces progress reports on its outcomes plan (*Growing Victoria Together*) in addition to the budget papers. However, this outcomes-focused reporting is not mandated by legislation. An option would be to legislatively mandate government outcome performance measurement and reporting. This would ensure that all future governments take a similar approach.

It will also be important to ensure strong links between outputs and outcomes at the departmental and entity level, and associated accountability. Existing mechanisms such as annual reports and budget papers could be used to convey the performance information to parliament. Any new mechanisms would need to complement these existing requirements.

A common criticism of government performance reporting is the difficulty in assessing progress from year to year when targets are regularly revised. As outcomes are generally achieved over a longer time frame, they are less likely to change from year to year compared with outputs.

A comprehensive reporting framework should balance financial and non-financial, and prospective and retrospective information across inputs, outputs and outcomes. The framework should recognise the trade-off between the benefits derived from reporting and the costs associated with producing these reports.

A further benefit of an enhanced planning and accountability framework is that it will enable a more systematic evaluation of programs and services across government.

Given the discussion above, you may wish to respond to the following questions.

Should a requirement to report progress against strategic plans be legislated?

Question: If so, should reporting of progress against strategic plans be at the level of:

- **whole-of-government**
- **departments**
- **entities?**

What accountability arrangements should be established for performance at input, output and outcome levels?

In terms of reporting, what do you consider to be the appropriate balance between:

- **financial and non-financial information**
- **prospective and retrospective information?**

3.2 Modernisation and simplification

3.2.1 Entities

Victoria has a large number of entities that range in size and complexity from small committees of management through to large public financial corporations. The government's ability to manage and monitor the operations of such a large number of entities is hampered by legislative inconsistency. The definition of public entities varies across Victorian Acts as do the different requirements prescribed under these Acts.

Currently, the level of government involvement in an entity (which is managed largely through departments) varies greatly and is determined by a number of factors. These encompass considerations such as whether the entity is established under statute, whether the government plays a role in appointing board members, or the entity's size and complexity.

At times, these entities transact with the private sector for the delivery of goods and services. However, the public sector's interest in these instances is limited to contractual arrangements with the private sector, which are reflected in the accounts of the public sector entities.

The definition of public entities for the purpose of public financial management should be clear and where appropriate, consistent with definitions used for other government purposes. Given the thorough and systematic approach used by the Public Administration Act, a strong case could be argued for the new legislation to align with the definitions in the Public Administration Act (reproduced in Appendix A of this paper).

In terms of reporting at the entity level, a one-size-fits-most approach is currently applied regardless of the size, risk or importance of the entity with most entities reporting on the same basis. This may not be appropriate. A more suitable approach could see entities producing reports with different amounts and levels of detail according to principles-based criteria outlined in the Bill. These principles would require some entities to report to parliament, but would allow other entities to report directly to their portfolio minister instead. Such a differential reporting framework could be based on various factors such as materiality, financial position, historical issues, public interest, control, administrative burden, and class of entity. This approach would be similar to the Australian Accounting Standards Board's distinction between general purpose reporting and special purpose reporting.

Given the discussion above, you may wish to respond to the following questions.

To which entities should the Public Finance Bill apply?

Should all elements of the Bill apply equally to all entities (for example, financial management, governance, reporting, procurement, compliance frameworks)?

If a differential framework were to be adopted, what form would it take and what criteria would it take into account (for example, financial position, materiality, public interest)?

3.2.2 Accrual-based appropriations and flexibility

Victoria has an accrual-based budgeting and appropriation framework. Within that framework, there are some residual cash elements, such as the warrant process (set out in section 1) and the cash-based nature of special appropriations. Given the adequacy of controls in the state's accrual accounting environment, it is now questionable whether these cash-based features remain appropriate.

There are also some highly detailed and prescriptive legislative provisions which should be reviewed. These provisions impose constraints on executive government while delivering very little additional information or control of executive government to parliament. Examples of these provisions include restrictions on shifting or augmenting appropriations.

Given the discussion above, you may wish to respond to the following questions.

What features of the cash-based system need to be retained?

What other technical provisions are no longer required?

3.2.3 Reporting

Public financial reporting provides important information to both executive government, which makes decisions about resource allocation, and parliament, which holds the executive accountable for those decisions. Under the current framework, the government provides numerous and frequent reports to parliament, both retrospectively and prospectively. The current framework focuses more on retrospective reporting. Examples of retrospective reporting include quarterly financial reports, the Mid-year Financial Report and Annual Financial Report, while the prospective reporting includes the Budget and Budget Update.

Frequency of financial reporting

There is questionable value in producing so many retrospective reports. For example, the quarterly financial reports do not substantially add to parliament's knowledge about the state's finances. One option for consideration would be to discontinue the publication of full financial reports for the September and March quarters. In their place, relevant information regarding performance in those quarters could be explicitly reflected in the latest estimates for the end-of-year outcome. The effects of the September quarter information could be explicitly stated in the Budget Update and the effects of the March quarter could be explicitly stated in the state Budget.

Longer term reporting

Another option for consideration is the production of longer term reports. This would be consistent with an outcomes-focused approach as outcomes are generally achieved over a longer time frame.

Prospective reporting in Victoria currently involves the publication of financial estimates over a four-year period while performance information is only provided for one year. These time frames could be aligned by matching the performance information reporting period to the financial estimates four-year period. This would provide greater transparency and accountability in performance management.

Historical trend data would enable government, citizens and parliament to better assess output delivery and outcomes performance.

In its 2008–09 Budget, the Commonwealth Government included fiscal projections for the underlying cash balance going forward twenty years as part of its medium-term fiscal outlook. It did this to allow the public to understand more clearly its fiscal policy and overall financial performance.

The United Kingdom, United States of America and New Zealand also prepare similar long-term reports on public finances. The time horizon covered in some of these reports extends up to seventy-five years.

Further, the International Public Sector Accounting Standards Board has recently commenced a project to produce a framework for the reporting and disclosure of information related to the long-term fiscal sustainability of government programs.

A financial management framework that includes long-term strategic plans and long-term fiscal reports would enable parliament and the public to assess the fiscal environment in which the government's longer-term objectives are set.

Timeliness of departmental and entity annual reports

A further issue for consideration is the timeliness of annual reports produced by departments and entities. In Victoria, the legislation requires annual reports to be tabled in the Parliament four months after the year end, which is longer than in some other jurisdictions and in standard business practice. Currently, the Australian Securities and Investments Commission requires disclosing entities to report within three months of the end of a financial year. In Western Australia, reporting entities are required to report within ninety days of the end of the financial year, or sooner, as prescribed.

A move to shorter reporting time frames in Victoria would result in more timely and up-to-date disclosure of information. This will enhance citizen engagement and the transparency and accountability of the reporting process.

Consolidated reporting

Another option to consider is to replace individual entity reporting with reporting at a higher level and in a more consolidated manner. This could be similar in manner to how private companies provide a consolidated report of their subsidiaries. In considering such an option, it is important to assess the value of individual entity reports and whether they provide parliament with meaningful information that would not be provided in a more consolidated report.

Any move to consolidated reporting would have to take into account accountability requirements, such as those associated with Commonwealth funding grants.

Improving accessibility

Many of the reports produced by government are quite technical in nature. Often this is because they must meet technical requirements such as accounting standards, but it means that they require a degree of specialist knowledge to be fully understood. A number of other jurisdictions (e.g. Canada and the United States of America) produce concise and targeted reports to reach specific audiences, including citizens' reports which act as a guide to the technical reports.⁵

One approach to improved performance reporting is to have a high level report card that includes a set of holistic key performance indicators that make clear what the government considers will create public value.

The private sector is increasingly utilising modern communication methods to engage stakeholders and the general public, and to improve access to reports. Examples include emails and the internet and short-form annual reports, which provide high-level summary information. This approach could be adopted for reporting at the whole-of-government, and department and entity level.

Given the discussion above, you may wish to respond to the following question.

What options for modernising and simplifying reporting should be considered?

3.2.4 Other public finance legislation

This review provides an opportunity to consolidate related Acts into one overarching framework for all government financial legislation. This would supplement the foundation Constitution Act. The following proposals could be considered:

- transfer the *Borrowing and Investment Powers Act 1987* and *Monetary Units Act 2004* into the new Public Finance Bill
- repeal the *Public Authorities (Dividends) Act 1983*
- transfer existing property and land functions to another Act.

More detail about these proposals is set out below.

As already mentioned, the new Bill may also require consequential changes to the *Administrative Arrangements Act 1983*.

Borrowing and Investment Powers Act 1987

The *Borrowing and Investment Powers Act 1987* was introduced shortly after the financial deregulation of the 1980s. It provides certain entities with access to financial instruments for the effective management of their exposure to financial risk, and centralises financial expertise for the state. Specifically, it provides powers to certain entities to borrow and invest state funds and sets out the processes and accountability mechanisms.

Generally, other Australian jurisdictions do not have separate legislation for borrowing and investment powers. These powers are usually part of the public financial management legislation or legislation governing entities. However, in Victoria the Borrowing and Investment Powers Act preceded the enactment of the Financial Management Act and the separation of these two Acts has continued.

One possible course of action is to repeal the Borrowing and Investment Powers Act and the borrowing and investment powers from all other legislation. The underlying principles of these Acts could be incorporated into the Public Finance Bill. This would create a more consistent and comprehensive financial management framework for Victoria.

The government is considering options to improve its monitoring and control over a wider range of entities than those currently included in the Borrowing and Investment Powers Act. This may require entities to invest centrally, enabling greater efficiencies and more effective monitoring and reporting of exposures. Entities would still retain autonomy to adopt the strategy appropriate to their business situation. The Public Finance Bill provides the opportunity to develop the legislative framework to support greater centralisation.

Monetary Units Act 2004

The *Monetary Units Act 2004* was enacted to enable certain government fees and penalties (listed under Schedule 1 of the Act) to be indexed more consistently. The Act dictates the conversion of these fees and penalties from monetary amounts to fee and penalty units. These units are indexed annually by the annual rate set down by the Treasurer. The annual rate has been relatively consistent with the consumer price index since 2004.

As the legislation is concerned only with one aspect of public finance, it could be included in the new public finance legislation. This would not reduce the level of transparency applied to the current policy and process.

Public Authorities (Dividends) Act 1983

The *Public Authorities (Dividends) Act 1983* was introduced to authorise the government to obtain annual dividends from certain entities and to subject them to the same expectations and discipline as private sector entities. Dividends from entities make a notable contribution to the consolidated fund (estimated to be \$421 million in 2008–09).

The Public Authorities (Dividends) Act has limited application today. Since its introduction, many of the entities to which it applied have ceased to exist. Contemporary practice is to insert dividend clauses into establishing legislation and industry Acts. The Public Authorities (Dividends) Act now only applies to three corporations, of which two already have dividend provisions in other Acts. Further, the formula for calculating dividends prescribed in this Act is no longer in use and has been superseded by the benchmarks set out in financial reporting direction 3A.

Consequently an option to consider is the repeal of the current Public Authorities (Dividends) Act and all dividend clauses in other legislation. These could be replaced with a high-level provision in the new Public Finance Bill enabling the Treasurer to impose a dividends policy framework. This option would not reduce the level of transparency applied to the current dividends policy and process.

Land and property functions

The Financial Management Act empowers the Minister for Finance to acquire land, lease land or premises for the purposes of other ministers or departments, and license and lease surplus Crown land and buildings. It also authorises the minister, on behalf of the Crown, to distribute any unclaimed property, whether real (i.e. land) or personal (i.e. chattels or legal rights), where the Crown is entitled to such property.

However, at present, a number of other ministers are empowered by Acts other than the Financial Management Act to make some specified decisions in relation to Crown land and premises. Where those powers are not specified, these other ministers rely on the Minister for Finance to acquire land, and lease land and premises on their behalf.

The land and premises provisions of the Financial Management Act were originally set out in the *Public Lands and Works Act 1964* and administered by the then Minister for Works and Services. The departments of public works and property services were abolished and the Act was repealed, in 1994. Powers over land and premises were not at that time perceived to be an integral part of a financial management framework, and so were not fully consolidated either into the Minister for Finance's responsibility or the Financial Management Act. Consequently, provisions relating to land and premises are still set out in a number of other Acts, including the *Land Act 1958*, the *Transfer of Land Act 1958* and the *Property Law Act 1958*. Victoria is the only state that has land and premises powers set out in public finance legislation. Due to the dispersal of these powers in several different Acts, it is also the only state with land and premises powers administered by several ministers. In light of the government's desire to consolidate and simplify current Victorian legislation, these powers could be considered in a comprehensive review of land and premises-related law. The government has recently announced it will review the Transfer of Land Act and the Property Law Act.

Consideration will need to be given to how to treat the existing Financial Management Act provisions while the comprehensive review is undertaken.

Given the discussion above, you may wish to respond to the following question.

Are the proposals for related legislation appropriate?

3.2.5 Procurement

The past decade has seen significant changes for procurement in Victoria. In developing a modern public finance system, it is necessary to consider:

- whether procurement principles should be included in the new legislation
- which key players should perform each of the functions
- to which entities should procurement policy apply.

Department of Treasury & Finance

Procurement principles

If principles-based legislation is adopted for the Public Finance Bill, the Bill could enshrine the procurement principles from the current ministerial directions:

- value for money
- open and fair competition
- accountability
- risk management
- probity and transparency.

Procurement governance framework

A new framework for government financial management would provide the opportunity to establish clear lines of accountability and responsibility for procurement. This could be done by having the legislation clearly reflect the current roles and responsibilities of the Minister for Finance, the Department of Treasury and Finance and the VGPB.

The policy-making function of the VGPB could be undertaken by a minister or by the Governor in Council. There are already precedents in the area of procurement. For example, policies and procedures specifically addressing capital expenditure and travel are set out in ministerial directions. In practice, the procurement function would become self-regulating. In other words, rather than investing in monitoring compliance, compliance should become clear through the operation of the system, that is, through the audit function and avenues for pursuing complaints.

For the policy breach handling function, complaints could be registered with the Minister for Finance and a panel of on-call, independent, qualified review officers, who would convene to review complaints when required.

Scope of the procurement framework

The scope of the VGPB and its policies only relates to the purchase of goods and services in departments and administrative offices. The board's area of responsibility does not extend to purchasing activities that relate to capital projects, which represents a significant portion of whole-of-government expenditure. Neither is the board responsible for oversight of purchasing undertaken by other entities (mainly public non-financial corporations and public financial corporations). At present, these other entities are advised, but not required, to use the VGPB guidance as best practice.

Given the discussion above, you may wish to respond to the following questions.

Should procurement principles be incorporated into the new Public Finance Bill?

What functions associated with procurement need to remain entrusted to a statutory body or be independent of government?

Is the scope and nature of procurement controls sufficient?

3.2.6 Principles-based legislation

The new legislation should be modern, easy to read and comprehensive in scope. This section considers a principles-based approach as a means of improving and modernising the current legislative framework.

Public finance legislation has two dimensions. In some matters it contains the compact between parliament and government about the relationship of the two institutions. In other matters it gives legal effect to the rules required for the governance of the public sector. In fact, the changes made by the *Financial Management (Miscellaneous Amendments) Act 2006* have already given the Minister for Finance considerable additional powers to set rules relating to public sector financial governance.

Principles-based legislation states in primary legislation the fundamental principles of the law, leaving other processes and detailed rules to subordinate legislation. Principles-based legislation focuses on assuring desired outcomes more than on procedural details or technicalities. Its purpose is to create a legal requirement (or opportunity) that something be done, not to establish how it is to be done. For example, a board may be required to have a policy about probity in receiving gifts, but remain free to tailor the policy to its own circumstances.

There are two important reasons to consider principles-based legislation in a context of public finance legislation. First, by focusing on the desired outcome (for example, promptness and adequacy of services) the legislation demands compliance with the outcome rather than the set of procedural rules needed to achieve it. Second, legislation that establishes clear principles, rather than prescribing detailed practices for giving effect to those principles, remains relevant in the face of operational evolution. This is especially so in relation to rules internal to the public sector, which is why the Financial Management Act (section 8) gives direction-making powers to the Minister for Finance.

As already noted, the powers of the Minister for Finance are to a considerable degree already principles-based. This is due to the interaction of the regulation-making power in section 59, and the direction-setting power in section 8. Beyond that, it is generally true that the objective of legislation often outlasts the particular mechanism enacted to achieve that objective.

The Public Administration Act also provides examples of principles-based legislation in Victoria. The Act established a framework for good governance in the Victorian public sector and in public administration generally in Victoria. A particular example is section 81 of the Act (reproduced in Appendix B of this paper), which sets out governance arrangements for public entities.⁶

Victoria's Financial Management Act is highly detailed, prescriptive and complex. Legislation in the area of public finance lends itself to a principles-based approach because it is essentially internal to the business of government. In only the rarest of instances does it affect the rights or obligations of individuals or invite consideration by the courts.

There has been a shift in recent times towards principles-based public finance legislation in other jurisdictions. Overseas examples include Sweden's *State Budget Act 1996*. In Australia, the Western Australian Government has recently introduced revised financial management legislation, which includes more streamlined provisions and devolved operational provisions. Queensland and Tasmania are currently reviewing their respective financial legislation and have indicated that they intend to develop principles-based legislation.

Department of Treasury & Finance

Principles-based legislation does not compromise or diminish the accountabilities and responsibilities set by a financial management framework. In addition, parliamentary scrutiny of the particular means by which the principles are carried into practice, and of the practices themselves, remains intact. However, an expansion of the principles-based approach could initially present difficulties for some key participants. Policy authors, for example, have previously relied on the legislation to mandate specific and detailed policies and compliance activities.

If a principles-based approach is adopted, the legislative framework in its entirety (including, for example, the financial reporting directions) should be readily available to the public, to ensure an appropriate level of transparency is maintained.

Given the discussion above, you may wish to respond to the following question.

Should the Public Finance Bill be drafted as principles-based legislation?

4. Next steps

4.1 Responding to this discussion paper

This discussion paper outlines the issues that the government considers important in developing a new Public Finance Bill. It suggests a range of potential options and raises a number of questions for comment.

We invite you to respond with your thoughts. Your comments are valuable to the construction of the state's future public finance framework and will help Victoria maintain its reputation as a leader in public financial management.

Submissions to this review are welcome and can be forwarded, in writing, to:

Public Finance Bill Project Team
Department of Treasury and Finance
Level 9, 1 Macarthur St
MELBOURNE VIC 3002

Submissions can also be emailed to: publicfinancebill@dtf.vic.gov.au

Written submissions should ideally be kept to no more than 20 pages. Individuals and organisations should indicate if they wish their submissions to be treated confidentially. Please note that freedom of information access requirements will apply to all submissions, even those treated as confidential.

Submissions are invited on the discussion paper until Friday 5 December 2008.

For a copy of the discussion paper and advice about the submission process visit www.dtf.vic.gov.au, email publicfinancebill@dtf.vic.gov.au or phone (03) 9651 5106. The discussion paper is available in an accessible format, such as large print or audio, on request.

For further information regarding this review, please contact:

Dean Yates, Deputy Secretary – Financial Reform, ph: (03) 9651 5369

Toni McGrath, Project Director – Public Finance Bill Project, ph: (03) 9651 5488

Your feedback on this discussion paper will contribute to the development of a new Public Finance Bill to be introduced in 2009.

4.2 Public Accounts and Estimates Committee Inquiry

In early 2008, the PAEC commenced its own inquiry into Victoria's public finance practices and legislation. The committee expects to present the findings of its investigations to parliament by the end of 2008. The government intends to consider the recommendations from the PAEC inquiry as part of its review and incorporate them, as appropriate, into the new Bill.

Appendix A: Extract from *Public Administration Act 2004*, Part 1, s. 5

PART 1—PRELIMINARY

5 What are public entities?

- (1) For the purposes of this Act a public entity is a body, whether corporate or unincorporated—
- (a) that is established—
 - (i) by or under an Act (other than a private Act) or the Corporations Act; or
 - (ii) by the Governor in Council; or
 - (iii) by a Minister; and
 - (b) in the case of a body corporate, the right to appoint at least one half of the directors of which is vested in the Governor in Council or a Minister or could have been so vested in the case of a body corporate established by an Order made by the Governor in Council or a Minister under the power given by the Act under which the Order is made; and
 - (c) that has a public function to exercise on behalf of the State or is wholly owned by the State; and
 - (d) in the case of a body that does not have any function to exercise other than the provision of advice or a report to any person or body—
 - (i) has written terms of reference guiding its operation; and
 - (ii) is required to provide the advice or report to a Minister or the Government; and
 - (iii) is declared to be a public entity for the purposes of this Act—
 - (A) by the Act or subordinate instrument or other document under which it is established; or
 - (B) by an Order under subsection (3)—
- but does not include—
- (da) a Department or an Administrative Office; or
 - (e) an exempt body; or
 - (f) a special body in its capacity as a special body; or
 - (g) a community health centre within the meaning of the Health Services Act 1988 or a body that provides aged care services that is, or is capable of being, registered under that Act; or
 - (h) a body, or a class of body, that is declared by an Order under subsection (2) not to be a public entity for the purposes of this Act.
- (1A) To avoid doubt and without limiting subsection (1), the following are public entities for the purposes of this Act—
- (a) the board of a TAFE institute within the meaning of the *Education and Training Reform Act 2006* (other than the TAFE division of a university);
 - (b) the Board of AMES and the Board of the Centre for Adult Education, within the meaning of the *Education and Training Reform Act 2006*.

- (2) The Governor in Council may, by Order published in the Government Gazette, declare a body, or a class of body, not to be a public entity for the purposes of this Act.
- (3) The Governor in Council may, by Order published in the Government Gazette, declare a body, or a class of body, that does not have any function to exercise other than the provision of advice or a report to any person or body and that satisfies the requirements of subsection (1)(d)(i) and (ii) to be a public entity for the purposes of this Act.
- (4) If an exempt body is a public entity for the purposes of this Act in a capacity other than its capacity as an exempt body, nothing in this Act that applies to the body as a public entity applies to the body in its capacity as an exempt body.

Example

A municipal council is appointed as a committee of management under section 14(2) of the *Crown Land (Reserves) Act 1978*. As a committee of management the municipal council is a public entity as it is established under an Act with a public function to exercise on behalf of the State. It is not, however, a public entity in its ordinary role as a municipal council because, in that role, it is an exempt body and exempt bodies are not public entities.

- (5) If—
 - (a) a provision of an Act other than this Act has the effect that a body (an advisory body) or a member of an advisory body or of the governing body (by whatever name called) of an advisory body is not subject to this Act—
 - (i) other than Part 5; or
 - (ii) other than Part 5 or except in accordance with Part 7; and
 - (b) the advisory body does not have any function to exercise other than the provision of advice or a report to any person or body—
- despite the provision of that other Act, the advisory body is not a public entity for the purposes of this Act unless the requirements of subparagraphs (i), (ii) and (iii) of subsection (1)(d) are satisfied in respect of it.
- (6) If a provision of an Act other than this Act has the effect that a body (a relevant body) or a member of a relevant body or of the governing body (by whatever name called) of a relevant body is not subject to this Act—
 - (a) other than Part 5; or
 - (b) other than Part 5 or except in accordance with Part 7—

despite the provision of that other Act, the relevant body may be declared by an Order under subsection (2) not to be a public entity for the purposes of this Act.

Appendix B: Extract from *Public Administration Act 2004*, Part 5, s. 81

Note that this section of the Act only applies to public entities established on or after the commencement of Part 5, unless applied by Order in Council to existing entities. The Act also allows for exemption, (s. 75 of the Public Administration Act).

PART 5—OPERATION OF PUBLIC ENTITIES

81 Duties of entity

- (1) The board of a public entity must—
 - (a) act consistently with the functions and objectives of the entity and with any business or strategic plan or other document relevant to the work program of the entity; and
 - (b) inform the Minister responsible for the public entity and the relevant Department Head of known major risks to the effective operation of the entity and of the risk management systems that it has in place to address those risks; and
 - (c) unless prohibited from doing so by or under any law, provide the Minister responsible for the public entity with any information relating to the entity or its operations that he or she requests; and
 - (d) except in the case of a Commissioner entity, ensure that adequate procedures are in place for—
 - (i) assessing the performance of individual directors; and
 - (ii) dealing with poor performance by directors; and
 - (iii) resolving disputes between directors; and
 - (e) ensure that a code of conduct applicable to directors is in place; and
 - (f) ensure that processes are in place to deal with conflicts of interests in directors that—
 - (i) apply to both financial and non-financial interests;
 - (ii) require full disclosure of interests at meetings of the board and the recording of the disclosure in the minutes of the meeting;
 - (iii) require the board to determine whether a conflict of interest in a matter is material;
 - (iv) enable the board to—
 - A. require the absence from a meeting of a director who has a material conflict of interest in a matter while the board is considering the matter;

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- B. prohibit such a director from taking part in any decision of the board in relation to the matter;
 - (v) require the board to notify in writing the Minister responsible for the entity as soon as practicable after becoming aware of any breach of the processes; and
 - (g) ensure that an adequate gifts policy for directors is in place; and
 - (h) except in the case of a Commissioner entity or as otherwise provided by an Order made under subsection (3) in the case of an advisory entity, ensure that adequate procedures are in place for the conduct of meetings and the making of decisions at meetings, including appropriate arrangements for acting directors, and that appropriate records of meetings are kept; and
 - (i) except in the case of an entity that has no money or other property under its management or control or as otherwise provided by an Order made under subsection (3) in the case of an advisory entity, ensure that appropriate financial records are kept; and
 - (j) ensure that adequate controls are in place to prevent fraudulent behaviour; and
 - (k) except in the case of an advisory entity, a small entity or an entity that is otherwise required to have its financial statements or accounts audited by the Auditor-General, ensure that its financial statements or accounts are audited by the Auditor-General at intervals of no greater than 3 years.
- (2) A public entity may satisfy a requirement under subsection (1) to have a particular code or policy in place by applying, with appropriate adaptations, a code or policy of another public sector body consistent with the public sector values.
- (3) The Governor in Council may, by Order published in the Government Gazette, make provision in relation to an advisory entity, or a class of advisory entity, in substitution for that made by paragraph (h) or (i) of subsection (1).

List of shortened forms

COAG	Council of Australian Governments
GVT	<i>Growing Victoria Together</i>
IMC	Integrated Management Cycle
OECD	Organisation for Economic Co-operation and Development
PAEC	Public Accounts and Estimates Committee
SPPs	Specific purpose payments
VGPB	Victorian Government Purchasing Board

Glossary of terms

Accountable officer	The accountable officer for a department is normally the head of that department. The accountable officer for a public body is normally the chief executive officer of that body.
Accountability	The state of being accountable, liable, or answerable.
Accrual accounting	Recognition of revenue, expenses, assets, liabilities and equity when the economic transaction occurs, irrespective of the timing of the related cash flow. For example, revenue from sale of goods is recorded as of the invoice date rather than the date on which payment is received.
Administrative office	A body or group established under s. 11 of the Public Administration Act.
Annual appropriation	The limit of resources the Treasurer applies as (i) revenue to a department for provision of outputs, (ii) contributions to a department for additions to its asset base, and (iii) funding for payments made on behalf of the state. It is contained in the Appropriation Act and the Appropriation (Parliament) Act.
Australian Accounting Standards Board (AASB)	The Australian Accounting Standards Board (AASB) is an independent accounting standard-setter based in Melbourne. The AASB is committed to developing, in the public interest, a single set of high quality, understandable accounting standards that require transparent and comparable information in general purpose financial statements.
Bill	A proposed law (or statute, or piece of legislation) that is introduced into parliament but has not yet been passed. If passed and granted Royal Assent, it becomes an Act.
Budget estimates	The budget estimates are the amounts of money which executive government estimates the government will need to expend to meet its commitments.
Budget and financial management guidances	Budget and financial management guidances provide detailed guidance on the elements of the existing budget and financial management policy framework, and how it is to be applied. Budget and financial management guidances typically provide guidance on how to comply with relevant sections of the Financial Management Act, manage accrual output budget management issues or how to apply relevant Australian equivalents to International Financial Reporting Standards.
Consolidated fund	The government's primary account that receives all revenue raised by and granted to the state, and from which amounts are appropriated by parliament for specific purposes. The consolidated fund, together with the trust fund, forms the public account. All payments from it must be authorised by parliament.

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Consolidated revenue	<p>Parliament appropriates funds to departments out of consolidated revenue via appropriations Acts to fund:</p> <ul style="list-style-type: none">- the delivery of outputs- additions to the net asset base- other administrative activities.
Council of Australian Governments (COAG)	<p>The Council of Australian Governments (COAG) is the peak inter-governmental forum in Australia. COAG comprises the Prime Minister, state Premiers, territory Chief Ministers and the president of the Australian Local Government Association. The role of COAG is to initiate, develop and monitor the implementation of policy reforms that are of national significance and which require cooperative action by Australian governments (for example, national competition policy, water reform).</p>
Department and administrative heads	<p>Defined under section 4(1) of the Public Administration Act as a person employed as the head of either a department or administrative office.</p>
Executive government	<p>Victoria's executive government consists of the Governor, Premier, and the state's ministers.</p>
Estimated financial statements	<p>Estimated financial statements forecast financial results for the Victorian general government sector for the next three years. The prospective nature of these statements reflects a number of judgements about the most likely operating and financial conditions for the Victorian general government sector.</p>
Forward estimates	<p>Forward estimates represent planning projections for the forecast period (three years) based on unchanged policy and other assumptions.</p>
General government sector	<p>The general government sector comprises all government departments, offices and other bodies engaged in providing services free of charge or at prices significantly below their cost of production. General government services include those which are mainly non-market in nature, those which are largely for collective consumption by the community, and those which involve the transfer or redistribution of income.</p>
General purpose reporting	<p>Reports prepared for external users who do not have the ability to require or contract for the preparation of special reports to meet their specific information needs.</p>
Global appropriations	<p>Outlined in Schedule 1 of each annual Appropriation Act, global appropriations incorporate the provision of outputs and additions to the department's net asset base, to be used for the purchase of assets supporting the delivery of outputs, and payments on behalf of the state.</p>
Governor in Council	<p>Powers exercised by the Governor at the Executive Council meeting, on the advice of the Executive Council, which consists of the ministers of the state.</p>
Government Gazette (Victoria)	<p>The <i>Victoria Government Gazette</i> provides official notification of decisions or actions taken by, or information from, the Governor of Victoria, government authorities, government departments, local councils, companies and individuals.</p>

Growing Victoria Together (GVT)	<i>Growing Victoria Together (GVT)</i> is a ten-year vision that articulates what is important to Victorians and the priorities the government has set to build a better society. It is based on careful discussion and consultation with many groups in the community.
Inputs	Labour, materials and other resources used to produce outputs.
Integrated Management Cycle (IMC)	The Integrated Management Cycle (IMC) identifies the major planning, resource allocation, and accountability milestones through the year, and outlines the process requirements and the relationships between various activities. The IMC is designed to be used as a tool to improve planning processes and capability in departments. The IMC comprises a calendar and guide.
International Public Sector Accounting Standards Board (IPSASB)	The International Public Sector Accounting Standards Board (IPSASB) focuses on the accounting and financial reporting needs of national, regional and local governments, related governmental entities, and the constituencies they serve. It addresses these needs by issuing and promoting benchmark guidance and facilitating the exchange of information among accountants and those who work in the public sector or rely on its work.
Investment Lifecycle Guidance material	These guidelines are to be applied to each investment of the Victorian Government so they provide the maximum benefit for the citizens and businesses of Victoria. They provide practical assistance to shape investment proposals, inform investment decisions, monitor delivery of investments and track the ultimate attainment of benefits.
Legislation	Laws enacted by a legislature or parliament.
Machinery of government	The expression 'machinery of government' has long been used to refer to the allocation and reallocation of functions between departments and ministers. In Victoria, machinery of government matters are the sole responsibility of the Premier.
Minister	A member of the government responsible for one or more portfolios or government departments; he or she is also a member of Cabinet.
Ministerial directions	In the case of this discussion paper, ministerial directions support the Financial Management Act. They specify matters with which government departments and public bodies must comply to implement and maintain appropriate financial management practices. In so doing they achieve a consistent standard of accountability and financial reporting. The directions specify high-level requirements for financial management. This allows government departments and public bodies to develop specific systems, procedures and compliance practices.
Multi-year appropriations	Multi-year appropriations make amounts available for a particular purpose over more than one financial year.
Non-government organisation	An organisation that is neither owned nor controlled by government.
Outcomes (government)	Outcomes refer to the government's desired or intended impacts/effects on the community.
Outputs	Outputs are goods or services produced or delivered by, or on behalf of, a department or entity.

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Parliament	The Parliament of Victoria consists of the Queen, the Legislative Assembly, and the Legislative Council; also used to refer to the two houses.
Program budgeting	Program budgeting sets programs as the basis for budget appropriations.
Public account	The government's official bank account, maintained at one or more banks as required by the Financial Management Act. It holds the balances of the consolidated fund and the trust fund.
Public non-financial corporations	The public non-financial corporations sector comprises bodies mainly engaged in the production of goods and services (of a non-financial nature) for sale in the market place at prices that aim to recover most of the costs involved (e.g. water and port authorities).
Public financial corporations	Public financial corporations are bodies primarily engaged in the provision of financial intermediation services or auxiliary financial services.
Public service bodies	Defined under s. 4(1) of the Public Administration Act to mean a department; administrative office; or the State Services Authority.
Public value	Public value is what the public values in terms of public services and efficiency.
Service delivery	In Victoria, service delivery relates to the production or delivery of outputs by, or on behalf of, a department and its entities to achieve government's desired outcomes. Output performance measures relating to quantity, quality, timeliness and cost are used to assess each department's performance in service delivery.
Special bodies	Those bodies prescribed under s. 6(1) of the Public Administration Act, and any body declared by the Governor in Council, under s. 6(2) of the Act, to be a special body for the purpose of the Act.
Special purpose reporting	Reports tailored to meet the specific information needs of a particular user.
Specific Purpose Payments (SPPs)	Grants made by the Commonwealth to state and territory governments subject to terms and conditions laid down by the Commonwealth, generally with a view to ensuring that Commonwealth policy objectives (or national objectives agreed between the Commonwealth and the states) are met.
State Services Authority (SSA)	The State Services Authority (SSA) is responsible for fostering the development of an efficient, integrated and responsive public sector which is highly ethical, accountable and professional in the ways it delivers services to the Victorian community.
Subordinate legislation	Regulations or similar rules made under the authority of an Act.
Tax	A sum of money demanded by a government for its support or for specific facilities or services, levied upon incomes, property, sales, et cetera.

Treasury management guidelines	The Treasury management guidelines set a framework to guide government business enterprises in the development and management of their treasury function.
Trust fund	Trust fund comprises a series of separate trust accounts which contain money held for a specific purpose(s), each generally but not necessarily administered by one department.
Uniform Presentation Framework	The primary objective of the Uniform Presentation Framework is to ensure that the Australian, state and territory governments present their financial statements on a standard, comparable basis. The format of the Uniform Presentation Framework is based on the reporting standards of the Australian Bureau of Statistics (ABS) Government Finance Statistics (GFS) framework.
Victorian Government Purchasing Board (VGPB)	The Victorian Government Purchasing Board (VGPB) was established under the Financial Management Act and replaced the State Tender Board from 1 February 1995. The VGPB meets bi-monthly to develop and approve policies, approve major requisitions from departments, and discuss related procurement policy and practice matters. Three of the VGPB members, including the Chairperson, are external appointees, and the remainder are appointed from government departments. VGPB reports to the Minister for Finance.
Warrant	A warrant is a written authority to spend specified sums during the financial year from the consolidated fund, the government's bank account. A warrant must be signed by the Treasurer, the Auditor-General and the Governor. Conceptually, a warrant is similar to approval to draw cheques on a bank account.
Westminster system	The system of government that exists in Great Britain and which has been copied, to a greater or lesser extent, by many Commonwealth countries; so called because it is named after the precinct of Westminster, where the House of Commons and the House of Lords meet.
Whole-of-government	Includes departments and entities.

Endnotes

- ¹ B Perrin, 'Moving from outputs to outcomes: practical advice from governments around the world', *Managing for Performance and Results Series*, January 2006, p. 6.
- ² Organisation for Economic Co-operation and Development, *Modernising government: the way forward*, OECD Publishing, Paris, 2005, p. 76.
- ³ MH Moore, *Creating public value: strategic management in government*, Harvard University Press, Cambridge, Massachusetts, 1995.
- ⁴ For the debate, see J Alford, 'The limits to traditional public administration, or rescuing public value from misrepresentation', *The Australian Journal of Public Administration*, vol. 67, no. 3, 2008, pp. 357-366.
- ⁵ See examples: *Popular Report 2005*, District of North Vancouver, viewed 16 October 2008, <http://www.dnv.org/popular_report/2006/main.html>; *The Federal Government's financial health: A citizen's guide to the 2007 financial report of the United States government*, United States Government, viewed on 16 October 2008, <http://www.whitehouse.gov/omb/financial/reports/citizens_guide.pdf>.
- ⁶ Note that this section of the Act only applies to public entities established on or after the commencement of Part 5, unless applied by Order in Council to existing entities. The Act also allows for exemption (s. 75 of the *Public Administration Act 2004*).

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