

Performance Budgeting in Australia

by
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This article describes how the principles of management for results have worked in practice over the past two decades in Australia. The current performance information framework involves, among other things, the accrual-based outcomes and outputs policy, performance agreements between heads of agencies and their responsible ministers, and regular review and assessment, particularly at agency level.

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1. Description of the performance system

Financial management in Australia has been shaped by the principles of “management for results” since the introduction of the Financial Management Improvement Program (FMIP) in 1983 as part of a wide-ranging public sector reform strategy (Parliament of the Commonwealth of Australia, 1990).

Financial management’s focus on results has evolved considerably over the two decades since the FMIP established rudimentary programme-based planning and reporting on cash movements. Today the information gathered includes comprehensive and detailed accrual-based reporting on plans and actual results for each outcome, output and administered activity in each department and agency across the general government sector.

The nature of performance information in Australia’s financial management framework may have changed, but the essential objectives remain very much the same: to improve both the cost-effectiveness of resource use and public accountability while devolving financial management responsibility and flexibility to those who deliver policies and programmes.

1.1. Background

Australia’s current arrangements arose from budgetary reforms associated with the *National Commission of Audit 1996*, an independent review commissioned by the then incoming Australian government (Commonwealth of Australia, 1996). That review considered aspects of the management and financial activities of the Australian government and how they were recorded. The commission’s main recommendations were that:

- government management skills and government finances operate on a more business-like footing;
- the transparency of government finances be further improved;
- the culture and operations of the Australian public service reflect a more businesslike approach.

Between 1996 and 1999, legislative and administrative changes were introduced that reflected the principles espoused by the National Commission of Audit:

- The Audit Act 1901 was replaced in 1997 by new financial legislation for government departments, agencies, authorities and companies. The

legislation comprised the Financial Management and Accountability Act 1997 (FMA Act) and the Commonwealth Authorities and Companies Act 1997 (CAC Act), as well as the Auditor-General Act 1997.

- Financial management moved to a principles-based framework, with clear lines of accountability.
- The Charter of Budget Honesty Act 1998 (the Charter) was introduced in response to a specific recommendation of the *National Commission of Audit 1996*. The Charter provides a framework for a more transparent conduct of fiscal policy. *Inter alia*, it requires:
 - ❖ governments to disclose their fiscal strategy and to base that strategy on principles of sound fiscal management. The principles are identified in the Charter;
 - ❖ reporting on the fiscal strategy at budget time (including a statement of risks), half-year, and end-of-year. Prior to an election, a fiscal outlook statement is also required;
 - ❖ specific guidelines governing the costing of election commitments by the government and the opposition, and release of the information.

Other key reforms were implemented in 1999/2000 in addition to the legislative changes. These included: the move to accrual budgeting (including accrual appropriations); an outcomes and outputs resource management and performance framework; and increased flexibility and responsibility for agency chief executives (also reflected in the Public Service Act 1999).

The financial management and public administration legislation that replaced the Audit Act 1901 eliminated detailed legislation, mandatory requirements and directives relating to authority and action on public funds. Those arrangements were replaced by more general provisions that give chief executives the authority to set their own internal operating procedures and delegations, subject to general principles of efficient, effective and ethical use of resources.

The new arrangements also established performance agreements between chief executives and their ministers. The agreements generally cover the key goals and objectives for the CEO and their agencies.

The reforms of the 1990s aimed to establish clear responsibility and accountability for financial and non-financial performance. They sought to hold agency heads responsible for performance. The requirements for central controls on comprehensive evaluation plans were relaxed; at the same time, greater emphasis was placed on the development of precise and measurable performance information.

Until 1996, agencies were required to submit formal portfolio evaluation plans each year, assessing all programmes within their area of responsibility over a five-year period. Experience with the variable quality of evaluations and their usefulness or lack thereof for decision making suggested that a more focused and balanced approach to evaluation and performance measurement might yield better overall results. In 1996, agencies were encouraged to use new evaluation and performance monitoring techniques in ways that contributed most to efficient, effective and ethical management. The Department of Finance and Administration ("Finance"), in co-operation with the Australian National Audit Office, released a set of good practice principles for performance information (ANAO and Department of Finance and Administration, 1996).

While there have been benefits from the reforms of the mid to late 1990s, the Australian government has recognised the need for regular review and assessment of the reforms. This was undertaken most recently in 2002, when the Australian government initiated the Budget Estimates and Framework Review. The review was primarily aimed at ensuring greater timeliness and accuracy of budget estimates information, including cash data, and ensuring that the public service was adequately equipped to deliver the improvements. The major themes of the review report were:

- a greater focus on programme information;
- more detailed and timely reporting of financial information;
- strengthened processes to monitor agency financial performance, cash flows and estimates construction;
- ensuring that systems are capable of capturing and recording increased information requirements;
- increasing the number of professional staff in Finance and line agencies with the necessary financial and analytical skills.

The recommendations of the review were accepted by the government in November 2002. This included confirmation of accrual budgeting and Finance's power to amend agency financial estimates to ensure that the quality and timeliness of the whole-of-government estimates meet the best achievable standard.

In retrospect, the accrual-based outcome and outputs policy changes initiated in 1999/2000 were a significant challenge for the government, parliament, the budget, management and technical staff of central and line agencies, and information technology systems. The full impact of those changes was not obvious to the planners or to those working within the system in the early years of operation. This highlights the importance of monitoring and refining reform initiatives, especially when they are complex, wide-ranging and ambitious.

1.2. Institutional framework

Australia operates within a three-tier federal structure. National, provincial and local governments are elected independently and have the autonomy to make decisions on matters within the scope of their responsibilities. The major public services are delivered through state and territory governments – for example, most areas of health, education, infrastructure, utilities, law and order, and community services. The funding for those services is collected mainly at the national level and transferred to states, territories and local governments through direct payments. A minor proportion of the transfers are provided for specific purposes under conditions set by the national government.

Under the devolved financial framework at the national level, performance management (including performance measures and programme evaluation) is generally the responsibility of individual ministers and their departments and agencies, although outcomes must be agreed with the Minister for Finance and Administration.

The Australian government's outcomes policy requires every department and agency within the general government sector, including statutory bodies, to identify comprehensive and explicit outcomes, outputs and performance measures for the quantity, quality, price and effectiveness of their activities. They are required to report on those items and any major evaluations in their budget plans (portfolio budget statements) and their end-of-year results (in annual reports). Further details of performance measurement arrangements are provided in Box 1.

Major and whole-of-government initiatives may require cross-portfolio agreement on evaluation and review strategies; this may include the departments and agencies involved in implementing the policies as well as Finance and/or the Department of the Prime Minister and Cabinet.

Users of performance information published by departments and agencies are primarily parliamentary committees which scrutinise budget estimates and annual reports. The main users in parliament are the Joint Committee of Public Accounts and Audit (JCPAA) and the Senate Standing Committee on Finance and Public Administration (SCFPA).

In relation to reporting in agency annual reports (which are signed by agency heads), the JCPAA approves requirements for reporting performance information in annual reports that are issued each year by the Department of the Prime Minister and Cabinet; these requirements must be adhered to by all FMA Act agencies. All CAC agencies must comply with reporting requirements specified in the CAC Act. The requirements do not change much from year to year other than to reflect changes in the components, such as adoption of Australian equivalents of international financial reporting standards and more detail on governance and corporate intentions.

Box 1. **Overview of the Australian government's outcomes framework**

The purpose of the outcomes framework is outlined in the following extract from Finance's policy guidance, first published in November 2000 and updated in 2003:

"The outcomes and outputs framework is intended to be dynamic and flexible. It works as a decision hierarchy:

- Government (through its ministers and with the assistance of relevant agencies) specifies the outcomes it is seeking to achieve in a given area.
- These outcomes are specified in terms of the impact government is aiming to have on some aspect of society (*e.g.* education), the economy (*e.g.* exports) or the national interest (*e.g.* defence).
- Parliament appropriates funds to allow the government to achieve these outcomes through administered items and departmental outputs.
- Items such as grants, transfers and benefit payments are administered on the government's behalf by agencies, with a view to maximising their contribution to the specified outcomes.
- Agencies specify and manage their outputs to maximise their contribution to the achievement of the government's desired outcomes.
- Performance indicators are developed to allow scrutiny of effectiveness (*i.e.* the impact of the outputs and administered items on outcomes) and efficiency (especially in terms of the application of administered items and the price, quality and quantity of outputs) and to enable the system to be further developed to improve performance and accountability for results."

The framework applies to all agencies and authorities in the general government sector, and the agency or authority is the basic unit of organisation* – that is, outcome statements are agency statements but must be agreed by the portfolio minister and the Minister for Finance and Administration. Performance measures and targets are set by each minister for their areas of responsibility, taking account of the conditions under which they operate, including the available budget.

The framework is intended to serve a number of objectives:

- a strategic objective: to guide overall resource allocation (budget measure) decisions by the government in the budget context;
- as the basis for parliament to appropriate money in the annual appropriation acts. In practice, neither departmental outputs (18% of total expenses) nor administered programmes appropriated by special or standing appropriations (73% of total expenses) are appropriated against outcomes; only administered programmes included in the annual appropriation acts (9% of total appropriations) are appropriated by outcome;

Box 1. Overview of the Australian government's outcomes framework (cont.)

- an agency management objective: departmental outputs and administered programmes are directed to the achievement of the results or impacts specified in the relevant agency's outcome statement;
- accountability and transparency to parliament and other stakeholders, achieved by reporting on the agency's performance in producing the government's intended outcomes through the departmental outputs it delivers and the programmes it administers on behalf of the government.

* Department of Finance and Administration, 1998, p. 9.

The Auditor-General has authority, under the Auditor-General Act 1997, to initiate financial and performance audits of agencies and programmes to inform parliament; however, he/she does not audit budget material. The Auditor-General has undertaken many performance audit reports examining the quality, coverage and information systems associated with performance information.¹

The Department of Finance and Administration (Finance) is responsible for providing guidance on performance management policies relating to budget-funded bodies and requirements for government statutory authorities and companies. Finance issues guidelines to agencies on the level of performance reporting, to be provided in agencies' statements to parliament as part of the information on the annual budget.

Finance also has responsibility for providing the government with advice on whole-of-government expenditure priorities. In this context, Finance provides advice to the cabinet and ministers on the performance of agencies and programmes, including when assessing new policy proposals in the annual budget process. Proposals for changes to the budget and medium-term estimates in the budget process, including new policies and savings, must identify the outcome they are intended to contribute to as well as key milestones for implementation and the agency's strategy for monitoring results.

Finance is responsible for developing policies on the review of expenditure initiatives; individual departments and agencies have ongoing responsibility for monitoring performance and undertaking evaluations of their own programmes. However, in October 2006 Finance established a strategic review unit (the Unit) that provides advice to senior ministers on matters warranting major (strategic) review as part of the budget process. The Unit co-ordinates cross-agency consultation on strategic reviews and administers those reviews approved by ministers. The strategic reviews will typically cover high-priority,

large, complex, cross-agency initiatives, and are intended to assist the government in improving the efficiency, effectiveness and appropriateness of expenditure programmes (including tax expenditure).

2. Measurement and assessment of results

The Australian government's performance information framework places a strong emphasis on agency-level outcomes as the foundation for assessment. Outcomes are defined as the results, impacts or consequences of actions by the Australian government for the Australian community. Outputs are the goods and services produced by the individual department or agency on behalf of the government that contribute to outcomes for external organisations or individuals. Outcomes are decided by the responsible ministers in consultation with the Minister for Finance and Administration. Individual ministers are responsible for choosing outputs, which are decided at a broad level by cabinet in the budget process. The emphasis on explicit measures of results is crucial to the usefulness of the framework as a tool for performance assessment and evaluation.

Performance information in Australia is meant to contribute to financial management and budgeting at three levels: internal agency management; whole-of-government resource management; and external accountability.

Agencies are expected to undertake their own performance assessment and evaluation as part of normal internal management practice. At a minimum, agencies are required to identify outcomes, administered items and outputs covering all expenditure within their area of responsibility. They are required to identify, measure and report publicly on key performance indicators for the quality and quantity of outputs and effectiveness indicators that assist in measuring the success of their contribution to identified outcomes. Published performance information on agency plans is provided at budget time (in portfolio budget statements), and after the end of the year the results are published in their annual reports.

It is widespread practice for agencies to monitor and report on a range of key indicators on a regular basis throughout the year. Practices vary from sophisticated reporting techniques such as balanced scorecards, performance dashboards or traffic light reports, to providing a list of progress against key indicators, showing variances from plans, as a supplement to the financial progress reports or to meet public reporting obligations.

There are no specific whole-of-government outcomes at the national level in Australia. Most state and territory governments have high-level targets or objectives that agencies are expected to consider in their planning and operations. The main mechanisms for using performance information for

whole-of-government resource management are budget process review requirements and specific cabinet-directed reviews of important programmes or budget measures. These arrangements are explained in Section 3 below.

A particular challenge to the development of performance information at the national level is that most public services are delivered through state and territory governments. Consequently, the Australian government does not control the use of resources and has limited influence on performance. One exception is for specific-purpose payments from the Australian government to states and territories, which generally require performance reporting and achievement of targets or performance conditions. For example, specific performance benchmarks are set for literacy, numeracy and participation in schools, the quantity and quality of housing for disadvantaged people, and a range of health services delivered through cross-jurisdictional agreements by state and territory governments.

Portfolio budget statements contain details of the origin and uses of resources available to each general government sector agency. Uses of funds are disaggregated by outcome and within each outcome, by departmental (controlled) and administered resources. Performance indicators and measures are reported for each outcome in terms of effectiveness and output quantity, and quality. Differences between plans and actual results on performance measures are not routinely used directly in budget formulation. However, they are sometimes used by agencies and Finance to support arguments for revision to programmes or to identify options for budget savings.

The Australian National Audit Office (ANAO) and parliamentary committees have expressed concerns about the overall quality of information in published reports, particularly in relation to outcomes.² The government's Budget Estimates and Framework Review also identified the need to examine agency outcomes information to ensure that it is consistent with the policy framework and appropriate to the needs of the government and parliament.

The review of outcomes is currently being undertaken by Finance in consultation with all other general government sector agencies. The focus of the review is on improving the specification of outcomes, to ensure that they refer to explicit impacts rather than outputs or objectives, and to strengthen the measures and methodology for assessing individual agency contributions to outcomes.

Finance has developed a list of questions to assist in diagnosing the quality of performance information; the list is also useful as a framework for monitoring improvement over time. The questions are used by Finance as a basis for dialogue with agencies about the quality of their performance information. Agencies and the ANAO have used the questions as a reference for their own purposes in designing and assessing performance information.

The basic outcomes review is expected to be completed in 2007/08. However, it will be important for continued monitoring and support to achieve sustained improvements in quality of information and behaviour in agencies. Improvements in the quality of performance information are expected to make it more useful in supporting management and policy decisions on programmes.

3. Integrating and using performance information in the budget process

The effect of performance information on decision making and resource allocation in the budget process is mixed.

The outcomes policy has resulted in the development and reporting of performance information by all agencies in the general government sector. This offers considerable scope for that information to be used in budget and management decision-making processes. At present, the potential for using the information has not been fully realised. There are initiatives to increase the emphasis on performance information and reviews, for example through revisions to the format of new policy proposals and by launching a study to assess budget review arrangements and propose options for reform.

The format of new policy proposals was reviewed and revised by Finance and the Department of the Prime Minister and Cabinet in late 2004. The changes require departments and agencies to identify the key benefits, risks and milestones for each proposal, as well as related implementation issues, to inform cabinet's consideration of the proposal. These changes provide the basis for realising new policies to manage the implementation process, track progress and inform evaluation.

Expenditure and programme reviews are a central feature of the Australian budget process, and the area where performance information is used to inform budget decision making. The Australian government revised review arrangements in October 2006 to achieve a more co-ordinated strategic process better linked to budget planning and resource allocation. The new arrangements involve Finance administration of procedures for identifying and managing reviews, in co-operation with other departments. Decisions on which major areas of public expenditure should be reviewed in any given year are made by senior ministers in the budget process. The results of the reviews are considered at the beginning of the following budget process by the senior ministers setting priorities.

A small number of strategic reviews will be undertaken each year on major programmes and cross-agency themes, including tax expenditures and taking account of intergenerational considerations.

The new arrangements supplement rather than replace agency performance measurement and evaluation activities. Wider independent review and evaluation activity relating to government policies and programmes also continues, for example through parliamentary inquiries, independent commissions, eminent persons and non-governmental organisations.

4. Reporting of performance information

Every year, as part of the budget-related documentation, each portfolio (i.e. a collection of related agencies under the responsibility of a minister of state) provides an extensive report on the plans for the budget and the forward estimates period for each of its constituent agencies. These portfolio budget statements³ include details of all sources and uses of funds by outcome.

Financial information on outcomes is supplemented by information on the administered items and outputs that contribute to each outcome. Also included is an extensive set of performance indicators, measures and targets for planned results and details of future evaluations. The portfolio budget statements also include a full set of budgeted financial statements for the agency covering four future years, as well as the estimated actual result for the current year.

The portfolio budget statements are a primary source of information for Senate committees during the budget scrutiny hearings following the presentation of the budget. Statements incorporating similar information are also provided in relation to other appropriation bills during the year.

The use of the information found in portfolio budget statements by Senate committees varies across agencies, from situations where there are many questions on achievements against indicators to situations where there are relatively few. Finance is working to improve the usefulness of these statements to parliament and other stakeholders, including in relation to the type and quantity of performance information they contain. The format and content of the statements will be reviewed in depth in 2007, as part of the Australian government's initiative to reduce red tape within the administration.

Aligned to portfolio budget statements are agency annual reports, which are published within four months of the end of each financial year. They contain audited financial statements and an explanation of agency performance during the financial year in question. They also publish actual results against individual performance measures for outcomes and outputs and the implications of evaluations finalised during the year.

The quality of performance reporting in annual reports has improved significantly since the introduction of accrual-based budgeting. For example, it is increasingly common for agencies to report portfolio budget statement targets in the same table as results, followed by a commentary on the reasons for major discrepancies and how agencies intend to respond to disappointing results.

There remains a wide variation in the quality of reports and the information contained in them.⁴ In an effort to encourage improvement, Finance and the ANAO jointly published a better practice guide for performance information in annual reports (ANAO and Department of Finance and Administration, 2004). The guide contains practical advice on the main areas for improvement, including the performance reporting framework, data management and measurement, and explanation of results. The guide also contains a large number of good practice examples for agencies to consider and emulate where appropriate.

Published performance information is only one of many types of information used by the cabinet and ministers to assess revenue and expenditure proposals in a budget decision-making context. Ministers rely on analysis and information in new policy proposals and reviews contained in confidential cabinet submissions and portfolio budget submissions prepared by the proposing agency. This information is often not publicly available. In addition, ministers rely heavily on policy and financial advice from Finance, which provides a policy and financial assessment of all expenditure proposals under consideration in the annual budget process.

5. Key challenges

A key challenge with current arrangements is to ensure that the links between programmes, outputs and outcomes are clear and measured effectively. The benefits of programme and outcome performance information relate primarily to agency efficiency and effectiveness. Finance is seeking to encourage improvement in the quality and precision of performance information and evaluation in agencies. The aim is to develop skills, systems and a culture in agencies to raise the standard and usefulness of performance information for internal planning and for constructive dialogue with external stakeholders.

A further challenge is to ensure that the government has better access to performance information by better integrating it into the decision-making phase of the budget. The government's decision to adopt a more centrally coordinated strategic review framework and its initiatives for review of the quality of agency information on outcomes will help overcome some of the variability of agency performance information and improve its overall usefulness.

Continuing pressure for improving the effectiveness and sustainability of government expenditure is a perennial challenge. Over the last six years, from 2000/01 to 2005/06, annual government expenditure increased by AUD 50 billion. Both new policy spending and growth in expenditure for the existing stock of government programmes have driven this increase.

New policy spending accounted for around 48% (or AUD 24 billion) of the total increase. A large part of this spending has been in high-priority areas for the government, in particular national security and defence, health, and social

security and welfare. These areas will remain sources of spending pressure over the medium term. While they are high priority, it is acknowledged that they also should be subject to review.

Expenditure on continuing programmes accounted for 52% (or around AUD 26 billion) of the overall government expenditure increase between 2000/01 and 2005/06. This group includes large programmes in high-priority spending areas, as well as a large number of small to medium-sized programmes.

The new strategic review arrangements are intended to ensure that an integrated and systematic framework is in place to allow ministers to:

- focus on the allocation of government expenditures;
- identify appropriate areas for review;
- ensure that programmes and outcomes remain aligned with policy priorities, are effective, and are managed efficiently.

6. Solutions

Better integration of performance information into agency management processes and information systems will lead to better-informed decisions and better policy outcomes. Improving the relevance and quality of information available for the decision-making phases of the budget process is a long-term challenge that will require sustained effort from Finance and agencies.

Finance's current focus is on establishing the new strategic review framework, simplifying policies and procedures to meet financial management requirements, and improving the quality of financial and non-financial reporting. The aims are to improve financial management compliance and accountability while making existing and new programmes more coherent, more effective and better targeted to current government priorities.

7. Lessons learned and impact

Australia's approach to incorporating a focus on performance has been a long-term, iterative process. This has provided many benefits, not least the opportunity to learn from experience before proceeding with further reforms. This has also been important because of the interrelationship between performance and other aspects of the financial, accountability, political and management environment. The complexity of interactions and incentives is difficult to comprehend in isolation from practical experience, making "big bang" changes potentially high risk.

The iterative approach to improvement has allowed Australia to proceed with care, making refinements as unanticipated or unintended effects occur, and keeping to a long-term path of management for results.

Supplementary guidance, training and advice are being developed as part of continuing efforts to achieve better performance information. These efforts will continue alongside further research and sharing of good practices within and outside Australia.

Australia has faced two recurring themes in establishing good performance information:

- the quality of performance information in relation to agency contributions to outcomes and outputs;
- the limited use of the performance information for decision making in the budget context.

Outcomes and outputs will remain essential parts of Australia's budgeting and management framework. However, it is important to ensure that links between programmes, outputs and outcomes are clear and are measured effectively, particularly if this performance information is to be relied on for budget decision making.

As with other aspects of financial management reforms associated with the devolution of responsibility, it is crucial that new policies and practices are well understood by people in line agencies and that these people have the skills, capacity, resources and authority to implement the initiatives effectively. Implementation is much slower and more uneven if those responsible for data and measurement are incapable or unable to make the necessary changes.

With respect to enhancing the utility of performance information for budget decision making, a major challenge in introducing a systematic approach to programme reviews will be to ensure that such reviews add value to government considerations, use agency resources efficiently, and do not become a mechanical exercise.

Notes

1. For a list of performance reports by the Australian National Audit Office, see www.anao.gov.au.
2. For example, see JCPAA, 2002; SCFPA, 1999, 2000 and 2007; and ANAO, 2003 and 2007.
3. Portfolio budget statements are available on each department's website or can be accessed through the Australian government budget portal at www.budget.gov.au.
4. For further information on the quality of performance information in annual reports, refer to ANAO, 2003 and 2007.

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