

The Auditor-General  
Audit Report No.14 2009–10  
Performance Audit

## **Agencies' Contract Management**

**Australian Federal Police**

**Austrade**

**Department of Foreign Affairs and Trade**

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of Australia 2009

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Canberra ACT  
25 November 2009

Dear Mr President  
Dear Mr Speaker

The Australian National Audit Office has undertaken a performance audit in the Australian Federal Police, Austrade and the Department of Foreign Affairs and Trade in accordance with the authority contained in the *Auditor-General Act 1997*. I present the report of this audit and the accompanying brochure. The report is titled *Agencies' Contract Management*.

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

Yours sincerely

A handwritten signature in black ink, appearing to read 'Ian McPhee', is positioned above the printed name and title.

Ian McPhee  
Auditor-General

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

## AUDITING FOR AUSTRALIA

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

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# Abbreviations and Glossary

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|           |  |
|-----------|--|
| ACT       | Australian Capital Territory   |
| AFP       | Australian Federal Police  |
| ANAO      | Australian National Audit Office   |
| AusTender | A system administered by the Department of Finance and Deregulation and accessible to the public through the Internet, for agencies to publish and report information regarding procurement and contracts. |
| Austrade  | Australian Trade Commission  |
| BPG       | Better Practice Guide  |
| CEO       | Chief Executive Officer  |
| CEIs      | Chief Executive Instructions   |
| CMP       | Contract Management Plan   |
| CPGs      | Commonwealth Procurement Guidelines  |
| DFAT      | Department of Foreign Affairs and Trade  |
| DIISR     | Department of Innovation, Industry, Science and Research   |
| FMA Act   | <i>Financial Management and Accountability Act 1997</i>  |

FMA Regulation 9     *Financial Management and Accountability Regulations 1997*

Regulation 9 Approval of spending proposals – principles

An approver must not approve a spending proposal unless the approver is satisfied, after reasonable inquiries, that giving effect to the spending proposal would be a proper use of Commonwealth resources (within the meaning given by subsection 44 (3) of the Act).

*Note:* When this regulation commenced, subsection 44 (3) of the Act defined *proper use* to mean efficient, effective and ethical use that is not inconsistent with the policies of the Commonwealth.

FMA Regulation 10     *Financial Management and Accountability Regulations 1997*

Regulation 10 Approval of future spending proposals

If any of the expenditure under a spending proposal is expenditure for which an appropriation of money is not authorised by the provisions of an existing law or a proposed law that is before the Parliament, an approver must not approve the proposal unless the Finance Minister has given written authorisation for the approval.

FMIS                      Financial Management Information System

ICT                        Information and Communication Technology



## **Summary and Recommendations**



# Summary

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## Introduction

1. Contracting in many Australian Government agencies involves a significant level of expenditure and agency resources. Contracting activity ranges from straightforward procurements such as the provision of advisory services through to complex long term projects that may involve the development of information and communications technology. It may involve an oral or a written contract.
2. To support its operations, each year the Government purchases billions of dollars in goods and services, including capital acquisitions. In 2007–08, the Government purchased \$24.6 billion of goods and services from suppliers,<sup>1</sup> being 30 per cent of its total goods and services expenses. In comparison, in constant dollars, the Government spent \$23.2 billion on supplier goods and services in 1997–98. This also was 30 per cent of its total goods and services expenses.
3. Government agencies entered into around 69 500 contracts in 2007–08 worth more than \$26.4 billion,<sup>2</sup> 99 per cent of which had a value of less than \$5 million. Many of these contracts were for the provision of goods and services for periods greater than one year.
4. The Commonwealth Procurement Guidelines (CPGs) establish the core procurement policy framework and articulate the Government's expectations of all departments and agencies subject to the *Financial Management and Accountability Act 1997 (FMA)*.<sup>3</sup> The CPGs establish the Government's procurement policy for agencies. The Guidelines focus on value for money and how it may be achieved by agencies when procuring. The CPGs advise that:

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<sup>1</sup> These figures exclude expenditure on capital acquisitions, such as the purchase of military equipment. Source: Department of Finance and Deregulation, Available from: <<http://www.finance.gov.au/publications/commonwealth-consolidated-financial-statements/2008.html>> [accessed 29 September 2009].

<sup>2</sup> These figures include expenditure on capital acquisitions. Source: Department of Finance and Deregulation (AusTender), available from: <<http://www.finance.gov.au/publications/statistics-on-commonwealth-purchasing-contracts/index.html>> [accessed 29 September 2009].

<sup>3</sup> Commonwealth Procurement Guidelines – FMG 1, available from: <<http://www.finance.gov.au/publications/fmg-series/procurement-guidelines/index.html>> [accessed 29 September 2009].

Procurement encompasses the whole process of acquiring property or services. It begins when an agency has identified a need and decided on its procurement requirement. Procurement continues through the processes of risk assessment, seeking and evaluating alternative solutions, contract award, delivery of and payment for the property or services and, where relevant, the ongoing management of a contract and consideration of options related to the contract.<sup>4</sup>

5. The CPGs guide agencies to develop contract terms and conditions consistent with the financial management framework underlying the procurement of goods or services. In so doing, they aid agencies in achieving value for money in their purchasing.

6. Contract management is an important phase in the procurement cycle that commences after the contract is signed. It focuses on managing the rights and obligations of parties to the contract and ensuring that goods and services are delivered in accordance with the contract.

7. In July 2009, the Minister for Finance and Deregulation announced the next steps in the Government's approach in purchasing and contract management.<sup>5</sup> The Minister announced that the Government was conducting scoping studies in a number of product markets to determine whether coordinated procurement arrangements, such as negotiating whole-of-government contracts, can improve overall value for money in these markets. In addition, the Minister outlined reforms to government purchasing to promote value for money and to achieve better results for businesses and the community, including the appointment of a Procurement Coordinator to oversight government procurement practices and policies.

## Audit objective and scope

8. The audit objective was to assess the effectiveness of agencies' contract management by determining if they had sound practices and systematic approaches to this activity. Particular attention was given to each agency's:

- day-to-day management of individual contracts; and
- approach to managing its contract population.

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<sup>4</sup> Department of Finance and Deregulation, *Commonwealth Procurement Guidelines*, December 2008, p. 3.

<sup>5</sup> Minister for Finance and Deregulation, *Australian Government Procurement Statement*, 28 July 2009.

9. The audit examined contract management in three agencies: the Australian Federal Police (AFP), the Australian Trade Commission (Austrade) and the Department of Foreign Affairs and Trade (DFAT).

10. The audit had two parts. The first involved the ANAO reviewing the management of 30 small to medium size contracts (ten in each agency) with estimated expenditure for each of between \$80 000 and \$5 million. The majority of contracts were for the provision of a service, such as legal services or property management.

11. The second part of the audit involved an examination of each agency's policy and processes to manage its contract population. This involved reviewing how each agency managed its contract data, monitored and reported on supplier performance, and managed risks, training and supplier relationships.

## Overall conclusion

12. The CPGs indicate that the aim of individual contract management is to ensure that goods and services are provided to the required standard within the agreed schedule so as to achieve value for money. Generally, once a contract is signed, the contract's duration is much longer than the initial procurement stage. Therefore, consistent and informed contract management is important for an agency to get the most value from each procurement.

13. Overall, the ANAO concluded that, for the three audited agencies, contract management processes and practices provided an adequate level of support for the provision of goods and services. Notwithstanding, there were a number of instances where there was insufficient evidence that delegates had approved contract variations or invoice payments. Additionally, none of the agencies periodically reviewed the success of its approach to contracting such as through monitoring the percentage of contracts completed on time and on budget, or the number and purpose of contract variations, so as to improve procurement and contract management practices.

14. Consequently, agencies will benefit from:

- improving management and recording of payments, including compliance with relevant Finance Regulations; and
- giving more attention to the approval process for contract variations.

15. The three agencies' procurement and contract advisory units provided a satisfactory level of support for agency staff to manage small to medium size

contracts. Given the devolved nature of contract management in agencies and in light of agencies' continued reliance on contracts with the profit and not-for-profit sectors, the audit identified potential improvements in these units' roles. These included:

- improved processes to provide contract management advice; and
- periodically reviewing agency-wide contracting performance, for example, through analysis of the contract register or surveys, to encapsulate agency trends in contract management practices and approaches which delivered superior contract outcomes.

16. Accordingly, the ANAO has made two recommendations. The first is aimed at strengthening agency compliance with Finance Regulations when they vary contracts. The second encourages agencies to develop a systematic approach to advising staff who manage contracts, and for agencies to review the success of their approaches to contract management.

## Key findings by Chapter

### Day-to-day management (Chapter 2)

17. Daily management involves several activities including contract payments, monitoring and reporting, and varying contracts. The ANAO reviewed the management of 30 contracts worth approximately \$37 million.

#### *Payments*

18. The ANAO reviewed 45 recent supplier invoices and found 21 had insufficient evidence of approval by a delegate. Additionally, 85 per cent of contract managers interviewed advised that they did not check payments (or did not know how to check payments) in their agency's Financial Management Information System (FMIS), relying on their accounts payable section, as well as the internal checks within the finance system, to ensure payments were accurate and timely.

#### *Payments to small businesses*

19. Government policy for payments to small businesses requires agencies to adopt maximum payment terms 'not exceeding 30 days' from the date of receipt of correctly rendered invoices. The implications of agencies not paying correctly-rendered invoices from small businesses within 30 days are that they are not complying with Government policy, and that they may be required to pay interest on late payments for contracts with a worth up to \$1 million. Six of

the 30 supplier contracts reviewed were with small businesses. Thirty six of the 45 invoices reviewed were paid within the 30 days, while nine were paid after 30 days, two of which were for small businesses.

20. We also examined the results of the Department of Innovation, Industry, Science and Research's annual *Survey of Australian Government Payments to Small Business* for 2006–07 and 2007–08. While Austrade and DFAT reported that they paid more than 90 per cent of their small business invoices within 30 days, the number of small business invoices the AFP reported as paid within 30 days dropped from 76 per cent in 2006–07 to 69 per cent in 2007–08. The AFP advised that this was due to a largely decentralised and manual accounts payable process. AFP further advised that improvements to its FMIS and related processes had since increased compliance.

21. The results of the invoice review and contract managers' responses to interview questions on payments indicated that many contract managers would benefit from financial skills training. The latter training involves agencies determining which financial controls and reports were most important for contract managers. For example, where an FMIS checks for duplicate invoices, training could include advice for contract managers of the existence of such a control.

### *Monitoring and reporting by contract managers*

22. The ANAO interviewed contract managers to determine how they monitored their contractors' performance. Seventy five per cent advised they had regular contact with the contractor ranging from ad hoc contact to scheduled meetings and performance reports. Only ten of the 29 contract files contained documentation of monitoring activities, such as copies of supplier reports, minutes of meetings or records of email or telephone communications.

23. While there were potential improvements in the monitoring of contractors' work, for instance, in documentation of decisions and communication, agencies' monitoring and reporting were largely commensurate with the complexity and risk of the contracts reviewed.

### *Contract variations*

24. Twenty three of the 30 contracts had at least one variation suggesting that the 'norm' was to vary contracts. The majority of variations (53 per cent) were for an extension to the duration of the contract. Other variations included the addition of services, increased pricing, changes to personnel, and/or reporting requirements.

25. The ANAO reviewed contract files for evidence of properly executed variations and found 80 per cent of files contained signed correspondence between both parties. However, for some variations there was either no correspondence on file showing the agreement of both parties, or documentation was unsigned. There was also a small number of variations approved after the expiry of the contract.

### *Compliance with legislation*

26. Finance Regulations set out the requirements for approval of current and future spending proposals. FMA Regulation 9 requires that an approver must not approve a proposal to spend public money unless the approver is satisfied, after reasonable inquiries, that giving effect to the spending proposal would be a proper use of Commonwealth resources, that is, an efficient, effective and ethical use of public money that is not inconsistent with the policies of the Commonwealth.

27. FMA Regulation 10 requires authorisation for a spending proposal where any of the expenditure under the spending proposal is expenditure for which an appropriation of money is not authorised by the provisions of existing laws or a proposed law before the Parliament. If so, an approver must not approve the proposal unless the Finance Minister (or delegate) has given written authorisation for the approval. FMA Regulation 10 authorisation most commonly arises in relation to multi-year spending proposals. Where an agency requires FMA Regulation 10 authorisation, it must obtain this from the Finance Minister's delegate before seeking FMA Regulation 9 approval.

28. The ANAO reviewed 55 variations across 23 contracts and identified 32 that required FMA Regulation 9 approval and/or FMA Regulation 10 authorisation. Eleven of these 32 variations did not have documentation on file indicating that a delegate had approved and/or authorised the variation.

29. Around 30 per cent of contract managers interviewed did not know about these two Regulations and whether they had applied them. The consequence was that if a contract manager changed a contract without obtaining approval, he or she may have committed the agency to a spending proposal without complying with legislation.

30. Agencies will benefit from reviewing, where necessary, their policies, guidelines and training, including refresher training, affirming that their personnel understand and comply with FMA Regulations 9 and 10.



## **Agencies' management of their contract populations (Chapter 3)**

31. The approach an agency takes to manage its contract population, the resources devoted, and the effort required, is best guided by:

- the number, complexity, and value of its contracts; and
- the importance of contracts to agency goals.

32. We reviewed each agency's contract register to determine the number of active contracts and their value. On 30 June 2008, the three agencies had over 2100 active contracts worth more than \$2 billion.

33. The three agencies advised that they recorded contract expenses in their financial statements under the heading 'Suppliers, provision of goods and services to external entities'. We reviewed each agency's financial statements to determine growth in external supplier expenses and external supplier expenses as a percentage of total departmental agency expenses. From 2005–06 to 2007–08, the AFP's and DFAT's supplier expenses grew by 28 per cent and 30 per cent respectively, while Austrade's reduced by 12 per cent.

34. In 2007–08, the three agencies committed approximately 40 per cent of their departmental expenses to external suppliers. The nature and size of contracting in the three agencies warranted each agency having a systematic approach to manage its large population of contracts.

35. To oversee the administration of procurement and contracts and assist their contract managers, each agency had established a procurement and contract advisory unit. Each advisory unit:

- developed and maintained policy and guidelines;
- provided advice and training;
- managed the contract register; and
- prepared reports for internal and external audiences.

36. Contract management in the AFP and DFAT was mostly decentralised. In the AFP the procurement and contract advisory unit managed some agency-wide contracts and two of the AFP's units also had procurement and contract advisory support teams providing assistance to AFP staff. DFAT placed specialist contract managers in four of its divisions. Contract management in Austrade was fully decentralised.

### *Managing and reporting contract population data*

37. For agencies to manage their contract populations they need systems to collect, manage and disseminate information for internal and external purposes. The principal method for recording such information was through each agency's contract register.

38. The three agencies' contract registers had the basic characteristics necessary to meet their external reporting requirements, for example, in recording information such as contractor name, contract start and finish dates, and value. However, there were some limitations in terms of the accuracy, consistency and completeness of the information in the register, such as:

- fourteen of the 30 contracts were incorrectly listed in contract registers;
- financial data recorded in the contract registers related to different types of information, leading to some ambiguity in interpretation. For example, the data was sometimes a potential and sometimes a confirmed expenditure. Additionally, in some cases, the financial data was for the current year commitment or expenditure, while other data was for the life of the contract (that is, commitment or expenditure over several years). Clarifying the nature of the financial data would assist users of contract registers; and
- limited monitoring of contract end dates by AFP and DFAT affecting the preparedness of agencies to manage follow-on arrangements.

39. The ANAO considers that there is merit in agencies considering the costs and benefits of linking the contract register to the FMIS and broadening access to the register. We noted that:

- none of the contract registers was linked to the agency's FMIS, reducing the ability to track and report payments, particularly where the contract was for several years. The AFP has since moved the register into its FMIS, DFAT is considering linking theirs, while Austrade had assessed the resources required to link the two systems and found that presently it would be too expensive to connect them; and
- there was limited access to the contract register. View access in two agencies was limited to the procurement and contract units and to the originator of the contract record. This inhibited the sharing of information. If more staff were able to access contract data (remaining mindful of security and confidentiality requirements), they could determine if the goods and services they required were already being

provided to the agency and, if so, whether they could use existing contracts for those purposes.

40. The three agencies conducted some agency-wide monitoring and reporting of contracts including through affirmations of compliance with financial legislation<sup>6</sup> and through financial commitment registers. Although each agency had many contracts, there was minimal agency-wide monitoring of: supplier performance, annual contracting costs, numbers of extensions and variations, and numbers of contracts finished on time and within budget.

### *Central agency leadership*

41. Finance organises procurement discussion forums and distributes a procurement bulletin on Commonwealth procurement. While some briefings and presentations may have introduced aspects of contract management, the latter was not a direct focus. These forums provide the opportunity to discuss and share ideas on contract management alongside the current focus on procurement.

## Summary of agencies' responses

42. Each of the audited agencies agreed with the two recommendations in this report. Agency responses to each of the recommendations are shown in the body of the report. Agencies' general comments are shown at Appendix 6.

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<sup>6</sup> Chief Executive Officers (CEOs) make these affirmations through providing their Ministers with annual Certificates of Compliance with financial legislation.

# Recommendations

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*The following recommendations are based on findings from fieldwork at the audited agencies and are likely to be relevant to all APS agencies. Therefore, all APS agencies should assess the benefits of implementing the recommendations in light of their circumstances.*

## **Recommendation No. 1**

### **Para 2.61**

The ANAO recommends that agencies review and where required strengthen their compliance with Finance Regulations, with specific reference to contract variations and management of contract records.

## **Recommendation No. 2**

### **Para 3.44**

The ANAO recommends that agencies managing a broad range and large number of contracts:

- (a) develop a systematic approach to disseminating information on contract management; and
- (b) periodically review aggregate contract management information to identify trends in contract management performance and to use the data to improve contract management approaches.

## **Audit Findings and Conclusions**



# 1. Introduction

---

*This chapter provides the background to the audit. It defines and includes information on contract management, and it outlines the audit objective, criteria, scope and methodology.*

## Background

**1.1** Contracting is an important part of how the Government does business with the profit and not-for-profit sectors, and therefore needs to be managed well. Contracting activity ranges from straightforward procurements such as the provision of advisory services through to complex long term projects that may involve the development of information and communications technology. It may involve an oral or a written contract.

**1.2** Agencies require processes and guidelines to manage their contracts and to comply with legislation and government policy. Key elements of contract management involve managing risks to the success of projects, as well as managing relationships and resources, specifying responsibilities, and behaving legally and ethically. Contracting activity in many Australian Government agencies represents an important business activity, often involving a significant level of expenditure and the use of substantial agency resources.

**1.3** The Department of Finance and Deregulation maintains a system called AusTender to collate information on government contracting. Using AusTender data, Table 1.1 shows that the number of contracts entered into by Australian Government agencies fell from 87 132 in 2005–06 to 69 493 in 2007–08. During this period, the value of these contracts also reduced from \$29.4 billion to \$26.4 billion.<sup>7</sup>

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<sup>7</sup> These figures include expenditure on capital acquisitions.

**Table 1.1**

**Total contracts entered into by Government agencies**

| Financial Year | Value \$b | Numbers of Contracts |
|----------------|-----------|----------------------|
| 2005–06        | 29.4      | 87 132               |
| 2006–07        | 29.0      | 82 532               |
| 2007–08        | 26.4      | 69 493               |

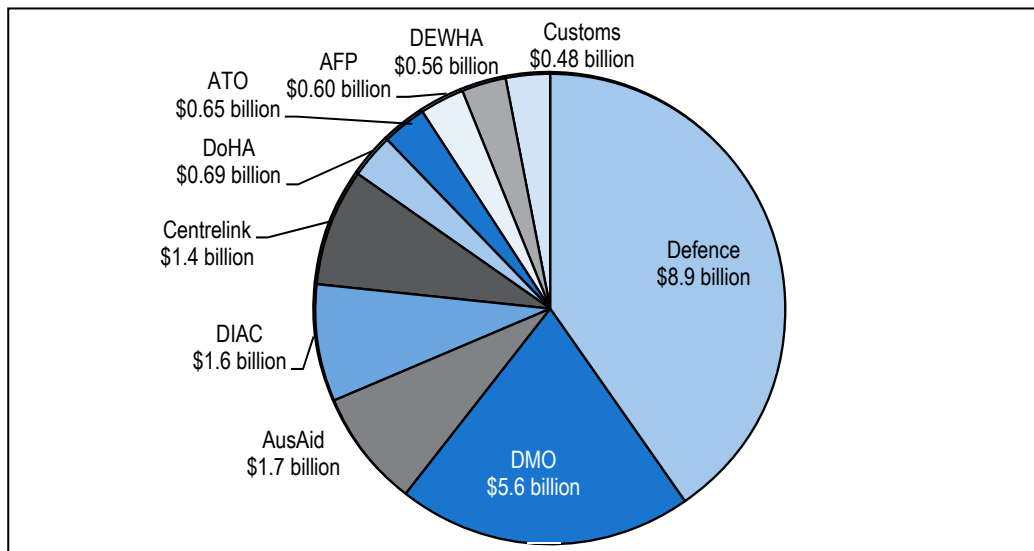
Source: Department of Finance and Deregulation (AusTender).

**1.4** Of the 69 493 contracts registered in AusTender for 2007–08, 99 per cent had a value of less than \$5 million. In 2007–08, the average value of government agency contracts worth less than \$5 million was approximately \$135 000. Thousands of staff in government agencies are involved in the management and administration of contracts. Further data on the Government’s contracting expenditure is in Appendix 1.

**1.5** Figure 1.1 shows the ten agencies with the largest new financial contractual commitments in 2007–08. The majority of committed contract expenditure in 2007–08, \$22.19 billion or 84 per cent, was by these ten agencies.

**Figure 1.1**

**Top ten agencies by value (\$ billion) of contracts signed in 2007–08**



Source: Department of Finance and Deregulation (AusTender), Available from: <http://www.finance.gov.au/publications/statistics-on-commonwealth-purchasing-contracts/index.html>.



## Government expenditure on suppliers

**1.6** To support its operations, each year the Government purchases billions of dollars of goods and services, including capital acquisitions. To further understand contracting expenditure, we reviewed the Australian Government's consolidated financial statements to identify supplier expenses as a proportion of total goods and services expenses in 1997–98 to 2007–08.

**1.7** In 2007–08 the Government purchased \$24.6 billion in goods and services from suppliers,<sup>8</sup> being 30 per cent of its goods and services expenses. Figure 1.2 shows that, in constant dollars,<sup>9</sup> in 1997–98 the Government spent \$23.2 billion on supplier goods and services, which also was 30 per cent of its total expenses. In other words, while this points towards agencies' reduced expenditure on contracts in recent years, over a ten year period, agency expenditure on contractors or suppliers was relatively stable.<sup>10</sup>

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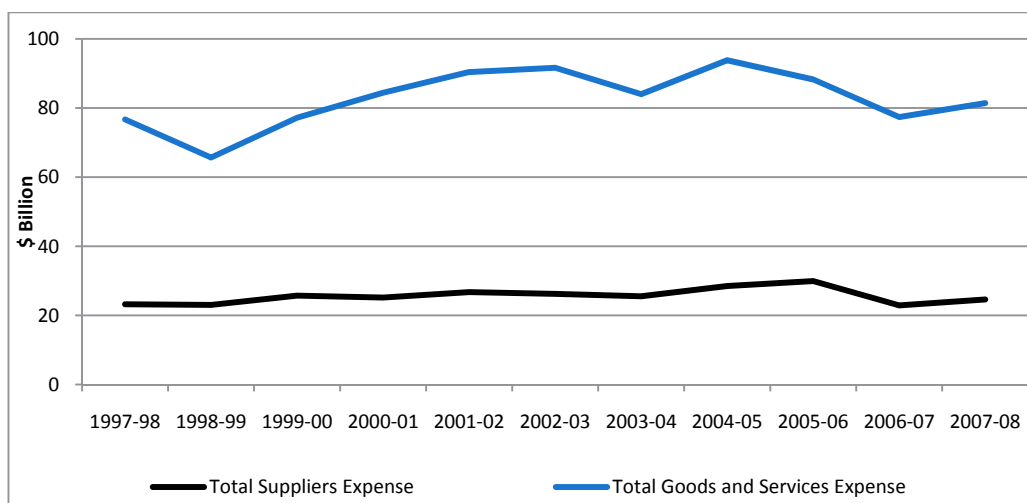
<sup>8</sup> Expenditure on supplier goods and services in this series excludes expenditure on capital acquisitions, such as the purchase of new military equipment.

<sup>9</sup> The amounts were adjusted for inflation using the Reserve Bank's CPI index, and expressed in average 2007–08 values.

<sup>10</sup> The Commonwealth Procurement Guidelines refer to procurements from suppliers. The three audited agencies used the terms contractors and suppliers interchangeably, as does this report. The Department of Finance and Deregulation advised that it had not developed definitions for the terms 'contractor, supplier and provider'. The department defined terms in the context of use. For example, the department wrote that in certain contexts 'contractor' can mean a company that supplies certain goods (and which may also be described as a supplier), or it can mean an individual who provides labour hire services through a third party company (that can also be defined as a service 'provider').

**Figure 1.2**

**Government expenditure on goods and services including suppliers, 1997–98 to 2007–08<sup>11</sup>**



Source: Australian Government consolidated financial statements 1997–98 to 2007–08.

## Legislation and government policy in procurement

**1.8** The main legislation and policy affecting agency procurement are:

- the *Financial Management and Accountability Act 1997*<sup>12</sup> (FMA Act) and *Regulations*<sup>13</sup> that provides the basis for the proper management of public money and public property; and
- the *Commonwealth Procurement Guidelines* (CPGs)<sup>14</sup> that establishes the Government's procurement policy for departments and agencies

<sup>11</sup> *Consolidated Financial Statements For Year Ended 30 June 2008*, p. 35 and 96. Expenses are defined as:

- Goods and services - employee benefits, suppliers, depreciation and amortisation, net foreign exchange loss, net write-down and impairment of assets, net losses from the sale of assets, and other goods and services; and
- Suppliers – supply of goods and services, operating lease rental expenses, and other. Available from: [http://www.finance.gov.au/publications/commonwealth-consolidated-financial-statements/docs/CFS\\_2008.pdf](http://www.finance.gov.au/publications/commonwealth-consolidated-financial-statements/docs/CFS_2008.pdf) [accessed 6 May 2009].

<sup>12</sup> The *Financial Management and Accountability Act 1997* (current). Available from <[http://www.comlaw.gov.au/ComLaw/Legislation/ActCompilation1.nsf/0/41293840813D0989CA25757D0082542C/\\$file/FinanMgmtAccount1997WD02.pdf](http://www.comlaw.gov.au/ComLaw/Legislation/ActCompilation1.nsf/0/41293840813D0989CA25757D0082542C/$file/FinanMgmtAccount1997WD02.pdf)> [accessed 29 April 2009].

<sup>13</sup> *Financial Management and Accountability Regulations 1997* (current). Available from <[http://www.comlaw.gov.au/ComLaw/Legislation/LegislativeInstrumentCompilation1.nsf/0/04AB6BBD481B19F8CA25757F0015A7A0/\\$file/FinanManAccount1997.pdf](http://www.comlaw.gov.au/ComLaw/Legislation/LegislativeInstrumentCompilation1.nsf/0/04AB6BBD481B19F8CA25757F0015A7A0/$file/FinanManAccount1997.pdf)> [accessed 29 April 2009].

subject to the FMA Act, and principles for agencies' acquisition of property and services. The procurement policy framework is a subset of the financial management framework related to the procurement of property or services. The CPGs are based on the FMA Act principles of value for money, efficient, effective and ethical use of resources, and accountability.

**1.9** Building on existing legislation and policy, the Minister for Finance and Deregulation released a statement<sup>15</sup> in July 2009 announcing reforms to government purchasing to improve value for money and to achieve better results for businesses and the community. These reforms included appointment of a Procurement Coordinator to oversight government procurement practices and policies. The appointee will provide the Government with a clearer picture of agencies' procurement and to what extent they implement government procurement policy.

## Contract management

**1.10** The CPGs indicate that:

Procurement encompasses the whole process of acquiring property or services. It begins when an agency has identified a need and decided on its procurement requirement. Procurement continues through the processes of risk assessment, seeking and evaluating alternative solutions, contract award, delivery of and payment for the property or services and, where relevant, the ongoing management of a contract and consideration of options related to the contract.<sup>16</sup>

**1.11** Agencies that comply with the CPGs in the early phases of procurement, before the contract is signed, have a sound basis for signing contracts with terms and conditions favourable to the Commonwealth.

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<sup>14</sup> Department of Finance and Deregulation, Financial Management Guidance No. 1, *Commonwealth Procurement Guidelines*, p. 2, available from: <http://www.finance.gov.au/publications/fmg-series/docs/CPGs-2008.pdf> [accessed 27 April 2009].

<sup>15</sup> Department of Finance and Deregulation, *Australian Government Procurement Statement*. Available from: [http://www.financeminister.gov.au/media/2009/docs/Australian\\_Government\\_Procurement\\_Statement.pdf](http://www.financeminister.gov.au/media/2009/docs/Australian_Government_Procurement_Statement.pdf) [accessed 10 August 2009].

<sup>16</sup> *ibid.*, p. 10.

**1.12** Contract management is an important phase in the procurement cycle that commences after the contract is signed.<sup>17</sup> It is the process that ensures all parties meet their obligations. It includes managing the contractual relationship and ensuring that goods and services are delivered to specifications.

**1.13** Contracts can vary in value from hundreds of dollars to hundreds of millions of dollars, in duration from days to years, and in complexity from simple to complex. Examples of the purposes of agency contracts include:

- services such as financial, travel, or human resource management;
- property management, including the cleaning and maintenance of offices;
- computer system development;
- freight and transport services, including courier services;
- development and maintenance of equipment;
- supply of goods such as copying paper to complicated equipment; and
- construction projects from standard office buildings and equipment to specialist quarantine facilities.

**1.14** The contract management approach an agency adopts, the resources devoted, and the effort required, is dependent on the purpose, number, type, complexity, duration and value of its contracts.

**1.15** Good contract management can reduce costs and keep costs stable for goods and services provided to or on behalf of the government agency. An inadequate contract management approach has the potential to adversely impact on an agency's capacity to achieve value for money and to soundly manage its resources.

## **Previous reviews**

**1.16** The ANAO has conducted several audits over the past five years that have addressed elements of contract management. Common themes identified

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<sup>17</sup> FMA Regulation 3 defines a Commonwealth contract as 'an agreement for the procurement of property and services under which the Commonwealth is obliged, or may become obliged, to make a payment of public money, available from: <http://www.comlaw.gov.au/comlaw/Legislation/LegislativeInstrumentCompilation1.nsf/0/32745DE18FB8EB77CA25757F0010E308?OpenDocument> [accessed 15 April 2009].

as areas for improvement in contract management included risk management, payments, monitoring, measuring and reporting on performance, training, and management of variations. A selection of ANAO audits and other publications about contracting is listed in Appendix 2.

## Audit approach

### Objective and criteria

**1.17** The audit objective was to assess the effectiveness of agencies' contract management by determining if they had sound management practices and systematic approaches to this activity. Particular attention was given to each agency's:

- day-to-day management of individual contracts; and
- approach to managing its contract population.

### Scope and methodology

**1.18** As mentioned earlier, the Department of Finance and Deregulation's AusTender data show that in 2007–08 approximately 69 000 contracts had a value of less than \$5 million. These were 99 per cent of all contracts recorded in AusTender. Since the majority of agency engagement with suppliers of goods and services is within this range, the ANAO focused on these contracts.

**1.19** The audit examined contract management in three FMA Act agencies, the Australian Federal Police (AFP), the Australian Trade Commission (Austrade) and the Department of Foreign Affairs and Trade (DFAT). Table 1.2 outlines the role, number of staff and annual expenditure for the three agencies. Chapter 3 contains more specific information about the three agencies' contract populations.

**Table 1.2**

#### Summary information on AFP, Austrade and DFAT

| Agency | Role and staffing   | Total expenses<br>2007–08 |
|--------|---|---------------------------|
| AFP    | To enforce Commonwealth criminal law and protect Commonwealth and national interests from crime in Australia and overseas.<br><br>Approximately 6500 staff operating in Australia and overseas. | \$1.25 billion            |

| Agency   | Role and staffing  | Total expenses<br>2007–08 |
|----------|--|---------------------------|
| Austrade | To assist Australian businesses contribute to national prosperity by succeeding in trade and investment internationally, and promoting and supporting productive foreign investment in Australia.<br>Approximately 1000 staff operating in Australia and overseas. | \$206 million             |
| DFAT     | To advance the interests of Australia and Australians internationally.<br>Approximately 3500 staff operating in Australia and overseas.  | \$806 million             |

Source: AFP, Austrade and DFAT 2007–08 annual reports.

**1.20** The three agencies maintained contract registers that recorded their contract details. DFAT also maintained a separate register for its overseas posts' contracts. These latter contracts were not included in the audit.

**1.21** The audit had two parts. The first involved the ANAO reviewing the management of 30 contracts (10 in each agency) with estimated expenditure of between \$80 000<sup>18</sup> and \$5 million. The majority of contracts were for the provision of a service, such as legal services or property management.

**1.22** Fieldwork involved:

- examining individual contract documentation;
- interviewing each of the 23 contract managers;
- examining each agency's contract management policy and guidance documentation;
- reviewing each agency's contract data; and
- discussions with each agency's procurement and contract advisory units and other relevant agency areas involved in contract management.

**1.23** The second part of the audit involved an examination of each agency's policy and processes to manage its contract population. This involved reviewing how each agency managed its contract data, monitored and

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<sup>18</sup> Agencies procuring goods and services, where the value is greater than \$80 000, must comply with the Commonwealth Procurement Guidelines' mandatory procedures. There are special requirements for the procurement of construction services where the threshold for reporting is \$9 million.

reported on supplier performance, managed risks and training, and supplier relationships.

**1.24** Fieldwork was conducted between December 2008 and April 2009. The audit was conducted in accordance with ANAO's Auditing Standards at a cost of \$440 000.

## **Report structure**

**1.25** In addition to this introductory chapter, this report has two other chapters:

- Chapter 2 examines the day-to-day management of 30 contracts across the three agencies; and
- Chapter 3 examines each agency's approach to managing its contract population.

## 2. Day-to-day management

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*This chapter reviews the management of a sample of 30 small to medium size contracts across the AFP, Austrade and DFAT.*

**2.1** This chapter reviews one part of the procurement process, which is the management of 30 contracts worth approximately \$37 million. The majority of reviewed contracts were for the provision of a service, such as legal services or property management.

### Contracts reviewed

**2.2** Ten contracts were selected from each agency's contract register based on the following criteria:

- a value of between \$80 000 and \$5 million;
- the contract was for goods and services; and
- five were completed and five were operational contracts.

**2.3** Applying these criteria, the selected contracts:

- had values ranging from \$120 000 to \$4.2 million.
- had terms of one to eight years, with an average term of 3.5 years;
- all had options to extend, with the average extension being one year;
- were for goods and services:
  - seven contracts were for the provision of goods — diesel generators, office stationery, information technology hardware, an x-ray machine, an electron microscope, and physical security equipment. One contract was for the provision of goods overseas; and
  - 23 contracts were for the provision of services — banking, administration (project management, switchboard, transcription and travel services), property maintenance (cleaning, repair and engineering services), human resources (payroll and employee assistance services), internal audit, strategic advice, logistics, and property evaluation. Two of these contracts were for the provision of services overseas.



**2.4** Fourteen of the 30 contracts had a fixed cost<sup>19</sup> and 16 were standing offers<sup>20</sup> for the purchase of goods and/or services as required, therefore they did not have an agreed value.

**2.5** Each contract had a contract manager, with time spent administering the contract ranging from five to 100 per cent of his or her time. The larger more complex contracts had full time contract managers.

**2.6** Using data from the sample, the chapter reports findings on the following day-to-day issues:

- payments;
- administration of variations;
- documentation; and
- risk based approach to managing contracts.

## Payments

**2.7** The ANAO reviewed the policies and procedures contract managers followed to ensure invoices were approved and paid in accordance with financial requirements.

**2.8** The ANAO Better Practice Guide, *Developing and Managing Contracts*<sup>21</sup>, states that:

Before payments are made evidence is required that the delegate has certified that goods and services have been received and have met the required standard of performance.

Payments should be made following receipt of a correctly rendered invoice or other statement of expenditure. All necessary authorisations and approvals should have been obtained prior to making the payment.

**2.9** The three agencies' procurement and contract management policies advised on payment of invoices as follows:

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<sup>19</sup> A fixed cost contract is one where the total cost of the contract is specified at contract execution.

<sup>20</sup> A standing offer contract is one where the agency has the option of using the services or obtaining the goods of the service provider as required. Therefore, the total cost of the contract is not specified when the contract is signed.

<sup>21</sup> Australian National Audit Office, op. cit., p. 81.

- the *AFP's National Guideline on procurement and contracting* advised that payments should be made in accordance with the provisions of the contract and only following receipt of a correctly rendered invoice. The Guideline stated that it was a companion to the Commissioner's Financial Instructions, and as such, did not contain specific advice on the payment of invoices;
- the *DFAT Procurement Manual 2005* had a small section on the payment process which advised that the contract manager should be satisfied that the work had been successfully completed before payment, and that invoices should be in accordance with the conditions of the contract. The Manual stated that good administration of a contract included prompt payment of accounts. It further stated that maximum payment terms were not to exceed 30 days from the date of receipt of a correctly rendered invoice; and
- *Austrade's Revised Procurement Guidelines* and the *How to Guide on Contract Management in Austrade* did not provide detailed advice on the payment process, although the *How to Guide* advised that payments should be linked to performance as defined in the contract terms and conditions. The *Guidelines* and *How to Guide* were designed to be read in conjunction with the *Chief Executive's Instructions* and *Administrative Services Manual* which described payment processes.

**2.10** During the contract manager interviews, the ANAO asked contract managers whether they were aware of their agency's policy for invoice payments. Most contract managers demonstrated a reasonable understanding of agency payment policy, including requirements to verify the invoice was correct, obtain payment approval from the appropriate delegate and forward the invoice to the finance area for processing.

**2.11** The CPGs<sup>22</sup> state it is an agency's responsibility to ensure that adequate and appropriate documentation including payment information is kept for each stage of a procurement. To test compliance with this policy, we reviewed the 29 contract files<sup>23</sup> for copies of invoices, and found that 18 files did not have copies. A number of contract managers advised that they did not keep copies

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<sup>22</sup> Department of Finance and Deregulation, op. cit., p. 19.

<sup>23</sup> A file was not maintained for one of the contracts examined in Austrade.

of invoices on file once they sent them to the finance unit for processing and storage.

**2.12** The ANAO reviewed 45 recently paid supplier invoices and found that for 24 invoices there was evidence that the contract manager:

- confirmed that goods or services were received as specified by the invoice and that the invoice was correct for payment;
- obtained approval for payment of the invoice from the correct delegate; and
- forwarded the invoice to the finance area for payment.

**2.13** The ANAO could not confirm for the remaining 21 invoices that they were correctly approved by the delegate. This was because either the agencies could not provide evidence of payment approval occurring electronically or on paper, or the signature on the invoice provided was illegible and the delegate had not printed their name. In some instances, particularly where no paper copy was found, it was possible that there was a record keeping problem. Nevertheless, this potential breach of both Finance Regulations and agency Chief Executive Instructions (CEIs) has implications for both the contract manager and the finance section of the agency if payments were processed without adequate delegate approval.

**2.14** During their interviews, contract managers were asked how they ensured that payments were made on time and that there were no duplicate payments. Only four of the 23 contract managers (17 per cent) interviewed advised that he or she either checked the finance system directly or kept a separate record of payments. The majority (83 per cent) advised that they did not check payments (or did not know how to check payments) and relied on their accounts payable section, as well as the internal checks within the finance system, to ensure payments were accurate.

**2.15** Where contract managers do not access their agency's FMIS, it would be advisable for them to maintain an independent record, either paper or electronically, of invoice payments and other financial approvals to:

- confirm actual payments;
- aid in the detection and prevention of duplicate payments; and
- accurately track contract expenditure (particularly for contracts that run for lengthy periods).

**2.16** The results of the invoice review and responses to the interview questions on payments indicated that many contract managers would benefit from the financial skills training provided by the agency, as many had not. Ideally the training would include agencies confirming which financial controls were most important for contract managers and timely advice from central procurement areas (for example, on guidelines). As noted in Chapter 3, procurement and contract management training in agencies focused on the early stages of the procurement process, so while financial requirements such as FMA Regulations 9 and 10 were included, daily management of the contract, including invoice payment, was not always covered.

**2.17** It would be beneficial for the three agencies to review, and strengthen where necessary, their policies on the payment of invoices, and to ensure their staff understand and comply with them. It would also be beneficial for each of the three agencies to consider the benefits of providing contract managers with access to the FMIS to improve management of payments.

## **Payment policy for small business**

**2.18** Government policy for payments to small businesses requires agencies to adopt maximum payment terms ‘not exceeding 30 days’ from the date of receipt of correctly rendered invoices.<sup>24</sup> Six of the 30 supplier contracts were with small businesses.

**2.19** The Department of Finance and Deregulation defines ‘the day that payment is made’ as:

The day that the agency’s system generates a payment request into the banking system for payment to the small business.<sup>25</sup>

**2.20** The ANAO reviewed 45 invoices. Of these, 36 were found to have been paid within 30 days, while nine were paid after 30 days. Two of the invoices that were paid after 30 days were for small businesses.

**2.21** The ANAO requested information on how the three agencies identified which providers were small businesses. All agencies advised that they asked

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<sup>24</sup> Department of Finance and Deregulation, Finance Circular 2008/10 *Procurement 30 Day Payment Policy for Small Business*, defines a small business as an enterprise that employs less than the full time equivalent of 20 persons on the day that the written contract under which the payment is to be made is entered into, p. 2. Available from: <<http://www.finance.gov.au/publications/finance-circulars/2008/10.html>> [accessed 22 April 2009].

<sup>25</sup> *ibid.*, p. 3.

suppliers to identify themselves as a small business when responding to tenders. The AFP and DFAT flagged small businesses within their FMISs while Austrade manually identified late payments that it made to small businesses.

**2.22** We also examined the results of the Department of Innovation, Industry, Science and Research's annual *Survey of Australian Government Payments to Small Business*.<sup>26</sup> Survey responses for the three audited agencies' timing of payments to small business in 2006–07 and 2007–08 are outlined in Table 2.1.

**Table 2.1**

**Agency compliance with the Government's 30 day payment policy**

| Agency   | 2006–07<br>Percentage not paid<br>in 30 days | 2007–08<br>Percentage not paid<br>in 30 days |
|----------|--|--|
| AFP      | 24   | 31   |
| Austrade | 16   | 9  |
| DFAT     | 6  | 5  |

Source: AFP, Austrade and DFAT responses to the Department of Innovation, Industry, Science and Research *Survey of Australian Government Payments to Small Business*.

**2.23** Table 2.1 shows that Austrade and DFAT reported that they paid a majority of their small business invoices within 30 days. The AFP's reported payment of small business invoices within 30 days decreased from 76 per cent in 2006–07 to 69 per cent in 2007–08. The survey asked if there were any constraints that affected the agency's ability to comply with the 30 day payment policy. The AFP advised that this was due to the accounts payable process being entirely manual, coupled with a large geographical base and a centralised processed centre. The AFP further advised that improvements to its FMIS and related processes had since increased compliance.

**2.24** The implications of agencies not paying correctly rendered invoices from small businesses within 30 days are that they:

- were not complying with Government policy; and

<sup>26</sup> The Department of Innovation, Industry, Science and Research oversees a survey of the performance of all FMA Act departments and material agencies against the Government's policy of adopting maximum payment terms not exceeding 30 days for payment of invoices valued up to and including \$5 million (including GST) for small business.

- could be liable for interest on late payments for written contracts with a value up to \$1 million.<sup>27</sup>

## Monitoring

**2.25** The ANAO's Better Practice Guide, *Developing and Managing Contracts*<sup>28</sup>, states:

Performance management involves:

- Performance monitoring – collecting data on performance;
- Performance assessment – deciding whether performance meets the entity's needs; and
- Taking appropriate action – such as understanding and extending features of good performance, correcting areas of under-performance; or amending contract requirements to meet changing needs.

Performance management must be undertaken throughout the life of the contract and for all contracts, whether straightforward or complex. Along with performance indicators and standards, arrangements for monitoring and assessment should have been set out and agreed in the contract along with action that would result for non performance.

**2.26** As part of the review of individual contracts, the ANAO reviewed:

- agencies' performance monitoring; and
- whether contract files contained evidence of performance monitoring.

**2.27** The ANAO interviewed contract managers to determine how they monitored their suppliers' performance. Of the 75 per cent who advised that they had regular contact with the contractor:

- 36 per cent had formal, regular contact with the contractor, (for example, in documented meetings and by correspondence); and
- 39 per cent had informal but regular contact with the contractor (for example, phone calls and ad hoc face to face meetings).

**2.28** A further 25 per cent did not have any form of communication with the contractor or only had direct contact on an exception basis.

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<sup>27</sup> Department of Finance and Deregulation, op. cit., pp. 4 and 5.

<sup>28</sup> Australian National Audit Office, op. cit., p. 82.

**2.29** Although the amount of performance monitoring varied between contracts, we generally found that larger contracts were monitored more often. Monitoring was principally conducted by staff reviewing monthly reports from suppliers and through meetings.

**2.30** There were some contracts where performance monitoring only occurred on an exception basis when there were issues. This was particularly the case for contract managers who had other work priorities, or who were responsible for smaller and simpler contracts.

**2.31** As part of the file review, the ANAO found that ten of the 29 contract files contained monitoring documentation, such as copies of supplier reports, minutes of meetings or records of email or telephone communications. Three contracts that were rated medium to high risk by the contract manager did not have any record of communication with the supplier available either electronically or on paper.

**2.32** There are implications of not keeping adequate records of communication between an agency and supplier. For example, if a dispute arises the contract manager will not have a clear record of events leading to the difference of views, putting the Commonwealth in a weaker negotiating position.

**2.33** In light of the above information about how agency staff manage contracts on a daily basis, contract managers would benefit from confirming that their monitoring identifies underperformance and services no longer required or which ought to be adjusted in some way. The three agencies also would benefit from strengthening their documentation of communication with suppliers.

## Administration of variations

**2.34** A variation is an amendment to a contract that changes the original terms or conditions of the contract. Variations are usually to alter services, personnel or to change pricing. Variations are also used to extend the contract.

**2.35** Processing and managing variations are key responsibilities of contract managers since they protect agencies from cost overruns and excessive claims. Variations (including extensions) were common in the reviewed contracts.

**2.36** Although many variations are for valid business reasons, the number, timing and nature of variations can also point to a range of issues such as poor contract management practices or where an agency may not have adequately

described the required goods or services during the tendering phase. Each agency had a policy that covered contract variations.

**2.37** Table 2.2 lists the number of contracts that had at least one variation (including extensions) for each agency.

**Table 2.2**

**Number of contracts with at least one variation**

|                                     | AFP | Austrade | DFAT | Total |
|-------------------------------------|-----|----------|------|-------|
| Contracts reviewed                  | 10  | 10       | 10   | 30    |
| Number of contracts with variations | 9   | 7        | 7    | 23    |

Source: ANAO analysis.

**2.38** Table 2.2 shows that over 75 per cent of the reviewed contracts had at least one variation with the majority for a contract extension. Other variations included the addition of services, increased pricing, addition of personnel, and/or reporting. Table 2.3 shows the number of contract variations for each agency and their purpose.

**Table 2.3**

**Number of contract variations and their purpose**

|                                  | AFP | Austrade | DFAT | Total |
|----------------------------------|-----|----------|------|-------|
| Extension of time                | 11  | 5        | 12   | 28    |
| Additional services or personnel | 7   | 1        | 4    | 12    |
| Price change                     | 2   | 1        | 5    | 8     |
| Other                            | 1   | 2        | 4    | 7     |
| Total                            | 21  | 9        | 25   | 55    |

Source: ANAO analysis.

**2.39** Table 2.3 shows that 51 per cent of variations were for an extension to the contract. A further 22 per cent were for additional services or personnel and 15 per cent were a change to pricing. Remaining variations were for other purposes such as amending liability clauses or changes to reporting requirements.

**2.40** 80 per cent of files contained signed correspondence between both parties. However, for some variations to AFP and DFAT contracts there was either no correspondence available in either electronic or paper form showing the agreement of both parties, or documentation was unsigned.



**2.41** One DFAT manager had a simple but useful approach wherein contract changes were summarised at the start of the file in a similar fashion to the contract management checklist mentioned earlier. Adequate contract documentation supports sound administration. Otherwise, for example, if the manager of a contract changes, the new officer may not have a clear record of supplier activity and will spend additional time understanding the nature of the contract and its variations, resulting in higher costs.

### ***Contract extensions***

**2.42** A contract extension is where a contract has an option to extend the agreed term for a further period, and both parties agree to extend for that period. An extension to the contract period can also be accompanied, for example, by a change in price, personnel, and/or services.

**2.43** Of the 28 extensions:

- extension length varied from one month to two years;
- the average extension length was one year;
- 24 extensions were in place before the previous contract expiry date; and
- four extensions were agreed after the expiry date of the contract.

**2.44** Contract extension negotiations that commence late can place the agency in an inferior negotiating position. This is especially so if a contract is critical to an agency's services since it shortens the time available to assess whether it still offers the best value for money. In effect, limited time restricts an agency's ability to assess the need for a contract, test the supplier's price in the current market, and/or modify contractual terms and conditions.

**2.45** Austrade had procedures to monitor contract end dates and to alert staff in enough time to conduct a new procurement process if necessary. The AFP also recognised these issues and — as a result — included in its *National Guideline on procurement and contracting* a requirement for relevant officers to consider these matters at least six months prior to the end of contracts, allowing enough time to assess the need for the contract's continuation and to seek alternatives. However, Table 2.4 shows that some contract managers in the AFP either relied on the contractor to advise on the contract end date or did not monitor the contract end date.

**2.46** During interviews, contract managers were asked how they identified when a contract was nearing completion. Table 2.4 shows their responses.

**Table 2.4****Mechanisms for monitoring contract completion date**

|  | AFP | Austrade | DFAT |
|--|-----|----------|------|
| Number of contract managers interviewed  | 7   | 6        | 10   |
| Contract manager monitors end date   | 3   | 4        | 6    |
| Contract manager relies on the procurement and contract management advisory unit | 0   | 2        | 1    |
| Contract manager relies on contractor to advise end date                         | 1   | 0        | 2    |
| Contract manager does not monitor end date                                       | 3   | 0        | 1    |

Source: ANAO analysis.

**2.47** Table 2.4 shows that 13 of the 23 contract managers advised that they monitored contract end dates themselves, three relied on the agency's contractor to advise them of the completion date, while a further four did not monitor end dates. While there is some benefit in the procurement and contract management advisory unit monitoring and advising on end dates, a core responsibility for contract managers is to understand and monitor key elements of the contracts they are managing, which includes the end dates.

**2.48** We also reviewed each agency's procurement and contract policy and found that Austrade and the AFP included guidance on how to manage an extension. The *AFP National Guideline on procurement and contracting*<sup>29</sup> advised:

Options to extend a contract must be in accordance with the terms and conditions of the current contract, and comply with relevant guidelines or regulations. For example, an extension must comply with the CPGs requirements for demonstrating value for money.

Consideration of a possible extension should commence in sufficient time to allow the alternatives to extension to be considered and possibly exercised. Extensions are not automatic; time must be allowed to prepare for an approach to the market and selection of a successful tenderer before the current contract expires.

**2.49** The ANAO suggests it would be beneficial for DFAT to strengthen advice to staff on management of extensions as the guidance provided in policy documents was limited. The goal would be to provide the contract manager with sufficient time to assess the supplier's performance and, if

<sup>29</sup> Australian Federal Police, December 2008, *AFP National Guideline on procurement and contracting*, p. 36.

necessary, to seek an alternative. The schedule for identification would be dependent upon the size, nature and complexity of the contract.

## Compliance with legislation when making variations

**2.50** The *Financial Management and Accountability Regulations*<sup>30</sup> advise on the approval and authorisation of current and future spending proposals. FMA Regulation 9<sup>31</sup> requires:

An approver must not approve a proposal to spend public money unless the approver is satisfied, after reasonable inquiries, that giving effect to the spending proposal would be a proper use of Commonwealth resources (within the meaning given by subsection 44 (3) of the Act).

*Note:* When this regulation commenced, subsection 44 (3) of the Act defined *proper use* to mean efficient, effective and ethical use that is not inconsistent with the policies of the Commonwealth.

**2.51** FMA Regulation 10<sup>32</sup> requires:

If any of the expenditure under a spending proposal is expenditure for which an appropriation of money is not authorised by the provisions of an existing law or a proposed law that is before the Parliament, an approver must not approve the proposal unless the Finance Minister has given written authorisation for the approval.

**2.52** The need to obtain FMA Regulation 10 authorisation arises in relation to multi-year spending proposals. Where an agency requires FMA Regulation 10 authorisation, it must obtain this from the Finance Minister's delegate before seeking FMA Regulation 9 approval.

**2.53** Contract managers were asked during interviews if they were aware of policies and procedures for obtaining FMA Regulation 9 approval and/or FMA Regulation 10 authorisation. Most contract managers showed at least a basic understanding of them. However, around 30 per cent of contract managers did not know about these two FMA Regulations and whether they applied them.

**2.54** For variations and extensions, the ANAO examined whether the three agencies obtained approval for the spending of public money for both the current and future financial years in compliance with these two Regulations.

**2.55** The ANAO reviewed 55 variations across 23 contracts, and found there were 32 that required FMA Regulation 9 approval and/or FMA Regulation 10

<sup>30</sup> Department of Finance and Deregulation, op. cit., *Financial Management Guidance No. 1*.

<sup>31</sup> Department of Finance and Deregulation, op. cit., *FMA Regulation 9*.

<sup>32</sup> Department of Finance and Deregulation, op. cit., *FMA Regulation 10*.

authorisation. Eleven variations to DFAT and AFP contracts did not have documentation showing that a delegate approved and/or authorised the variation. All of Austrade's variations had the required approvals and authorisations on file.

**2.56** If a contract manager is not aware of, or does not understand, the requirements of FMA Regulations 9 and 10, he or she may amend a contract without obtaining approval or authorisation, subsequently committing the agency to a spending proposal without complying with legislation. Whether the contract manager is the delegate or an advisor to the delegate, he or she must know the Regulations to ensure that they are followed.

**2.57** It is important, therefore, that agencies ensure that staff who are tasked with contract management responsibilities have sufficient knowledge of the relevant regulations to maintain financial control. Agencies will benefit from reviewing and, where necessary, strengthening their training, including refresher training, affirming that their personnel understand and comply with FMA Regulations 9 and 10. The application of these Regulations to contract variations is a relevant focus for agencies determining their compliance with financial management legislation.

## Documentation

**2.58** The contract manager is responsible for ensuring documentation is retained on an official file. While the amount of documentation depends on the nature and complexity of each contract, the contract manager must ensure there is sufficient, easily accessible, documentation retained either electronically or on paper so that staff understand the contract, and that there are records of relevant decisions, including approvals and authorisations, and the basis of those decisions.

**2.59** Ideally the contract file should contain where applicable:

- copies of relevant documents, including a copy of the signed contract and a copy of any extensions and variations;
- copies of approved invoices and/or purchase orders or a clear cross reference to where the record is kept. For example accounts management files or FMIS;
- copies of any contract management plan and risk assessment;
- records of communication between the contractor and the agency; and

- documentation of performance monitoring and reporting, as required by the contract.

**2.60** Each agency's procurement and contract management policy provided advice on the management of documentation. However, this was not always followed. We found that while most contracts had individual paper files for the purpose of maintaining documentation, contents varied from logically structured day-to-day management files through to small incomplete files or, in one case, to no file at all. There were also instances where agencies were unable to find documentation in either paper or electronic form. These findings suggest that agencies can give more attention to their records management.

## Recommendation No. 1

**2.61** The ANAO recommends that agencies review and where required strengthen their compliance with Finance Regulations, with specific reference to contract variations and management of contract records.

### Agencies' responses

#### *Australian Federal Police*

*Agreed.* The AFP acknowledges there are opportunities for improvement in the areas of compliance with Finance Regulations and providing advice to staff who manage contracts. To this end, the AFP has recently updated its guidance documents on contract management and has commenced providing tailored briefings to business areas.

#### *Austrade*

*Agreed.* Austrade agrees with the recommendation and intends to review guidance to contract managers on contract variations. The reviewed and, if needed, improved guidance will focus on value for money in contract extensions, Financial Regulations approval requirements and strengthening records management of decisions and approvals.

#### *Department of Foreign Affairs and Trade*

*Agreed.* DFAT will review its contract management process and procedures and ensure they fully comply with the Financial Regulations.

## Risk based approach to managing contracts

**2.62** Managing risk is an integral part of good management. The size, type, complexity, duration and value of a contract will determine the level of risk management. For example, a small simple contract with little risk to the achievement of agency goals would require less intensive management than a contract for the development of a specialist information technology system costing millions of dollars and having detailed specifications.

**2.63** The ANAO examined how the 23 staff managing the 30 contracts assessed risks. The staff advised that 22 of the 30 contracts were low risk, and eight were medium to high risk, of which three of the eight had a documented risk assessment on file and five did not. Where contract managers identified a contract as being medium to high risk, a structured risk assessment review was warranted. In several of the interviews, contract managers advised that a risk assessment had been undertaken as part of the initial procurement phase and it would be included in the tender evaluation file.

**2.64** Agencies will benefit from periodically reviewing the risk of a contract failing. Consequences of agencies not considering the risks of medium to high risk contracts are that:

- significant risks to service delivery may not be identified;
- policies, procedures and systems are not adequately developed to manage identified risks; and
- the effects of unanticipated events will be more severe and costly to remedy.

**2.65** Common contract risks identified by staff were value for money factors, general non-performance by suppliers, security of staff, and the impact of the current economic slowdown on contractors' ability to continue operating and to meet their contractual requirements. Agency-wide contracting risks are discussed in more detail in Chapter 3.

**2.66** Contract management plans (CMPs) are useful tools for managing risks to the success of contracts. CMPs typically contain a summary of contract details such as key dates and products, roles and responsibilities of personnel in both the agency and supplier, communication and reporting schedules, performance indicators and risk assessments. The detail required in a CMP depends on the risk and complexity of the contract. CMPs may range from a

simple summary of key details to comprehensive documents for more complex contracts.

**2.67** All three agencies encouraged, to varying degrees, the use of CMPs. Most notably, Austrade had developed a comprehensive CMP template. The ANAO found that seven of the 30 contracts utilised a CMP. In many instances the contract manager indicated that the contract did not warrant a lengthy CMP. The ANAO recognises that CMPs were not always necessary given the relative size, type and complexity of the contracts in the sample. However, given issues with monitoring and records discussed earlier in this chapter, the ANAO suggests that agencies consider introducing a simplified CMP or checklist (such as the example at Appendix 3). Staff could use the aid to record risks and the contractor's performance for contracts with a relatively lower risk profile.

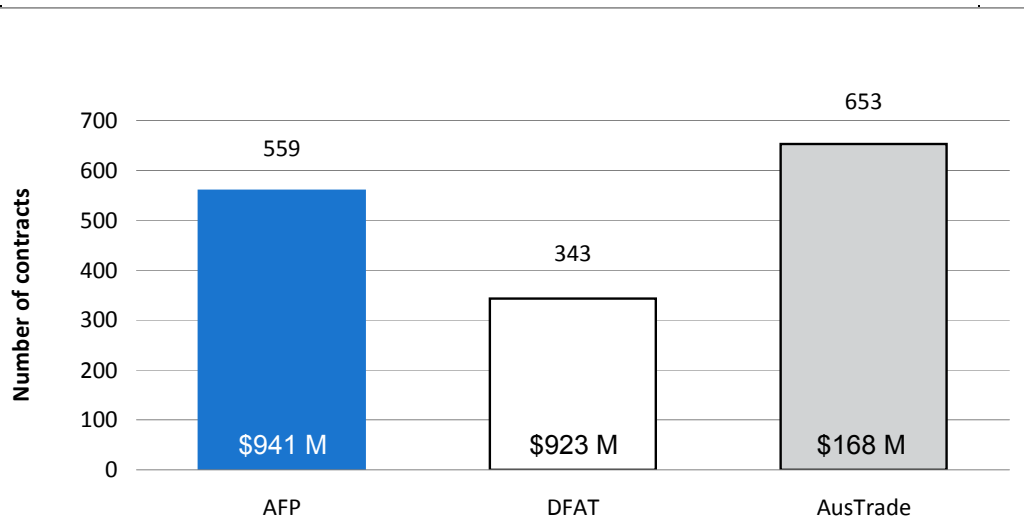
# 3. Agencies’ management of their contract populations

Chapter 3 examines AFP’s, Austrade and DFAT’s approaches to managing their contract populations.

3.1 Contract management is a significant business activity in the three agencies audited — AFP, Austrade and DFAT. Annually the three agencies manage hundreds of contracts worth millions of dollars and have hundreds of contract managers and administrators.

3.2 We reviewed each agency’s contract register to determine the number of active contracts and their value. Figure 3.1 shows, for each agency, the number of contracts and their total value on 30 June 2008.

Figure 3.1  
Number of contracts and their proposed expenditure at 30 June 2008<sup>33</sup>



Source: ANAO analysis of agency contracting information.

3.3 The DFAT data excludes overseas posts contracts for which DFAT maintained a separate register. The latter contained data on 550 leases worth approximately \$47.5 million.

<sup>33</sup> ANAO analysis of AFP, Austrade and DFAT contract register data.



**3.4** Agencies managing a broad range of contracts often appoint a senior manager with the responsibility for driving agency-wide contract management. Ideally, this approach is underpinned and supported by a centralised unit within each agency that provides guidance and monitors and reports on agency-wide contract performance.

**3.5** This chapter examines each agency's approach to managing its contract population, and reports findings on:

- agencies' approaches to contract management;
- management of contract population data;
- monitoring and reporting;
- risk management;
- policy; and
- training.

## Agencies' approaches to contract management

**3.6** To oversee the administration of contracts and assist agency contract managers, each audited agency had established a procurement and contract advisory unit. Each advisory unit:

- provided procurement and contracting advice and training;
- developed and maintained procurement and contracting policy and guidelines; and
- managed the agency's contract register and prepared reports for internal and external audiences.

**3.7** Table 3.1 describes the nature of each agency's procurement and contract advisory unit.

**Table 3.1**

**Procurement and contract advisory units**

| Agency   | Procurement and contract advisory unit  |
|----------|---|
| AFP      | <ul style="list-style-type: none"><li>• 21 staff of which seven conducted procurement, six managed contracts, and eight assisted with logistics such as provision of motor vehicles.</li><li>• 40 per cent of the unit's time was spent on contract management.</li></ul> |
| Austrade | <ul style="list-style-type: none"><li>• 4 staff. One full time resource dedicated to contract management and reporting.</li><li>• 40 per cent of the unit's time was spent on contract management.</li></ul>  |
| DFAT     | <ul style="list-style-type: none"><li>• 5 staff.</li><li>• 30 per cent of the unit's time was spent on contract management.</li></ul>   |

Source: ANAO analysis.

**3.8** The three agencies had slightly different approaches to manage their contracts:

- In the AFP a majority of contracts were managed by staff operating throughout the agency, with some agency-wide contracts managed by the procurement and contract advisory unit. In addition, three areas<sup>34</sup> had procurement and contract advisory support teams.
- In DFAT contracts were managed by staff operating throughout the department. In addition, DFAT had placed specialist contract managers in four of its divisions. The role of these staff varied and ranged from overall responsibility for the management of all contracts in that location to providing assistance to specific contract managers as required.

**3.9** In Austrade all contracts were managed by staff operating throughout the agency.

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<sup>34</sup> The areas were the AFP's Information Services, International Deployment Group, and ACT Policing units.

## Management of contract population data

**3.10** The Joint Committee of Public Accounts and Audit, *Report 379, Contract Management in the Australian Public Service*, recommended that agencies must establish and maintain contract registers.<sup>35</sup> The Government agreed in principle with this recommendation.<sup>36</sup> In addition, the ANAO's Better Practice Guide, *Developing and Managing Contracts*<sup>37</sup> advises that contract registers are most useful when they:

- contain relevant details such as start and finish dates, contractor name, value and duration;
- identify responsibility for maintaining the register;
- have procedures for maintaining the accuracy and completeness of its data; and
- have controls to ensure unauthorised staff do not have access to contract details.

**3.11** To manage their contracts agencies need systems to collect, manage and disseminate information for internal and external purposes. The principal method in each agency for recording contract information was through the contract register and financial management information systems (FMISs).

**3.12** In addition, each of the agencies shared general information on contract management through their intranet sites, bulletins, and through conducting training.

### Agency contract registers

**3.13** Each agency had different procedures for entering and maintaining data in their contract registers:

- in the AFP, contract data was checked and entered by a member of the procurement and contract management unit;

<sup>35</sup> Joint Committee of Public Accounts and Audit, *Report 379, Contract Management in the Australian Public Service*, p. iii. Available from: <http://www.aph.gov.au/house/committee/jpaa/contracts/contents.htm> [accessed 3 May 2009].

<sup>36</sup> Available from: [http://www.aph.gov.au/house/committee/jpaa/contracts/gr\\_379.pdf](http://www.aph.gov.au/house/committee/jpaa/contracts/gr_379.pdf) [accessed 11 May 2009].

<sup>37</sup> Available from: [http://www.anao.gov.au/uploads/documents/Developing\\_and\\_Managing\\_Contracts.pdf](http://www.anao.gov.au/uploads/documents/Developing_and_Managing_Contracts.pdf) [accessed 31 March 2009].

- DFAT contract managers entered data into the contract register, where it was checked and then approved by the procurement and contract advisory units. DFAT staff located overseas biannually send documents to the procurement and contract advisory unit; and
- Austrade contract managers entered data into the contract register, where it was checked and approved by the procurement and contract advisory unit. Austrade's overseas staff were able to remotely access and enter data into their contract register.

**3.14** Contract registers were principally used to meet external reporting requirements such as reporting on AusTender,<sup>38</sup> for Senate Order reporting,<sup>39</sup> and for listing consultancies on agency websites and in annual reports. Other purposes included identifying responsibility for procurement of goods and services, and for recording and management of contract details.

**3.15** Each agency's register recorded information such as contractor name, contract start and finish dates, and value.<sup>40</sup> We compared file information on the 30 contracts against information in the contract register. Of the 30 contracts reviewed, 14 were incorrectly listed in the contract register. The most common errors were incorrect start and/or finish dates and variations to contract duration or costs, limiting the usefulness of the register to support monitoring and reporting.

**3.16** The ANAO also noted that financial data recorded in the contract registers related to different types of information, leading to some ambiguity in its interpretation. For example, register users would not be clear if the data was for potential or confirmed expenditure. Additionally, in some cases, the financial data was for the current year commitment or expenditure, while other data was for the life of the contract (that is, commitment or expenditure over several years). It would be beneficial for the three agencies to review and improve their processes and practices for confirming the accuracy and completeness of their data.

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<sup>38</sup> AusTender is the Australian Government's central location for publication and reporting of information relating to procurement activity. The Gazette Publishing System requires agencies to include data in AusTender on all contracts (including consultancy contracts) greater than \$10 000.

<sup>39</sup> The Senate Order requires agencies to place on the Internet a list of all contracts to the value of \$100 000 or more that have been entered into or are still current at the end of each calendar and financial year.

<sup>40</sup> Each agency's contract register did not identify whether the contracts were funded by departmental or administered funds.

**3.17** At the time of the audit, none of the registers were connected to the agencies' financial management information systems (FMISs).<sup>41</sup> The benefits of an agency linking its contract register and FMIS include:

- enabling more accurate and efficient reporting of contracts;
- enabling contract goods and/or services and actual payments to be tracked against contracts, improving agencies' ability to manage expenditure and to monitor variations and under and overspending;
- improving visibility of existing supply and service contracts across different units; and
- simplified monitoring of contract expiry dates.

**3.18** The audit also found that view access in AFP was limited to the procurement and contract unit and to the originator of the contract record. In DFAT access was limited to the procurement and contract unit and approved staff in the area from which the contract originated. This inhibited the sharing of information, which could lead to the agency unknowingly employing more than one supplier for the same services. This was more likely to occur in large entities where the existence of duplicate services would be less obvious. The importance of maintaining the security and confidentiality of some information may limit access to some information in registers;

**3.19** The ANAO concluded that the three agencies contract registers had the basic characteristics required to meet their external reporting requirements. However, as the three agencies managed large numbers of contracts, they would benefit from reviewing whether they can strengthen quality assurance of their data, make better use of information in their registers and FMISs, and where they have not already done so, from reviewing the costs and benefits of linking their contract registers and FMISs.

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<sup>41</sup> The AFP has since incorporated its contract register into its Financial Management Information System. DFAT is considering linking theirs, while AusTrade has assessed the resources required to link the two systems and found that presently it would be too expensive to connect them.

## Monitoring and reporting

**3.20** The ANAO's Better Practice Guide, *Developing and Managing Contracts*<sup>42</sup> advises:

Better practice entities incorporate reporting on contracting activity into their regular management reporting arrangements. This should involve the development of a number of contracting performance measures and the periodic measurement and reporting against them as an integral part of the entity's management reporting regime. This will assist in reinforcing the importance of good contracting practices and also provide assurance to senior management on the agency's performance in this area, including its compliance with policy and reporting requirements.

**3.21** The level and nature of agency-wide contract performance monitoring is most useful when aligned with the significance of an agency's purchase of goods and services from the profit and not-for-profit sectors. For example, an agency managing hundreds of contracts that vary in purpose and type would benefit from a more comprehensive monitoring regime than an agency with a small number of simple contracts that requires single payments.

**3.22** The three agencies conducted some agency-wide monitoring of contracts through, for example:

- management of their risk, fraud and business plans;
- monitoring annual procurement proposals; and
- their procurement and contract advisory units monitoring and answering questions from contract managers.

**3.23** The three agencies also prepared some reports on their overall contract management performance. Reports included:

- results of their monitoring on compliance with government policy: for example, Certificates of Compliance,<sup>43</sup> and compliance with the

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<sup>42</sup> ANAO Better Practice Guide—*Developing and Managing Contracts*, p. 5. Available from <[http://www.anao.gov.au/uploads/documents/Developing\\_and\\_Managing\\_Contracts.pdf](http://www.anao.gov.au/uploads/documents/Developing_and_Managing_Contracts.pdf)> [accessed 31 March 2009].

<sup>43</sup> Certificates of Compliance are useful tools for monitoring agency compliance with legislation. The Chief Executives of agencies under the FMA Act are required to provide a completed Certificate to their portfolio minister and a copy to the Minister for Finance and Deregulation. The Certificate consolidates a range of existing agency reporting requirements, and is intended to provide an overview of the agency's compliance with the Government's financial management framework. Details of any breaches must be provided with the Certificate, focusing on remedial measures that are to be taken to improve agency compliance.

Government's policy of payment of invoices within 30 days for small business;<sup>44</sup>

- financial commitments registers for current and future years; and
- budget versus actual expenditure.

**3.24** While overall expenditure on contracts was monitored as part of the budgeting process, there was little agency-wide monitoring of suppliers' performance. Although each agency had large numbers of contracts, none periodically monitored contracting costs, numbers of extensions and variations, and contracts finished on time and within budget compared with those finished over time and budget. Extending their performance monitoring, for example, through analysis of the contract register or surveys, to encapsulate trends in contract management performance will benefit central procurement areas, better positioning the agency to assess risks to effective contract management and target improvements accordingly.

**3.25** The three agencies would benefit from determining what additional information would assist senior management to better understand the success of contracting and therefore assist in decisions. For example, periodic review of the:

- numbers of contracts completed on time and within budget would assist management to better understand the degree of success of the agency's procurement and contracting;
- numbers and types of variations. This could inform the agency of the extent to which original procurement processes were unusual or insufficient. If options to extend are regularly enacted this may indicate that the agency is not testing the market when it perhaps should;
- numbers of contracts with the same supplier, and contracts for the supply of the same goods or services with different suppliers. This data would inform future decisions regarding packaging of services and to obtain best overall value for money; and
- the proportions of high, medium and low risk contracts, and variations in these contracts over time.

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<sup>44</sup> Finance Circular 2008/10, Procurement 30 Day Payment Policy for Small Businesses. Available from <<http://www.finance.gov.au/publications/finance-circulars/2008/10.html>> [accessed 23 April 2009].

**3.26** Periodically reviewing performance for various groups of contracting activity (for example, administered versus departmental expenditure, different programs or different divisions) will help procurement and contract advisory units and senior management to identify key areas to focus improvements. An example where agency-wide monitoring has improved agency performance is in payments to small and medium-sized businesses. Another example of how the collection and analysis of data can inform senior management on the performance of their contracting is shown in Table 3.2. The Table shows that Agency A’s procurement and contract management were more likely to be working well, in comparison with Agency B’s procurement and contract management which required attention.

**Table 3.2**

**Contracts completed on time and within budget**

| Agency A   | Agency B   |
|--|--|
| 90 per cent of contracts completed on time       | 40 per cent of contracts completed on time       |
| 80 per cent of contracts completed within budget | 45 per cent of contracts completed within budget |

Source: ANAO.

**3.27** Agencies managing a broad range and a large number of contracts would benefit from such periodic review to assist in targeting improvements in processes and practices. As such, the ANAO has identified this issue in Recommendation No.2 at the end of this chapter.

**Risk management**

**3.28** Contracting risks in the three agencies were principally identified and managed by agency staff in business areas, with risks escalated through the hierarchy on an exception basis. Through this approach, several major contracting risks were incorporated into their risk management plans.

**3.29** Common risks in risk management plans included the risk of non-compliance with government and agency policy, record keeping, and training. Other contracting risks identified in their risk management plans are listed in Table 3.3.



**Table 3.3****Agency-wide contract management risks**

| Agency   | Contracting risks  |
|----------|--|
| AFP      | <ul style="list-style-type: none"> <li>• Monitoring of capital expenditure against budgets.</li> <li>• Procurement time frames.</li> </ul>   |
| Austrade | <ul style="list-style-type: none"> <li>• Performance Measurement Framework (corporate and individual) fails to drive desired behaviours and/or ability to meet external reporting requirements.</li> <li>• Failure to effectively identify and manage instances of fraud.</li> </ul> |
| DFAT     | <ul style="list-style-type: none"> <li>• Failure to meet budgetary targets.</li> </ul>   |

Source: ANAO analysis.

## Policy

**3.30** A key means to address contract management risks is through the development and implementation of policy and training. Well designed contract management policy is a source of information and guidance for staff in the performance of their roles and responsibilities.

**3.31** Contract management policies can:

- assist agencies to make informed decisions;
- provide a basis for agencies to administer their contracts through defining, for example:
  - roles and responsibilities;
  - approval and other processes to be followed;
  - data management;
  - the management of contract extensions and variations;
  - performance monitoring and reporting requirements; and
  - records management requirements.

**3.32** The review of agencies principal procurement and contract management policy found each agency had adequate policies that were in alignment with the government procurement framework, including the CPGs. We found, however, that agencies could strengthen their guidance on contract variations, relationship management and records management. Additionally, references to relevant financial policies, such as the CEIs, could be improved.

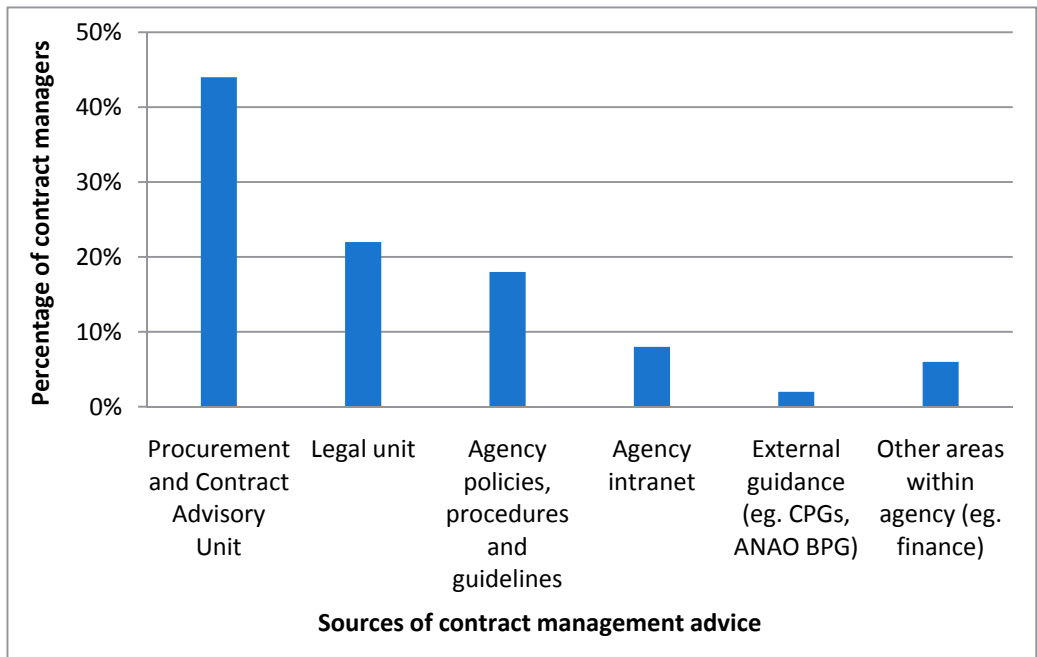
As an example to support this observation, DFAT’s principal policy on contracting did not cover the management of variations (specifically extensions). A consequence was that staff had limited guidance on how to manage variations.

**Sources of contract management advice**

**3.33** Contract managers used a range of sources for management advice, while principally relying on their procurement and contract advisory unit. Figure 3.2 shows the different sources of guidance which contract managers advised they accessed.

**Figure 3.2**

**Sources of advice**



Source: ANAO analysis.

**3.34** Seventy five percent of contract managers stated that they were aware of agency contract management policies (usually on the agency intranet). However, as indicated in Figure 3.2, most contract managers preferred to contact the procurement and contract advisory unit for guidance and support.

### *Administering contract management advice*

**3.35** As mentioned earlier, the three agencies' procurement and contract advisory units provided advice to agency-wide staff involved in managing contracts. The ANAO examined how each unit provided advice to staff.

**3.36** DFAT's procurement and contract advisory unit maintained a database, accessible to all staff in the unit, that recorded answers and responses to questions on contract management. In Austrade, responses to procurement and contract management queries were cleared through one officer to ensure consistency.<sup>45</sup> The AFP's and Austrade's procurement and contract advisory units did not have a process or practice that allowed staff to share information and good practice (for example, a contract manager forum or network that met regularly).

**3.37** Due to the large numbers of contract managers and administrators in the three agencies, it would be worthwhile for them to consider sharing information and ideas. This sharing would assist staff to develop networks, and to consider different approaches to addressing problems and issues. Also, agencies' initiatives could play a role in the wider administration of government procurement and contracting through sharing of ideas and experiences, thereby assisting in revisions of government-wide policies.

## **Training**

**3.38** An important element of contract management is that managers are trained to understand government and agency requirements. Agencies can assess their training requirements by identifying the nature of their contracting environment and reviewing their current training programs to identify gaps in coverage. Training, including refresher courses, should be provided regularly and attendance records should be kept.

**3.39** Training in each agency covered a range of topics including:

- agency procurement policy and procedures;
- the Commonwealth procurement framework;
- government and agency financial policy (such as delegations and Certificates of Compliance); and

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<sup>45</sup> The position was that of Procurement and Contracts Manager.

- legal aspects of procurement including intellectual property, liability and risk, security and confidentiality, dispute resolution and termination, and agreements.

**3.40** All three agencies conducted training on procurement and contract management in group sessions, one on one training and, in Austrade, through on-line learning modules accessible via the intranet. Of the 23 contract managers:

- 43 per cent had procurement training and 23 per cent had contract management training (training for both may have been combined); and
- 39 per cent of contract managers had completed other forms of in-house training that covered aspects of contract management, including induction, risk or financial management.

**3.41** Four AFP, two Austrade and two DFAT contract managers indicated that they had not completed any contract management training. While most of these officers had experience in the subject area of the contract, there were two who indicated they had limited experience and no training.

**3.42** The majority of training was on the early stages of the procurement cycle covering tendering and contract development. The consequence was that staff knowledge of contract management requirements was limited. This was supported, as outlined in Chapter 2, by the results of the invoice review and contract managers' responses to the questions on payments. These responses suggested that compliance with legislation and agency policy was an area where many staff would benefit from training.

**3.43** Also, the ANAO noted that while the contract managers would have benefitted from an overview of the procurement process, most of the contract managers in DFAT and the AFP were not involved in the early stage of procurement. As discussed in Chapter 2, additional training in policies and procedures, risk management and the management of extensions and variations would assist staff.

## Recommendation No. 2

**3.44** The ANAO recommends that agencies managing a broad range and large number of contracts:

- (a) develop a systematic approach to disseminating information on contract management; and
- (b) periodically review aggregate contract management information to identify trends in contract management performance and to use the data to improve contract management approaches.

### Agencies' responses

#### *Australian Federal Police*

*Agreed.* As noted in the proposed report, the AFP has moved its contract register into its Financial Management Information System. The AFP is currently at the testing and validation stage of enabling business areas to access enhanced reporting through its business warehousing (business intelligence) system.

#### *Austrade*

*Agreed.* Austrade agrees with the recommendation. Austrade has already developed an online training module for the delivery of procurement and contracts management training and will periodically review the content to ensure its currency.

Austrade will consider further improvements to information available to contracts managers including a new frequently asked questions section to be available electronically on Austrade's Intranet.

Austrade is currently scoping requirements to enhance monitoring of contract management performance.

#### *Department of Foreign Affairs and Trade*

*Agreed.* In disseminating information on contract management, DFAT commits to provide guidance to users. The audit has helped identify opportunities for improvements. The Department will review mechanisms such as e-learning systems, formal and informal briefings and training sessions, information forums and improved user guides and templates.

The recommendation to review aggregate contract management information will require a significant overhaul of the systems currently used by DFAT to collate and disseminate contract data. As outlined within the report, the

Department is currently considering incorporating its contract register into its Financial Management Information System. This is expected to produce additional capability to review more effectively aggregate contract information to enable additional reporting capacity to senior management.

## Finance's role

**3.45** Finance and the ANAO have a strong interest in sound contract management and have a range of publications to assist agencies to understand contract and procurement issues. In February 2007, Finance and the ANAO jointly published a Better Practice Guide, *Developing and Managing Contracts*.<sup>46</sup> The Guide identified issues and considerations for agencies in developing and managing contracts.

**3.46** Finance organises procurement discussion forums and distributes a procurement bulletin on Commonwealth procurement. Additional information on Finance's activities is in Appendix 4. While some briefings and presentations may have introduced some aspects of contract management, it is not a direct focus. The forums are opportunities for agencies to share information on similarities and differences in their approaches to contract management. Consequently, the ANAO suggests that Finance consider the potential benefits of including, in its procurement forums, sessions for agencies to discuss and share ideas on contract management. Such sessions may also inform the Government's Procurement Coordinator of matters relevant to this new role.

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Ian McPhee

Auditor-General

Canberra ACT

25 November 2009

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<sup>46</sup> Australian National Audit Office, op. cit.

# Appendices





## Appendix 1: AusTender contracting data<sup>47</sup>

### Government Contracts 2007–08<sup>48</sup>

|           | Total  | SME    | %    | Other  | %    |
|-----------|--------|--------|------|--------|------|
| Value \$m | 26 361 | 9743   | 37   | 16618  | 63   |
| Number    | 69 493 | 37 878 | 54.5 | 31 615 | 45.5 |

Source: Government contracts: ratio of goods to services 2007–08

|           | Total  | Goods  | %  | Services | %  |
|-----------|--------|--------|----|----------|----|
| Value \$m | 26 361 | 9988   | 38 | 16 373   | 62 |
| Number    | 69 493 | 26 572 | 38 | 42 921   | 62 |

### Contracts reported by the top 10 FMA agencies

| Agency  | 2007–08       |                  | Rank    |         |         |
|---|---------------|------------------|---------|---------|---------|
|   | Value \$m     | % of total value | 2007–08 | 2006–07 | 2005–06 |
| Department of Defence                                       | 8898          | 33.8             | 1       | 1       | 1       |
| Defence Materiel Organisation                               | 5629          | 21.4             | 2       | *N/A    | *N/A    |
| AusAID  | 1694          | 6.4              | 3       | 6       | 10      |
| Department of Immigration and Citizenship                   | 1589          | 6.0              | 4       | 12      | 7       |
| Centrelink  | 1394          | 5.3              | 5       | 4       | 4       |
| Department of Health and Ageing                             | 694           | 2.6              | 6       | 8       | 32      |
| Australian Taxation Office                                  | 655           | 2.5              | 7       | 7       | 6       |
| Australian Federal Police                                   | 597           | 2.3              | 8       | 11      | 14      |
| Department of the Environment, Water, Heritage and the Arts | 562           | 2.1              | 9       | 17      | 24      |
| Australian Customs Service                                  | 481           | 1.8              | 10      | 2       | 3       |
| <b>Total</b>  | <b>22 193</b> | <b>84.2</b>      |         |         |         |

<sup>47</sup> Available from: <<http://www.finance.gov.au/publications/statistics-on-commonwealth-purchasing-contracts/index.html>> [accessed 6 May 2009].

<sup>48</sup> The Commonwealth Procurement Guidelines defines a small to medium size enterprise, SME, as an Australian or New Zealand firm with fewer than 200 full time equivalent employees, p. 7. Available from <<http://www.finance.gov.au/publications/fmg-series/docs/CPGs-2008.pdf>> [accessed 27 April 2009].

## Summary of agency contracting 2007–08

| Summary                      | Total value \$m | % of total value |
|------------------------------|-----------------|------------------|
| Total of top 10 agencies     | 22 198          | 84               |
| Total of other agencies      | 4163            | 16               |
| <b>Total of all agencies</b> | <b>26 361</b>   | <b>100.0</b>     |

\*Note: Prior to 2007–08, Department of Defence and Defence Materiel Organisation contracts were reported under a single agency, the Department of Defence.

## Appendix 2: ANAO's reports and publications on contracting

The following is a selection of ANAO reports tabled in the last three years which include contract management issues.

### 2008–2009

- ANAO Audit Report No.27 2008–09, *Management of the M113 Armoured Personnel Carrier Upgrade Project*.
- ANAO Audit Report No.24 2008–09, *The Administration of Contracting Arrangements in Relation to Government Advertising to November 2007*.
- ANAO Audit Report No.19 2008–09, *CMAX Communications Contract for the 2020 Summit*.
- ANAO Audit Report No.5 2008–09, *The Senate Order for Departmental and Agency Contracts (Calendar Year 2007 Compliance)*.
- ANAO Audit Report No.2 2008–09, *Tourism Australia*.

### 2007–2008

- ANAO Audit Report No.33 2007–08, *The National Capital Authority's Management of National Assets*.
- ANAO Audit Report No.23 2007–08, *The Management of Cost Recovery By Selected Regulators*.
- ANAO Audit Report No.11 2007–08, *Management of the FFG Capability Upgrade*.
- ANAO Audit Report No.9 2007–08, *Defence Material Organisation Major Projects Report 2007–08*.

### 2006–2007

- ANAO *Better Practice Guide–Developing and Managing Contracts*, February 2007.  
ANAO Audit Report No.24 2006–07, *Customs' Cargo Management Re-engineering Project*.

## Appendix 3: Contract Management Checklist

### Contract Management Checklist

| Contract Management Checklist  |   |
|--|---|
| Contractor   | Name:<br>ABN:<br>Address:<br>Contractor Representative:<br>Position:<br>Telephone:<br>Facsimile:<br>Email:<br>SME: Yes/No   |
| Contract Details:  | Specification or scope of work.   |
| Contract Manager:  |   |
| Contract Sponsor:  | Note: the Contract Sponsor should have sufficient delegations to approve contract invoices for payment and any variations to the contract under FMA Regulations 9 and 10. |
| Contract Start Date:   |   |
| Contract End Date:   |   |
| Contract extension options:  | Note: Possible contract extensions should be examined at least 6 months before the contract end date to give the agency time to go out to market if required.             |
| Payment schedule:<br><br>Total contract value<br><br>Payment arrangements: | Detail how often payments are to be made (eg. on completion of deliverables, at milestones or monthly).   |
| Invoice verification:  | Who will confirm invoices are correct? (should be Contract Manager).<br>Who will authorise payment of invoices? (should be Contract Sponsor).                             |
| Incentive or Penalty Payments:   | List any incentive or penalty payments that have been applied.  |
| Milestones:  |   |
| Performance Indicators:  |   |
| Reporting Requirements:  | Format/frequency.   |

|                             |   |
|-----------------------------|---|
| Communication Protocols:    | How regularly will agency and contractor communicate and format of communication?   |
| Risk assessment and review: | <p>What is the risk assessment at the beginning of the contract?</p> <p>Regularly review contract to determine if risk status has changed in any significant way.</p> |

Source: ANAO

## **Appendix 4: The Department of Finance and Deregulation's activities in procurement**

Finance advised that it had hosted nine Procurement Discussion Forums (Forums) since November 2007. During this time a diverse range of procurement related topics was presented. The Forums:

- provided information on recent developments and/or initiatives;
- provided regular briefs on ongoing issues; and
- included presentations by other agencies. No commercial organisations had been invited to present.

Up until 2009, the Forums were held irregularly. In 2009 the Forums have been held every second month.

Attendance varies widely depending on participant interest in topics to be discussed and competing events. Typically 100 and 200 people attend each Forum.

There were 1115 officers on Finance's Forum distribution list. Membership of the mailing list is limited to Australian Public Service officers.

Finance also distributes a Procurement Bulletin to persons listed on the Forum distribution list. The Bulletin:

- is distributed monthly;
- provides similar information to that provided through the Discussion Forums;
- provides those not attending the Forums with contact details on matters discussed; and
- provides an avenue for agencies to seek information from other agencies on procurement related matters.

Finance also publishes guidance on procurement. The following is a list of those publications.

### **The Good Procurement Practice Guidance series of publications**

- No. 1 Chief Executive's Instructions and Operational Guidelines for Procurement, November 2006.
- No. 2 Preparing and Maintaining an Annual Procurement Plan, November 2006.
- No. 3 Cooperative Agency Procurement, December 2007.
- No. 4 Establishing and Using Panels, December 2007.
- No. 5 Establishing and Using Multi-Use Lists, December 2007.
- No. 6 Providing Feedback and Handling Complaints, December 2007.

### **Guidance Material Co-produced by the Department of Finance and Deregulation with the ANAO**

- *ANAO Better Practice Guide—Developing and Managing Contracts – Getting the Right Outcome Paying the Right Price*, February 2007.

## Appendix 5: International audit reports on contract management

### **United Kingdom National Audit Office: *Central government's management of service contracts***<sup>49</sup>

This report examined how well government organisations were managing their service contracts, assessed against the good practice framework for contract management which was developed at the outset of the audit.

It found that organisations were not always according contract management the priority it deserved and were not always allocating appropriate skills and resources to the management of their service contracts.

### **United Kingdom National Audit Office: *Good practice contract management framework***<sup>50</sup>

In conjunction with the audit above, the UK National Audit Office also produced a good practice framework for contract management. The framework is a good practice guide for managing a broad range of contracts. It is particularly relevant for contracts where services are to be delivered over a long period of time (five years plus) where customers need to ensure that service levels and value for money are maintained over the duration of the contract.

The framework covers the stage where a contract has been signed and the service is up and running. It includes activities that organisations should consider when planning and delivering contract management, how to evaluate the risk and value opportunities inherent in contracts and how to develop contract management plans and priorities.

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<sup>49</sup> United Kingdom National Audit Office, *Central government's management of service contracts*, December 2008. Available from: [http://www.nao.org.uk/publications/0809/central\\_governments\\_managemen.aspx](http://www.nao.org.uk/publications/0809/central_governments_managemen.aspx), [accessed 26 March 2009].

<sup>50</sup> United Kingdom National Audit Office *Good practice contract management framework*, December 2008. Available from: [http://www.nao.org.uk/publications/0809/central\\_governments\\_managemen.aspx](http://www.nao.org.uk/publications/0809/central_governments_managemen.aspx) [accessed 26 March 2009].



## **Office of the Auditor General of Canada: *Contracting for Goods and Services – Northwest Territories***<sup>51</sup>

This audit reviewed a random sample of contracts to assess whether contracts were awarded in accordance with applicable laws, regulations and policies. It also assessed whether there was an adequate contracting framework and quality assurance process to help ensure that government departments and territorial corporations awarded and administered their contracts for goods and services in accordance with government policies and regulations.

The audit found that the policy framework was adequate but missing some elements. Policy and guidance was dispersed through many documents making it difficult for government employees to be aware of all components of the contracting process. The audit also found that a majority of contracts had deficiencies in their administration including exceeding spending authority and paying for goods and services before the contract was issued.

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<sup>51</sup> Office of the Auditor-General Canada, '*Contracting for Goods and Services – Northwest Territories*', June 2009. Available from <[http://www.oag-bvg.gc.ca/internet/english/nwt\\_200906\\_e\\_32627.html](http://www.oag-bvg.gc.ca/internet/english/nwt_200906_e_32627.html)> [accessed 20 August 2009].

## Appendix 6: Agencies' responses

*This Appendix contains general comments received on the audit report that are not shown in the body of the report.*

Each of the agencies involved in the audit were provided with the opportunity to comment on the proposed audit report in accordance with the provisions of section 19 of the Auditor-General Act 1997.

Agencies' responses to the recommendations have been included in the main body of the report under the subheading 'Agencies' responses' directly following the recommendation.

General responses are reproduced below.

### **Australian Federal Police**

The AFP agrees with the report's conclusion that its contract management processes and practices provide an adequate level of support for the provision of goods and services and that its procurement and contract management team provides a satisfactory level of support for AFP staff to manage small to medium size contracts.

By way of additional commentary, the AFP advises that it has significantly improved its compliance with the Government's 30 day payment policy for financial year 2008–2009 and that 96 per cent of payments to small business are made within 30 days.

### **Austrade**

Over the past two years Austrade has actively focused on improving the quality of its procurement and contract management practices. Measures have included the development of online training modules, development of templates and guidance material for staff, introduction of a contracts register with access available to all staff and engaging a full time Quality Assurance staff member to monitor all contract material and to meet publishing obligations.

Austrade will continue to identify and implement improvements to its contract management practices including the recommendations included in this report.

## **Department of Foreign Affairs and Trade**

The Department welcomed the review of its contract management processes. The findings will be instrumental in refining and focusing the direction of process improvements in DFAT's contract management. DFAT agrees with all the ANAO recommendations.

# Series Titles

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**ANAO Audit Report No.1 2009–10**

*Representations to the Department of the Treasury in Relation to Motor Dealer Financing Assistance*

Department of the Treasury

Department of the Prime Minister and Cabinet

**ANAO Report No.2 2009–10**

*Campaign Advertising Review 2008–09*

**ANAO Audit Report No.3 2009–10**

*Administration of Parliamentarians' Entitlements by the Department of Finance and Deregulation*

**ANAO Audit Report No.4 2009–10**

*The Management and Processing of Annual Leave*

**ANAO Audit Report No.5 2009–10**

*Protection of Residential Aged Care Bonds*

Department of Health and Ageing

**ANAO Audit Report No.6 2009–10**

*Confidentiality in Government Contracts – Senate order for Departmental and Agency Contracts (Calendar Year 2008 Compliance)*

**ANAO Audit Report No.7 2009–10**

*Administration of Grants by the National Health and Medical Research Council*

**ANAO Audit Report No.8 2009–10**

*The Australian Taxation Office's Implementation of the Change Program: a strategic overview*

**ANAO Audit Report No.9 2009–10**

*Airservices Australia's Upper Airspace Management Contracts with the Solomon Islands Government*

Airservices Australia

Department of Infrastructure, Transport, Regional Development and Local Government

**ANAO Audit Report No.10 2009–10**

*Processing of Incoming International Air Passengers*

Australian Customs and Border Protection Service

**ANAO Audit Report No.11 2009–10**

*Garrison Support Services*

Department of Defence

**ANAO Audit Report No.12 2009–10**

*Administration of Youth Allowance*

Department of Education, Employment and Workplace Relations

Centrelink

**ANAO Audit Report No.13 2009–10**

*2008–09 Major Projects Report*

Defence Materiel Organisation

# Current Better Practice Guides

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The following Better Practice Guides are available on the Australian National Audit Office website.

## SAP ECC 6.0

|  |           |
|--|-----------|
| Security and Control   | June 2009 |
| Preparation of Financial Statements by Public Sector Entities                                  | June 2009 |
| Business Continuity Management   |           |
| Building resilience in public sector entities  | June 2009 |
| Developing and Managing Internal Budgets   | June 2008 |
| Agency Management of Parliamentary Workflow  | May 2008  |
| Public Sector Internal Audit   |           |
| An Investment in Assurance and Business Improvement  | Sep 2007  |
| Fairness and Transparency in Purchasing Decisions  |           |
| Probity in Australian Government Procurement   | Aug 2007  |
| Administering Regulation   | Mar 2007  |
| Developing and Managing Contracts  |           |
| Getting the Right Outcome, Paying the Right Price  | Feb 2007  |
| Implementation of Programme and Policy Initiatives:  |           |
| Making implementation matter   | Oct 2006  |
| Legal Services Arrangements in Australian Government Agencies                                  | Aug 2006  |
| Administration of Fringe Benefits Tax  | Feb 2006  |
| User-Friendly Forms  |           |
| Key Principles and Practices to Effectively Design and Communicate Australian Government Forms | Jan 2006  |
| Public Sector Audit Committees   | Feb 2005  |
| Fraud Control in Australian Government Agencies  | Aug 2004  |
| Better Practice in Annual Performance Reporting  | Apr 2004  |
| Management of Scientific Research and Development  |           |
| Projects in Commonwealth Agencies  | Dec 2003  |
| Public Sector Governance   | July 2003 |
| Goods and Services Tax (GST) Administration  | May 2003  |

|  |           |
|--|-----------|
| Building Capability—A framework for managing learning and development in the APS | Apr 2003  |
| Administration of Grants   | May 2002  |
| Performance Information in Portfolio Budget Statements                           | May 2002  |
| Some Better Practice Principles for Developing Policy Advice                     | Nov 2001  |
| Rehabilitation: Managing Return to Work  | June 2001 |
| Building a Better Financial Management Framework                                 | Nov 1999  |
| Building Better Financial Management Support                                     | Nov 1999  |
| Commonwealth Agency Energy Management  | June 1999 |
| Controlling Performance and Outcomes   | Dec 1997  |
| Protective Security Principles<br>(in Audit Report No.21 1997–98)                | Dec 1997  |

