

The Auditor-General  
Audit Report No.31 2009–10  
Performance Audit

# **Management of the AusLink Roads to Recovery Program**

**Department of Infrastructure, Transport, Regional  
Development and Local Government**

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of Australia 2010

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Canberra ACT  
22 April 2010

Dear Mr President  
Dear Mr Speaker

The Australian National Audit Office has undertaken a performance audit in the Department of Infrastructure, Transport, Regional Development and Local Government in accordance with the authority contained in the *Auditor-General Act 1997*.

Pursuant to *Senate Standing Order 166* relating to the presentation of documents when the Senate is not sitting, I present the report of this audit and the accompanying brochure. The report is titled *Management of the AusLink Roads to Recovery Program*.

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

Yours sincerely

A handwritten signature in black ink, appearing to read '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

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# Abbreviations

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ACLG	Australian Classification of Local Governments
ACT	Australian Capital Territory
ALGA	Australian Local Government Association
ANAO	Australian National Audit Office
APMS	AusLink Program Management System (see IMS)
ARRB	Australian Road Research Board
AusLink Act (or the Act)	<i>AusLink (National Land Transport) Act 2005</i>
BITRE	Bureau of Infrastructure Transport and Regional Economics
CAATS	Computer Assisted Auditing Techniques
CEO	Chief Executive Officer
DITRDLG	Department of Infrastructure, Transport, Regional Development and Local Government
DOTARS	Department of Transport and Regional Services
FAGs	Financial Assistance Grants provided under the <i>Local Government (Financial Assistance) Act 1995</i> .
FRLI	Federal Register of Legislative Instruments
IMS	Infrastructure Management System (formerly APMS)
JCPAA	Joint Committee of Public Accounts and Audit
LGA	Local Government Authority
NSW	New South Wales
NT	Northern Territory
PBS	Portfolio Budget Statements
QLD	Queensland
R2R	Roads to Recovery
R2R Act	<i>Roads to Recovery Act 2000</i>
SA	South Australia



SPPs	Specific Purpose Payments made under section 96 of the Constitution.
TAMS	ACT Department of Territories and Municipal Services
TAS	Tasmania
VIC	Victoria
WA	Western Australia
WALGA	Western Australian Local Government Association

# Glossary

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Administrative Guidelines	Administrative Guidelines published pursuant to section 11 of the R2R Act. The purpose of the Guidelines was to explain how the initial R2R Program worked.
AusLink Roads to Recovery (AusLink R2R)	Second round of Roads to Recovery. This Program was delivered through Part 8 of the AusLink Act.
Chainage	Linear measurement along a road from a known point.
Funding Conditions	<i>Conditions Applying to Payments</i> determined by the Minister under section 90(1) of the AusLink Act and/or the conditions applying to the grant made under the Supplementary Roads to Recovery Program.
Notes on Administration	For AusLink Roads to Recovery and the Supplementary AusLink Roads to Recovery Program, issued by DITRDLG (replaced the R2R Administrative Guidelines).
Quarterly Report	Quarterly Reports (of actual and forecast expenditure for each project) submitted by LGAs provided the basis on which R2R payments were made to LGAs.
R2R Annual Report	LGAs were required by the Funding Conditions to submit Annual Reports to DITRDLG to account for the use of R2R Standard and Supplementary Program funds and certify that the LGA had complied with the Funding Conditions.
Sheeting/Resheeting	Where additional gravel is added on top of an existing road.
Standard Program	AusLink Roads to Recovery Program.
Supplementary Program	AusLink Supplementary Roads to Recovery Program.
Works Schedule	A proposal setting out the works for which R2R funding is sought.

## **Summary and Recommendations**



# Summary

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## Introduction

1. Of the nation's 810 000 kilometres of public roads, more than 650 000 kilometres (80 per cent) are local roads within the responsibility of local government.<sup>1</sup> Approximately one-third of these roads are sealed, with the remainder being unsealed (unformed, formed or gravel roads).<sup>2</sup>
2. The AusLink Roads to Recovery Program is an administered program within Outcome 1 ('Assisting the Government to provide, evaluate, plan and invest in infrastructure') of the Department of Infrastructure, Transport, Regional Development and Local Government (DITRD LG). Roads to Recovery is the largest investment in local roads ever undertaken. In total, over 13 years, \$4.18 billion<sup>3</sup> is to be paid by the Australian Government to local government for expenditure on the construction and maintenance of roads.
3. There have been four Roads to Recovery (R2R) Programs. The initial Program was established by the *Roads to Recovery Act 2000* (R2R Act) and provided \$1.2 billion over four years. It commenced in early 2001 as a single intervention to address the concern that local government road infrastructure was near the end of its economic life and its replacement was beyond the capacity of local government. The initial program was the subject of an Australian National Audit Office (ANAO) performance audit tabled in March 2006.<sup>4</sup>
4. A second four-year program commenced in July 2005, as part of the AusLink Land Transport Initiative. The AusLink R2R Standard Program was established under the *AusLink (National Land Transport) Act 2005* (AusLink Act or the Act)<sup>5</sup> and provided \$1.23 billion. There was also a separate, but related,

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<sup>1</sup> AusLink Annual Report 2007–08, p. 23.

<sup>2</sup> DITRD LG, *Local Government National Report: 2006–07 Report on the Operation of the Local Government (Financial Assistance) Act 1995*, p. 7. At the time of the ANAO audit, the 2007–08 Report had not been presented to the Parliament.

<sup>3</sup> For the composition of the \$4.18 billion see Figure 1.1 in Chapter 1 of this audit report.

<sup>4</sup> ANAO Audit Report No.31 2005–06, *Roads to Recovery*, Canberra, 1 March 2006.

<sup>5</sup> In June 2009, the *Nation Building Program (National Land Transport) Act 2009* (Nation Building Act) replaced the AusLink Act as the relevant land transport legislation.

AusLink R2R Supplementary Program concurrently in operation from June 2006 to June 2009 that provided \$307.5 million (the third program).

5. A fourth program commenced under the Nation Building banner<sup>6</sup> on 1 July 2009 and will continue through to 30 June 2014. The Nation Building R2R Program will provide \$1.75 billion.

6. It is the second and third R2R Programs (the AusLink R2R Programs) that are the subject of this performance audit.

## **AusLink R2R Programs**

7. Under the AusLink R2R programs, a total of \$1.537 billion was paid to more than 720 Local Government Authorities (LGAs) between July 2005 and June 2009. The distribution of R2R funds between the States and Territories was determined at the Ministerial level. In arriving at the actual distribution, consideration was given to the historical results from using the Financial Assistance Grants (FAGs) identified for local roads; and population and length of road under the control of the local government, with each of these two statistics weighted equally.<sup>7</sup> In turn, the allocation of funds within each State was determined using the formula applied by State Grants Commissions for FAGs identified for local roads.

8. Under the Standard Program, each Local Government Authority (LGA) was guaranteed its full life of program allocation by 30 June 2009, subject to the submission of satisfactory documentation such as work schedules and Quarterly and Annual Reports. Almost all LGAs received their full R2R allocation. Larger LGAs generally received an annual allocation capped at one quarter of their life of program allocation. However, subject to meeting certain conditions, smaller LGAs could access their full allocation at the start of the program. LGAs were required to spend all of their Standard Program funds by 31 December 2009.

9. The May 2006 Budget announced that a further \$307.5 million would be provided in 2005–06 as a supplement to the AusLink R2R Standard Program. Under the Supplementary Program, each funding recipient received a grant

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<sup>6</sup> Programs previously administered under the name 'AusLink' were renamed as *Nation Building* programs in 2008–09. Source: DITRDLG Annual Report 2008–09, p. 22.

<sup>7</sup> Consideration was also given to the long standing concern of South Australia that it received a disproportionately low level of funding under the FAGs identified for local roads.

equal to one quarter of its life of program allocation under the Standard Program. The funds were distributed and administered under similar funding conditions to those of the Standard Program, with funding recipients being required to acquit their project expenditures by submitting Quarterly and Annual Reports. However, unlike the Standard Program, funding recipients received their Supplementary Program allocations as a one off payment in June 2006, and were required to expend these funds by 30 June 2009.

10. The focus of the R2R Program is the renewal of local roads to meet social and economic needs. Most of the funds are provided in the form of grants direct to LGAs. These grants, together with other aspects of the program, are administered by a manager and up to three staff in the South East Roads Branch within the Canberra offices of DITRD LG. The small number of staff reflects the following program delivery decisions made at the time the program was first introduced:

- funds were to be paid directly to LGAs;
- project priorities were the choice of LGAs; and
- the process by which grants were paid to the LGAs was to be simple, with appropriate audit and accountability systems and arrangements put in place to ensure that there is due recognition by LGAs of the Commonwealth's contribution to local road projects.

## Audit scope and objectives

11. The audit scope covered the management of the AusLink R2R Standard Program and the AusLink R2R Supplementary Program. The scope did not include management of the Nation Building Roads to Recovery Program, which has only recently commenced. The audit objectives were to:

- assess the effectiveness of the management of the AusLink Roads to Recovery Program;
- assess the delivery of the program and management of the funding, including the extent to which the program has provided additional (rather than substitute) funding for land transport infrastructure; and
- identify opportunities for improvements to the management of the program.

12. A key part of the audit involved examination of the use of, and accountability for, R2R funds by a representative sample of 41 LGAs from four

States/Territories (representing almost six per cent of all funding recipients and eleven per cent of total funding provided under the program). This work included site inspections of more than 560 R2R funded projects, analysis of financial and other reports provided by the 41 LGAs to DITRDLG, and substantiation of the amounts charged to the program for selected projects. To supplement the audit sample, ANAO analysed data in the department's Infrastructure Management System (IMS).

## Overall conclusions

**13.** The R2R Program encompasses the largest investment in local roads undertaken by the Australian Government. By the time the Nation Building R2R Program concludes in June 2014, some \$4.18 billion will have been paid over 13 years to local government for expenditure on the construction and maintenance of roads.

**14.** As part of the AusLink R2R Standard and Supplementary Programs audited by ANAO, more than \$1.5 billion was paid to local government for expenditure on the construction and maintenance of roads in respect of more than sixteen and a half thousand projects. Almost all LGAs received their full R2R allocation under the Standard Program and all LGAs received their Supplementary Program allocations as an up front, once only payment. Accordingly, the key aspect of the programs relating to distribution of funds to local government and LGAs using these funds for road works have been effectively administered.

**15.** In terms of the benefits from the R2R Program, a fundamental principle underpinning the program is that the funding provided to LGAs was to be additional to existing road funding. Accordingly, LGAs are required to maintain their own spending on local roads and report their performance in this regard to the department. Over time, the expenditure maintenance obligation placed on LGAs has been made less demanding but still, there have been significant numbers of LGAs that have not maintained their own expenditure in one or more years (and some LGAs have not maintained their own expenditure in any year). In these circumstances, the administrative practice adopted has been to waive the requirement where a satisfactory explanation has been provided and ask that the shortfall be made up in later years; but this often does not occur.

**16.** Another key aspect of program design was to pay LGAs quarterly in advance based on LGAs reporting the expenditure to date and forecast



expenditure for the next three months in respect to each project they were undertaking under the program. Paying up to three months in advance was seen as necessary so that LGAs did not have to transfer funds from roadworks funded from their own resources.<sup>8</sup> However:

- there have been many instances of LGAs being paid more than three months in advance due to factors such as accelerated funding during the last quarter of each financial year (so as to fully spend the annual program allocation) notwithstanding that these payments did not reflect LGA cash flow needs, and LGAs overstating their actual expenditure and/or submitting unreliable expenditure forecasts;
- experience with the program has shown that many LGAs do not require payments to be made in advance, such that 54 per cent of all payments made under the Standard Program have been made in arrears (and 90 per cent of LGAs were paid in arrears in one or more quarters); and
- the cost to the Commonwealth of advance payments remains considerable (up to \$16.3 million over the life of the AusLink R2R Standard Program).<sup>9</sup>

17. Reflecting the judgement that LGAs were best placed to make decisions on road investment at the local level, the grant payment and acquittal processes were designed to be simple. However, there have been a range of important funding conditions where LGA compliance has been less than satisfactory. In this respect, and without detracting from the responsibility of individual LGAs to adhere to the prescribed funding conditions, there would be benefit in the department adopting a range of cost-effective strategies aimed at improving understanding of, and adherence to, program funding conditions and administrative arrangements by LGAs and their auditors. ANAO has made one recommendation to this end.

18. In addition, in light of experience as to how the program has operated over its first ten years, there would be benefit in the department reviewing key elements of the program design so as to confirm their continuing

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<sup>8</sup> In practice, DITRD LG scheduled the payments to LGAs for around the middle of the relevant quarter.

<sup>9</sup> ANAO's audit of the initial R2R Program estimated the interest cost of payments in advance to be between \$8.4 million and \$19.4 million (ANAO Audit Report No. 31 2005-06, op. cit., p. 29).

appropriateness, or otherwise proposing variations (recognising that decisions on program design are a matter for Government). In particular, there is value in consideration being given to:

- the formula that has been used to allocate R2R funding to individual LGAs in light of evidence of capacity constraints that affect the ability of some LGAs to both spend their R2R funds as well as maintain their own source expenditure on roads; and
- paying LGAs in advance rather than in arrears given that many LGAs have not sought payments to be made in advance and a significant proportion of advance payments that have been made have remained unspent by the respective LGAs for considerable periods of time.

19. DITRDLG has substantially implemented all recommendations made during the previous audit aimed at improving the administration of the program. In light of further experience with the program, ANAO has made a further two recommendations directed towards enhancing the administration of program accountability arrangements and strengthening the program governance framework.

## Key findings by Chapter

### Governance Framework (Chapter 2)

20. Key elements of the governance framework in place for the AusLink R2R Programs were:

- the AusLink Act;
- a list of funding recipients and the amounts they were to receive<sup>10</sup>;
- *Conditions Applying to Payments* (the Funding Conditions) determined under section 90 of the Act; and
- *Notes on Administration* issued by the department, for use by LGAs in conjunction with the Funding Conditions.

21. The documented governance arrangements reinforced the considerable autonomy granted to LGAs in their delivery of R2R-funded works. This included LGAs deciding which projects they would undertake using their

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<sup>10</sup> Determined by legislative instrument under Section 87 of the Act.

allocation of R2R funds, subject to providing DITRDLG with a works schedule. Works schedules are used by the department to assess whether the proposed works were eligible under the AusLink Act, as well as to satisfy itself that payments were not being made more than three months in advance of the planned commencement date of the works (the works schedules were to include start and completion dates). Notwithstanding that the department reinforced to LGAs on a number of occasions and in various ways the importance of works schedules being kept up to date, ANAO's examination of 41 LGAs revealed that, in many instances, the works schedules did not include the required information, or were inaccurate.

22. ANAO made a number of suggestions to DITDRLG regarding enhancements that could be made to IMS to facilitate LGA compliance with the works schedule requirements and monitoring by the department.<sup>11</sup> More broadly, there would also be benefits from DITRDLG:

- fully implementing the planned program of financial audits of LGAs (undertaken by a contractor) given that those audits that were conducted (less than two thirds of the audits that were proposed) identified that LGAs had not complied with 38 per cent of those requirements that were examined; and
- giving greater emphasis to structured program risk management and evaluation, given that the R2R Program has been in operation for more than ten years.

## **Financial Management (Chapter 3)**

### *Payment arrangements*

23. Almost all LGAs received their full R2R allocation under the Standard Program and all LGAs received their Supplementary Program allocations as an up front, once only payment.

24. Payments under the Standard Program were to be made quarterly in advance and LGAs were required under the funding conditions to spend payments within six months of receipt. However, a waiver was issued by DITRDLG if a satisfactory explanation was provided for not spending the

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<sup>11</sup> These included additional IMS fields to separately capture some types of information and generation of system reports to prompt follow-up action where required.

funds within this timeframe. ANAO's analysis of IMS data identified 435 instances (nearly nine per cent of all payments made under the Standard Program) where payments were not spent within six months of receipt.<sup>12</sup> The total amount of unspent R2R funds held by LGAs for more than six months as at the end of each quarter averaged more than \$3 million, but at times was as high as \$6.9 million. Where an LGA did not adhere once to the six months rule, it was common for this to be repeated.<sup>13</sup>

25. As a corollary, notwithstanding that payment in advance was intended to be the norm under the program, 90 per cent of LGAs were paid in arrears during one or more quarters, after expending their own funds on their R2R projects. More than one-half of all R2R payments made under the Standard Program were reimbursements to LGAs, comprising one in every three quarterly reports submitted to DITRDLG.

#### *Spending of program allocations*

26. Notwithstanding there was funding certainty and LGAs had four years in which to plan their roadworks and undertake the expenditure of funds, the life of program allocations for many LGAs exceeded their capacity to spend, on eligible roadworks, the funding provided.<sup>14</sup> In this context, as would be expected, over the life of the program, the number of LGAs that received more than their annual allocation declined year on year, as progressively more LGAs received their full program allocation. However, this trend was reversed in the final year of the program, when around one-half of all LGAs were in 'catch-up' mode and needed to increase their R2R expenditure. In this respect, some LGAs received up to almost 90 per cent of their full allocation as their final payout under the program.

27. This situation should also be considered in the context of the relatively high incidence of LGAs that have difficulty maintaining their own source

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<sup>12</sup> An additional 53 potential instances were also identified. However, there was insufficient information in DITRDLG's records to assess whether funds had or had not been expended within six months in these cases, as the respective LGAs had not submitted their quarterly reports for the relevant periods.

<sup>13</sup> Multiple breaches (up to seven times) were incurred by 96 per cent of all LGAs that had not complied with the six months rule. DITRDLG also made 14 payments to LGAs totalling nearly \$2.4 million which should not have been made, because the LGAs were in breach of the six months rule at the time and had not been issued with waivers.

<sup>14</sup> ANAO Audit Report No. 31 2005-06 also noted that there was a disproportionately large payout of program funds to LGAs in the final year of the initial R2R Program.

expenditure on roads at the same time as spending their R2R allocation.<sup>15</sup>

## **Program Outcomes and Accountability (Chapter 4)**

28. Of the approximately 16 750 road projects funded over the life of the AusLink R2R Program, most involved reconstruction, rehabilitation and widening of local roads; sealing along sections of gravel roads; sheeting and re-sheeting gravel roads with a new surface; or bridge or drainage works. In this context, LGAs have reported to DITRDLG that the key outcomes they achieved with their R2R funds have been: better asset management; improved road safety; and improved heavy vehicle access.

29. The grant payment and acquittal processes were, by design and in accordance with Government intentions, simple, with a range of post-payment audit and accountability arrangements in place. However, administration of the various accountability mechanisms for the significant quantum of program funding has not achieved full compliance. In particular:

- some seven per cent of LGAs did not agree to adhere to the funding conditions for the Supplementary Program prior to being paid a total of more than \$10 million in June 2006;
- LGAs are required to erect signs in the prescribed format at each end of the works when the work began, to be maintained for one year after the project was completed, but the required signs were not in place for 22 per cent of projects inspected by ANAO that were required to display signage;
- although Annual Reports from LGAs to DITRDLG provide key information on the use of funds, outcomes achieved and whether LGAs have maintained their own spending on roads, a large proportion (60 per cent) of Annual Reports have been provided late, with some

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<sup>15</sup> In addition, in March 2009, ALGA wrote to the Minister for Infrastructure, Transport, Regional Development and Local Government requesting that consideration be given to widening the definition of 'roads' to include 'other transport infrastructure' as: 'A number of councils in urban areas have identified other transport infrastructure being of a higher priority than roads and have raised the possibility of using their R2R Program funding for those priorities'.

20 per cent of the Reports containing errors and omissions of varying significance<sup>16</sup>;

- until recently, Annual Program Reports to the Parliament, which are required by the land transport legislation, have not been prepared in a timely manner, with the AusLink series of reports providing little in the way of reporting on the actual operation of the program; and
- the department did not establish and report against suitable performance indicators for the program.

### *Maintaining LGA expenditure on local roads*

30. The R2R Program was intended to address the problem that a significant amount of local government road infrastructure was reaching the end of its economic life and its replacement was beyond the capability of local government. It was for this reason that the funding provided under the program was to be additional to existing road funding. However, data sourced from the Bureau of Infrastructure Transport and Regional Economics (BITRE) within DITRD LG indicates that national net expenditure on roads by local government was higher in each of the first four years of the R2R Program (2000–01 to 2003–04) than in any of the next three years (2004–05 to 2006–07, the most recent data available at the time of the audit).

31. Consistent with the fundamental importance to the R2R Program that funds provided by the Commonwealth be additional to existing road funding, provisions were included in the legislation, the R2R funding conditions and the Notes on Administration requiring each individual LGA to maintain its own source expenditure on constructing and maintaining local roads. In relation to this obligation, changes to the expenditure maintenance requirements introduced at the start of the Standard Program placed the department in a significantly improved position to monitor compliance by LGAs with their expenditure maintenance obligations.<sup>17</sup> However:

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<sup>16</sup> These included important parts of the form not being completed; the required certification not being provided (including incorrect years being specified for the expenditure maintenance certificate and errors in calculating averages); reports prepared on an accruals rather than cash basis; and missing or incorrectly worded audit certificates.

<sup>17</sup> In particular, LGAs were required to specify the amount spent using their own resources in each year (from 2000–01) together with the reference average amount. However, if DITRD LG had also required LGAs to report their expenditures for the years 1998–99 and 1999–2000, it would have been able to determine each LGA's reference amount under the initial R2R Program, thus enabling it to monitor and quantify any cost shifting from LGAs to the Commonwealth since inception of the program.

- over time, changes to the program administrative arrangements have made the expenditure maintenance obligation less onerous for LGAs<sup>18</sup>; and
- the reporting by LGAs of their own source expenditure has been error prone<sup>19</sup> and has been inconsistent with other reporting on LGA roads expenditure.<sup>20</sup> In this respect, each year the department has written to numerous LGAs to clarify or correct apparent anomalies in reported expenditure figures for the current year or previous years. However, the department has not amended its administrative arrangements to require that LGAs have their own source expenditure included within that part of their R2R Annual Report that is audited.<sup>21</sup>

32. Most LGAs reported to DITRDLG that they had spent more than the reference amount, on roads, from their own resources, for each year of the Standard Program. However, each year, up to nine per cent of LGAs reported that they had not met the expenditure maintenance requirements. For example, in 2005–06, overspends totalled more than \$560 million, compared to underspends of almost \$28 million. Where LGAs reported that they have not met the expenditure maintenance obligation, DITRDLG's practice has been to issue a waiver of the expenditure maintenance requirement. No requests for a waiver have been refused, and more than 275 waivers have been issued.

33. DITRDLG advised non-compliant LGAs that they were expected to make up for a shortfall in the years following a breach of the expenditure maintenance requirements. Of the 53 LGAs with shortfalls in 2005–06, eight

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<sup>18</sup> For example:

- LGAs were able to reduce the standard five-year reference period to three-years by excluding the years with the highest and lowest expenditure; and
- LGAs were taken to have met the expenditure maintenance requirement where the average expenditure in that year and the previous year (or previous two years) exceeded the reference average (this is referred to as the averaging provisions).

<sup>19</sup> In this respect, a series of financial audits of LGAs commissioned by DITRDLG found that 29 per cent of the LGAs examined had misreported their own source expenditure for one or more years.

<sup>20</sup> Specifically, data compiled by the West Australian Local Government Association (WALGA) indicated that less than one quarter of the annual own source expenditure figures reported to the department by WA LGAs during 2000–01 to 2007–08 matched the figures reported to WALGA. In addition, nearly 90 per cent of LGAs did not maintain their own source expenditure in one or more years, some LGAs did not meet the requirement in any years, and 30 per cent of LGAs had not made up the cumulative shortfall (approximately \$56 million) as at 30 June 2008.

<sup>21</sup> Own source expenditure figures are reported by LGAs in Part 3 of the R2R Annual Report. The independent audit by the LGA's financial auditor covers Part 1 only.

LGAs were abolished and 18 LGAs again had shortfalls in one or more of the next three years. Of these 18 LGAs, 15 had not made up the cumulative shortfall at the time of the audit.<sup>22</sup> Similarly, around one-half of the LGAs that had not met the expenditure maintenance requirement in 2006–07 had not made up the shortfall at the time of the audit.

## Summary of agency response

**34.** DITRD LG's formal comments on the proposed audit report were as follows:

The audit found that the distribution of Australian Government funding under the Roads to Recovery Program to local government and local government authorities using these funds for road works have been effectively administered.

The audit also found that the Department of Infrastructure, Transport, Regional Development and Local Government (the Department) has substantially implemented all recommendations made during the previous audit and there is no suggestion that the administration of the program by the Department is not efficient and effective.

The Government's policy objective of providing funding directly to local government for the improvement of the local road system throughout Australia is being met and there is no evidence in the report that suggests systemic problems on the part of the Department or Local Government Authorities.

The audit raises some issues where consideration of future program arrangements may be warranted and the Department will work with local government authorities to achieve a greater consistency of understanding and interpretation of the program's administrative requirements.

The Department agrees to all of the recommendations.

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<sup>22</sup> At this time, a number of LGAs had not yet submitted their 2008–09 R2R Annual Reports.



# Recommendations

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Set out below are ANAO's recommendations and DITRDLG's abbreviated responses. More detailed responses are shown in the body of the report immediately after each recommendation.

**Recommendation No.1**  
**Para 2.82**

ANAO *recommends* that the Department of Infrastructure, Transport, Regional Development and Local Government strengthen the governance framework for the Roads to Recovery Program, including by:

- a) better resourcing the existing program of contracted financial audits of Local Government Authorities so that the program of audits is able to be fully delivered; and
- b) giving greater emphasis to structured risk management and program evaluation.

**DITRDLG Response:** Agree.

**Recommendation No.2**  
**Para 3.93**

ANAO *recommends* that, in light of the experience to date with the program, the Department of Infrastructure, Transport, Regional Development and Local Government review and advise Ministers on program design arrangements that will promote timely local government expenditure of Roads to Recovery funding on road work that is additional to that which would have otherwise occurred.

**DITRDLG Response:** Agree.

**Recommendation No.3**  
**Para 4.16**

ANAO *recommends* that the Department of Infrastructure, Transport, Regional Development and Local Government improve accountability to the Parliament for the Roads to Recovery Program by setting and reporting in its departmental Annual Report against an effectiveness target for the program.

**DITRDLG Response:** Agree.

**Recommendation  
No.4**

**Para 4.99**

ANAO *recommends* that, given the importance to both the Roads to Recovery and Strategic Regional Programs of Local Government Authorities maintaining their own level of expenditure on roads, the Department of Infrastructure, Transport, Regional Development and Local Government:

- a) obtain greater assurance over the accuracy of own source roads expenditure reported to it by Local Government Authorities by requiring these figures to be included in the scope of the Audit Certificate included with each Authorities' Annual Report on the use of program funds; and
- b) develop a more effective range of sanctions to apply in circumstances where own source expenditure has not been maintained, with a particular focus on those Local Government Authorities that frequently fail to maintain their annual expenditure and/or that do not make up shortfalls in later years.

**DITRDLG Response:** Agree.

## **Audit Findings and Conclusions**



# 1. Introduction

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*This chapter includes an outline of the AusLink Roads to Recovery Program and describes the audit objectives and approach. It also summarises progress made by the department in addressing recommendations from the previous ANAO audit on the initial Roads to Recovery Program.*

## Background

**1.1** The AusLink Roads to Recovery Program is an administered program within Outcome 1 ('Assisting the Government to provide, evaluate, plan and invest in infrastructure') of the Department of Infrastructure, Transport, Regional Development and Local Government (DITRD LG). Roads to Recovery (R2R) is the largest investment in local roads ever undertaken by an Australian Government. In total, over 13 years, \$4.18 billion<sup>23</sup> is to be paid to local government for expenditure on the construction and maintenance of roads.

**1.2** There have been four Roads to Recovery Programs. The initial Program commenced in early 2001 as a single intervention to address the concern that local government road infrastructure was near the end of its economic life and its replacement was beyond the capacity of local government. The initial Program was the subject of an Australian National Audit Office (ANAO) performance audit tabled in March 2006.<sup>24</sup>

**1.3** A second four-year program commenced in July 2005, as part of the AusLink Land Transport Initiative.<sup>25</sup> There was also a separate, but related, Supplementary Program concurrently in operation from June 2006 to June 2009.

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<sup>23</sup> For the composition of the \$4.18 billion see Figure 1.1.

<sup>24</sup> ANAO Audit Report No.31 2005–06, *Roads to Recovery*, Canberra, 1 March 2006.

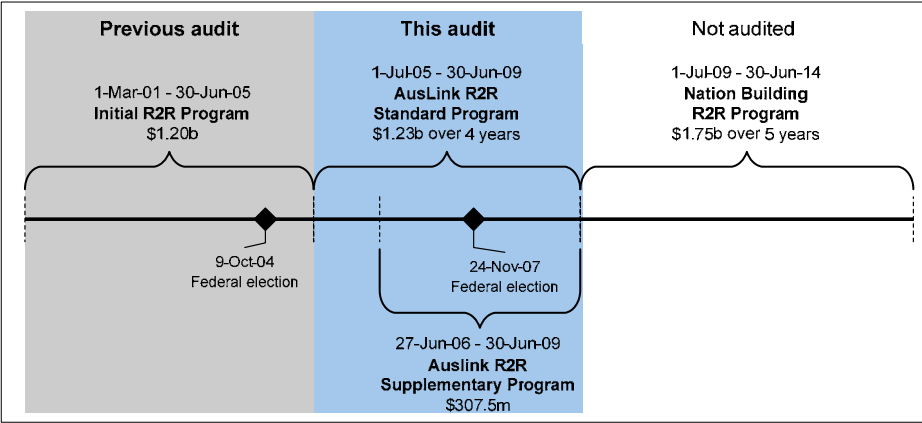
<sup>25</sup> With effect from 1 July 2004, the then Australian Government introduced a new approach to planning, funding and delivering land transport infrastructure. This approach was known as AusLink and was described as: 'the Australian Government's policy for improved planning and accelerated development of Australia's land transport infrastructure. It will revolutionise the planning and funding of Australia's national roads, railways and inter-modal terminals by taking a long-term, strategic approach to future needs.'

1.4 A fourth program commenced under the Nation Building banner<sup>26</sup> on 1 July 2009 and will continue through to 30 June 2014.

1.5 It is the second and third R2R Programs that are the subject of this performance audit. Figure 1.1 provides a timeline of the various R2R Programs and indicates performance audit coverage by ANAO.

**Figure 1.1**

**Roads to Recovery Program timeline**



Source: ANAO analysis of DITRDLG data.

**Program administration arrangements**

1.6 The focus of the R2R Program is the renewal of local roads to meet social and economic needs.<sup>27</sup> Most of the funds are provided in the form of grants direct to Local Government Authorities (LGAs). These grants, together with other aspects of the program, are administered by a manager (also responsible for the Black Spots Program), two other full time staff and one part time officer in the South East Roads Branch within the Canberra offices of DITRDLG. As part of the previous audit, DITRDLG advised ANAO in December 2005 that the small number of staff reflected the Government’s policy of ‘arms length’ administration of the program.

1.7 ANAO was also informed at that time that it was not the Government’s intention that DITRDLG closely oversight LGA operations. Instead, the

<sup>26</sup> Programs previously administered under the name ‘AusLink’ were renamed as *Nation Building* programs in 2008–09. Source: DITRDLG Annual Report 2008–09, p. 22.

<sup>27</sup> *Roads to Recovery Program Annual Report 2003–04*, p. 1.

obligation to meet the program funding conditions was placed with LGAs, including through the annual reporting and funding acquittal processes. DITRDLG further advised that the legislation governing the program was framed around the following program delivery decisions made by the then Government:

- funds were to be paid directly to LGAs;
- project priorities were the choice of LGAs; and
- the process by which grants were paid to the LGAs was to be simple, with appropriate audit and accountability systems and arrangements put in place to ensure that there is due recognition by LGAs of the Commonwealth's contribution to local road projects.

1.8 DITRDLG manages the program through the Infrastructure Management System (IMS),<sup>28</sup> which was implemented in December 2007 for the AusLink Investment, Black Spot and Roads to Recovery Programs. This provides 'an on line reporting and payment claims system for States, Territories, and Local Councils and the Australian Rail Track Corporation', that 'also facilitates improved program and financial management for the Department'.<sup>29</sup>

## Initial Roads to Recovery Program

1.9 The initial Program followed concerns raised by local government at the inaugural local roads congress held at Moree in New South Wales in March 2000.<sup>30</sup> The initial Program was established by the *Roads to Recovery Act 2000* (R2R Act).<sup>31</sup> A total of \$1.2 billion was paid to more than 730 LGAs between March 2001 and June 2005.<sup>32</sup> In this respect, the R2R Program is unusual in that funds are provided direct to local government rather than through the States and Territories.

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<sup>28</sup> In January 2010, DITRDLG advised ANAO that, in late 2009, the AusLink Program Management System (APMS) was renamed the Infrastructure Management System (IMS).

<sup>29</sup> DITRDLG *Annual Report 2007–08*, p. 37.

<sup>30</sup> *Roads to Recovery Program Annual Report 2002–03*, p. 1.

<sup>31</sup> The full title of the Act was: 'An Act to provide funding to supplement expenditure on roads'. The R2R Act remained in force after 30 June 2005 only insofar as it required LGAs to meet various obligations, such as the requirement to acquit funds received.

<sup>32</sup> ANAO Audit Report No. 31 2005-06, op. cit., p. 16.

**1.10** The R2R Act provided a Special Appropriation for payments to funding recipients identified in a list tabled in the House of Representatives. The Act specified that the payments to funding recipients must be made before 1 July 2005. Additional funds for unincorporated areas and the Indian Ocean Territories were provided through Annual Appropriations.<sup>33</sup>

## **Basis of allocations**

### *Financial Assistance Grants*

**1.11** The R2R Program runs in parallel with Financial Assistance Grants (FAGs) provided under the *Local Government (Financial Assistance) Act 1995*.<sup>34</sup> FAGs are provided in the form of untied general purpose assistance and 'identified' but untied local road funding. The general purpose grants are distributed between the States on a per capita basis. The roads grants are distributed between the States on a fixed share basis.

**1.12** The Local Government (Financial Assistance) Act requires National Principles to be formulated in consultation with State Ministers and a body or bodies representative of local government to govern the distribution of grants within each State. The National Principles came into effect from 1996–97 and apply to both grant components. The Principle applying to the identified road component requires distribution on the basis of road expenditure needs, including consideration of factors such as length, type and use of roads.

**1.13** Local Government Grants Commissions established within each State and the Northern Territory determine individual council allocations in accordance with the National Principles. Each State and the Northern Territory has its own methodology for calculation. These calculations for the identified local roads grants consider several factors that usually include population, road length, bridge length, topography and/or rainfall. After the Grants Commissions have determined the grant distribution, the State Minister recommends the allocation to the Commonwealth Minister for approval.<sup>35</sup>

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<sup>33</sup> Unincorporated areas are areas with no local council.

<sup>34</sup> In light of the States' constitutional responsibilities for local government, the Commonwealth grants are provided through the States as Specific Purpose Payments. For the purposes of the Local Government (Financial Assistance) Act, unless otherwise specified, the term State includes the Australian Capital Territory and the Northern Territory.

<sup>35</sup> In 2009–10, FAGs identified for local roads will provide payments to councils for local roads of about \$591 million.



**1.14** The recommendations for the intrastate allocation of the local roads FAGs for 2000–01 were used as the basis of the initial calculation for the R2R funding allocations.

*Interstate distribution of R2R funding*

**1.15** The distribution of R2R funds between the States and Territories was determined at the Ministerial level. The then Government considered that no single factor or a combination of factors provided a satisfactory distribution. In arriving at the actual distribution, consideration was given to:

- the historical results from using the FAGs identified for local roads; and
- population and length of road under the control of the local government, with each of these two statistics weighted equally.

**1.16** Consideration was also given to the long standing concern of South Australia that it received a disproportionately low level of funding under the FAGs identified for local roads.

*Intrastate distribution*

**1.17** The allocation of funds within each State was determined using the formula applied by State Grants Commissions for the FAGs identified for local roads. Therefore, in order to be a funding recipient, LGAs needed to be eligible for a local roads FAGs payment in the estimated 2000–01 payment calculations.<sup>36</sup>

**1.18** Allocations to individual funding recipients were set in a list tabled at the time of the R2R Act being presented to the Parliament. The R2R Administrative Guidelines<sup>37</sup> stated that each LGA was guaranteed its full life of program allocation by 30 June 2005, subject to the submission of satisfactory documentation such as works schedules and Quarterly and Annual Reports. Section 8 of the R2R Act addressed the issue of replacement funding recipients where a funding recipient ceased to exist before it had received the full amount

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<sup>36</sup> The Indian Ocean Territories and the unincorporated areas were outside this arrangement. Also, in line with the arrangements for local roads FAGs:

- in Western Australia, \$12.6 million, or seven per cent of the initial R2R Program funding for the State, was held back from LGAs for bridges and Aboriginal access roads; and
- in South Australia, \$15 million, or 15 per cent of the initial R2R Program funding for the State, was held back from LGAs for distribution in connection with the State's Special Local Roads Program.

<sup>37</sup> Published under section 11 of the R2R Act.

payable to it. This applied, for example, where LGAs were amalgamated or abolished.

**1.19** The initial R2R Program was managed by the then Department of Transport and Regional Services (DOTARS)<sup>38</sup> under simple administrative procedures, whereby LGAs would nominate the projects to be funded and report to the department.

## **Previous ANAO performance audit**

**1.20** In March 2006, ANAO tabled the report on its performance audit on Roads to Recovery. The audit scope covered development of the R2R Program, management of the initial R2R Program and changes made to the program funding conditions and administrative guidance for the AusLink R2R Standard Program. The scope did not include management of the Standard Program.<sup>39</sup>

**1.21** The audit objectives were to:

- assess the efficiency and effectiveness of the management of the initial R2R Program; and
- identify any opportunities for improvements to the management of the program.<sup>40</sup>

**1.22** The audit involved examination of the use of, and accountability for, R2R funds by a representative sample of LGAs from around Australia. This work included site inspections of selected projects funded under the program, analysis of financial and other reports provided to DOTARS by LGAs, and substantiation of the amounts charged to the R2R Program for the selected projects.

**1.23** The then DOTARS agreed with all of the recommendations, except for part (d) of Recommendation No. 10 (relating to LGAs accounting for funds allocated to special projects), which it agreed to with one qualification. In particular, the qualification stated that ‘the funds need to be clearly

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<sup>38</sup> Following the change of Government in November 2007, DOTARS was restructured, and was renamed the Department of Infrastructure, Transport, Regional Development and Local Government (DITRD LG). Source: DITRD LG Annual Report 2007–08, p. 2.

<sup>39</sup> ANAO Audit Report No. 31 2005–06, op. cit., p. 53.

<sup>40</sup> *ibid.*

identified but do not need to be held separately. Responsibility lies with the councils but the department will address this issue as part of the financial audits to commence in 2006–07'.<sup>41</sup>

**1.24** All recommendations (except No. 1) had been implemented by DITRDLG, primarily by improving the funding conditions and Notes on Administration of the AusLink R2R Program and enhancing IMS to assist in monitoring and reviewing the reporting and payment arrangements between DITRDLG and funding recipients.

**1.25** In respect to Recommendation No. 1, DITRDLG records indicated that a benefit-cost analysis of a representative sample of R2R projects funded by the Australian Government was scheduled to begin in November 2007. However, as the decision to extend the program had been taken by the Government ahead of any cost-benefit analysis of individual projects by the department, DITRDLG decided that the analysis would not be undertaken.<sup>42</sup>

## AusLink Roads to Recovery Program

**1.26** In January 2004, the then Australian Government announced that a further \$1.2 billion in R2R funding would be provided over the four years from July 2005 to June 2009.

**1.27** In July 2005, under Part 8 of the *AusLink (National Land Transport) Act 2005* (AusLink Act), the AusLink Roads to Recovery Program was established (referred to throughout this report as the Standard Program). Unlike the R2R Act, this Act did not specify how much funding was to be provided under the Standard Program. Instead, a legislative instrument was made that specified the amounts of Commonwealth funding to be provided for the program.<sup>43</sup> This instrument also specified the names of the entities that were to receive amounts totalling \$1.23 billion. This comprised the \$1.2 billion for grants payments to local government together with \$30 million for unincorporated areas and the Indian Ocean Territories (see Table 1.1).

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<sup>41</sup> ANAO Audit Report No. 31 2005-06, op. cit., p. 184.

<sup>42</sup> DITRDLG, Minutes of the Audit Committee meeting dated 17 December 2008, p. 8.

<sup>43</sup> Federal Register of Legislative Instruments F2005L02286, Determination of the AusLink R2R List pursuant to section 87 of the *AusLink (National Land Transport) Act 2005*, 2 August 2005.

**1.28** As occurred with the initial R2R Program, the distribution of funds within each jurisdiction to each LGA again followed the recommendations of the Local Government Grants Commissions for allocating the local roads component of FAGS. Accordingly, the AusLink R2R Standard Program funding allocations used the Grants Commissions' recommendations for 2004-05. As per the initial R2R Program, the formula took into consideration the population and road length as set by the local government grants commission for each State and the Northern Territory.

**1.29** Table 1.1 shows the distribution of the Standard Program funds across all States and Territories.<sup>44</sup>

**Table 1.1**

**State Distribution of AusLink R2R Standard Program funding**

State	Standard Program Allocation (\$)	Unincorporated Areas <sup>A</sup> (\$)	Total (\$)	(%)
NSW	340 000 004	2 515 000 <sup>B</sup>	342 515 004	27.9
VIC	250 000 000	64 000	250 064 000	20.3
QLD	250 000 000	-	250 000 000	20.3
WA	180 000 002	636 000 <sup>C</sup>	180 636 002	14.7
SA	99 999 996	10 785 000	110 784 996	9.0
TAS	39 999 997	-	39 999 997	3.3
NT	20 000 001	16 000 000	36 000 001	2.9
ACT	20 000 000	-	20 000 000	1.6
<b>Total</b>	<b>1200 000 000</b>	<b>30 000 000</b>	<b>1 230 000 000</b>	<b>100.0</b>
Notes: A. Unincorporated areas are areas with no local council. B. Comprises \$2 389 300 for NSW unincorporated areas and \$125 700 for Lord Howe Island. C. Comprises \$453 000 for Christmas Island and \$183 000 for Cocos (Keeling) Island.				

Source: ANAO analysis of DITRDLG data.

<sup>44</sup> The State distribution of the \$1.2 billion component of the AusLink R2R Standard Program funds was the same as under the initial R2R Program. However, there were differences between the initial Program and the Standard Program in the distribution of funds to unincorporated areas and the Indian Ocean Territories.

**1.30** The administration procedures for the AusLink R2R Standard Program were based on those of the initial R2R Program, with enhanced Funding Conditions and Notes on Administration following recommendations from the previous ANAO performance audit.

## AusLink Roads to Recovery Supplementary Program

**1.31** Announced in the May 2006 Budget, the then Australian Government provided a further \$307.5 million in 2005–06 as a supplement to the AusLink R2R Standard Program. Funding recipients received their Supplementary Program allocations in June 2006 and were required to expend these funds by 30 June 2009.

**1.32** Under the Supplementary Program, each funding recipient received a one off grant equal to one quarter of its life of program allocation under the AusLink R2R Standard Program. The funds were distributed and administered under similar funding conditions to those of the Standard Program, with funding recipients being required to acquit their project expenditures by submitting Quarterly and Annual Reports.

**1.33** The scope of this performance audit included the management of the Supplementary Program.

## Nation Building Roads to Recovery Program

**1.34** In April 2009, the Australian Government announced that it was investing \$26.7 billion on road and rail infrastructure through the Nation Building Program over the six year period 2008–09 to 2013–14. A component of this is the Nation Building R2R Program, where \$1.75 billion over five years from 1 July 2009 will be available to LGAs, and State and Territory governments responsible for unincorporated areas. This funding is an increase of \$50 million a year (or \$250 million over five years) compared to the previous annual allocation under the AusLink R2R Standard Program.<sup>45</sup>

**1.35** Table 1.2 shows the allocation of the Nation Building R2R Program funds across all States, Territories and unincorporated areas. The State distribution is approximately the same as the initial Program. The amount for each State has been divided between LGAs on the basis of the 2008–09

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<sup>45</sup> Media statement from the Minister for Infrastructure, Transport, Regional Development and Local Government, August 2008.

recommendations of each State's Local Government Grants Commission in relation to the roads component of the FAGs.<sup>46</sup>

**Table 1.2**

**Nation Building R2R Program allocations**

State	Total Allocation(\$)	(%)
New South Wales LGAs	484 000 000	27.7
Victorian LGAs	356 000 000	20.3
Queensland LGAs	356 000 000	20.3
Western Australian LGAs	238 080 000	13.6
South Australian LGAs	142 000 000	8.1
Tasmanian LGAs	57 000 000	3.3
Northern Territory LGAs	28 000 000	1.6
Australian Capital Territory Government	28 000 000	1.6
New South Wales Roads and Traffic Authority	3 400 000	0.2
Lord Howe Island	180 000	<0.1
Victorian Department of Transport	95 000	<0.1
South Australian Department of Transport, Energy and Infrastructure	15 400 000	0.9
Northern Territory Department of Transport	23 000 000	1.3
Shire of Christmas Island	655 000	<0.1
Cocos (Keeling) Islands Shire	270 000	<0.1
Unallocated funding for bridges and Aboriginal Access Roads in Western Australia	17 920 000	1.0
<b>Total</b>	<b>1 750 000 000</b>	<b>100.0</b>

Source: ANAO analysis of Determination of the AusLink Roads to Recovery List Pursuant to Section 87 of the Act (Instrument 2009/1).

<sup>46</sup> Letter dated 25 March 2009 from the Minister for Infrastructure, Transport, Regional Development and Local Government to LGAs.

## The AusLink R2R ANAO performance audit

**1.36** ANAO's 2008–09 Audit Work Program included a performance audit titled 'Management of the AusLink Roads to Recovery Program'.<sup>47</sup>

**1.37** This performance audit was conducted under Section 15 of the *Auditor-General Act 1997*. Its objectives were to:

- assess the effectiveness of the management of the AusLink Roads to Recovery Program, including the implementation of agreed recommendations made by the ANAO in its audit of the initial R2R Program;
- assess the delivery of the program and management of the funding, including the extent to which the program has provided additional (rather than substitute) funding for land transport infrastructure; and
- identify opportunities for improvements to the management of the program.

**1.38** The audit scope covered the management of the AusLink R2R Standard Program for the period 1 July 2005 to 30 June 2009 and the AusLink R2R Supplementary Program for the period 27 June 2006 to 30 June 2009. It did not cover the initial R2R Program which concluded in June 2005, or delivery of the Nation Building R2R Program which commenced on 1 July 2009 (although changes in administration arrangements for the program were examined, so as to inform the development of audit recommendations).

**1.39** The audit work involved a number of aspects, including:

- examination of DITRDLG records and discussions with DITRDLG officers responsible for administering the AusLink R2R Program;
- analysis of data recorded in IMS;
- site visits to a total of 563 AusLink R2R projects<sup>48</sup> across a representative sample of 41 LGAs (see Appendix 1),<sup>49</sup> together with

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<sup>47</sup> ANAO, Audit Work Program 2008–09, July 2008, pp. 98–99.

<sup>48</sup> Covering both the Standard Program and Supplementary Program.

<sup>49</sup> The audit selected a representative sample from four States/Territories focusing on an appropriate cross section of funding recipients encompassing: rural and metropolitan areas with various population sizes (the Australian Classification of Local Governments (ACLG) was used to categorise LGAs); and LGAs with small, medium and large annual allocations delivering low, medium and high numbers of projects under the program.

analysis of reports and certifications provided to DITRDLG by these LGAs in relation to all their AusLink R2R projects and expenditure. The sample included almost six per cent of the total number of funding recipients across Australia, with the sample LGAs receiving almost eleven per cent of the total amount of funding provided under the program (see Table 1.3); and

- examination of selected aspects of the R2R operations of a large number of LGAs from across Australia, primarily using Computer Assisted Auditing Techniques (CAATS).<sup>50</sup>

**1.40** The audit was conducted in accordance with ANAO auditing standards at a cost to the ANAO of \$690 000.

**Table 1.3**

**ANAO sample of funding recipients by State/Territory**

State/ Territory	Number of LGAs	% of State/ Territory	AusLink R2R Standard Program Allocation (\$)	AusLink R2R Supplementary Program Allocation (\$)	% of State Allocation
ACT	1	100.0	20 000 000	5 000 000	100.0
NSW	13	8.4	40 715 323	10 178 832	11.9
VIC	11	13.8	48 922 431	12 230 610	19.6
WA	16	11.3	24 630 277	6 157 571	13.6
<b>Sample Total</b>	<b>41</b>	<b>5.9</b>	<b>134 268 031</b>	<b>33 567 013</b>	<b>10.9</b>

Source: ANAO analysis of DITRDLG data and Local Government National Report 2005–06.

<sup>50</sup> For example, CAATS were used extensively during the audit to identify trends, anomalies and particular attributes of interest within the whole population of LGAs funded throughout the life of the AusLink R2R Standard Program and Supplementary Program.



## 2. Governance Framework

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*This chapter analyses the governance framework of the AusLink R2R Program including the conditions and guidelines for the program and the reporting arrangements for funding recipients.*

### Payment of funds to local government

**2.1** In Australia, local government is responsible for planning, developing and maintaining a significant amount of the key infrastructure for its communities. This includes local roads, bridges and footpaths. In this respect, the 2003–04 Annual Report on the operation of the *Local Government (Financial Assistance) Act 1995* stated that:

Local roads provide basic access from farms, factories and homes to schools, hospitals, work, shopping and to families and friends. Local roads are part of a network. They are vital feeder roads to the economically significant arterials and highways funded by Australian and State governments, so they are important to overall transport efficiency and to national economic performance.<sup>51</sup>

**2.2** Of the nation's 810 000 kilometres of public roads, more than 650 000 kilometres (80 per cent) are local roads.<sup>52</sup> Approximately one-third of these roads are sealed with the remainder unsealed (unformed, formed or gravel roads).<sup>53</sup>

**2.3** Local government is not included in the legislative powers of the Commonwealth specified by section 51 of the Constitution. As a consequence, local government remains the responsibility of State governments. In this respect, local governments are established under State legislation and are subject to State government oversight.

**2.4** Nevertheless, since 1974–75, successive Australian governments have provided general purpose funding for local government through Specific

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<sup>51</sup> DOTARS, *Local Government National Report: 2003–04 Report on the Operation of the Local Government (Financial Assistance) Act 1995*, p. 75.

<sup>52</sup> AusLink Annual Report 2007–08, p. 23.

<sup>53</sup> DITRDLG, *Local Government National Report: 2006–07 Report on the Operation of the Local Government (Financial Assistance) Act 1995*, p. 7. At the time of the audit, the 2007–08 Report had not been presented to the Parliament.

Purpose Payments (SPPs) to the States and Territories.<sup>54</sup> SPPs are made under section 96 of the Constitution, which provides that ‘the Parliament may grant financial assistance to any State on such terms and conditions as the Parliament sees fit’.

**2.5** The current arrangements for providing SPPs to local governments are embodied in the *Local Government (Financial Assistance) Act 1995*. This Act is administered by DITRDLG. It requires<sup>55</sup> funds to be passed to local government without undue delay, in their entirety, and in accordance with allocations determined by the relevant State Grants Commission.

**2.6** In 2008–09, the Australian Government provided \$2.4 billion in Financial Assistance Grants (FAGs) to local government through the States and Territories.<sup>56</sup> This amount included \$480 million in FAGs brought forward (paid in June 2009), to assist local government deal with the effects of the global financial crisis.<sup>57</sup> In 2009–10, local government is expected to receive more than \$1.9 billion in FAGs.<sup>58</sup> This amount comprises general purpose assistance of \$1.3 billion and ‘identified’ (but untied)<sup>59</sup> local road grants of \$591 million.

**2.7** Unlike FAGs, most R2R funds were provided direct to local government.<sup>60</sup> In this context, when announcing the initial R2R Program with the then Minister for Transport and Regional Services, the then Prime Minister stated that:

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<sup>54</sup> Submission by the Department of the Treasury to the House of Representatives Standing Committee on Economics, Finance and Public Administration inquiry into local government and cost shifting, September 2002, p. 1.

<sup>55</sup> Sections 11, 14 and 15.

<sup>56</sup> DITRDLG, *Annual Report 2008–09*, p. 97.

<sup>57</sup> *ibid.*, p. 95.

<sup>58</sup> Financial Assistance Grants to Local Government. <[www.infrastructure.gov.au/local/assistance/](http://www.infrastructure.gov.au/local/assistance/)> [accessed 11 November 2009].

<sup>59</sup> These grants are distributed on the basis of road expenditure needs (including consideration of factors such as length, type and use of roads) but the amounts paid may be used for any purpose, including on roads.

<sup>60</sup> A total of \$15 million of R2R funds was paid through the South Australian Local Government Grants Commission to 25 LGAs and regional associations for distribution as part of the broader South Australian Special Local Roads Program, administered by the Commission. In addition, some \$30 million was paid to the Indian Ocean Territories and those bodies, normally state road authorities, that administer unincorporated areas throughout Australia.

One of the greatest strengths of the *Roads to Recovery* Program is that the funding will go direct to Local Government and allow councils to spend the money according to their priorities.<sup>61</sup>

**2.8** Legal issues concerning the direct funding of local government were considered when the Roads to Recovery Program was originally developed in 2000. The Program was originally administered under the R2R Act. However, since that Act was developed and the program established, Constitutional issues concerning the direct funding of local government have been raised in the Tax Bonus Case decided upon by the High Court.<sup>62</sup> In this respect, advice to agencies from the Attorney-General's Department is that they may proceed with settled spending programs without obtaining further advice but, if there is doubt, the Attorney-General's Department can be contacted for advice on the management of Constitutional risk.

**2.9** In February 2010, DITRDLG advised ANAO that the department, with the Attorney-General's Department and the Australian Government Solicitor, was examining the constitutional risk associated with the R2R Program in the wake of the Tax Bonus case.

## Governance arrangements

**2.10** The *AusLink (National Land Transport) Act 2005* (AusLink Act or the Act) was assented to on 6 July 2005. Parts 3 to 8 of the Act commenced on 28 July 2005, the date of proclamation by the then Minister for Transport and Regional Services.<sup>63</sup>

**2.11** Part 8 of the Act governed the AusLink R2R Program. The Act specified that payments can only be used 'on the construction or maintenance of roads'. The terms 'construction', 'maintenance' and 'road' were also defined in the Act. However, the Act contained no discretionary power to expand the definition of road.

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<sup>61</sup> The Hon John Howard MP, Prime Minister and the Hon John Anderson MP, Deputy Prime Minister and Minister for Transport and Regional Services, *\$1.6 billion Investment in Roads*, Joint Media Release, 27 November 2000.

<sup>62</sup> *Pape v Commissioner of Taxation and Anor.* (2009) HCA 23; (2009) 83 ALJR 765; (2009) 257 ALR 1.

<sup>63</sup> Commencing on 27 June 2009, the name of the Act was changed to the *Nation Building Program (National Land Transport) Act 2009*.

**2.12** Before DITRD LG could make the first payment under the AusLink R2R Program, the Act required the Minister to:

- under section 87, by legislative instrument, determine a list of all LGAs and the amounts they were to receive<sup>64</sup>; and
- under section 90, by legislative instrument, determine the conditions that apply to payments under Part 8 of the Act.

**2.13** Notes on Administration (in effect, replacing the initial R2R Program's Administrative Guidelines) were also issued by DITRD LG and were intended as an administrative tool for LGAs to use in conjunction with the funding conditions. Rather than being published by the authority of the Minister, as occurred under the initial R2R Program, the Notes on Administration were provided to the Minister for his information.<sup>65</sup>

## **List of funding recipients**

**2.14** The AusLink Roads to Recovery List pursuant to section 87 of the Act was determined by the then Minister for Local Government, Territories and Roads on 2 August 2005 and registered on the Federal Register of Legislative Instruments (FRLI) on 15 August 2005. The list set out the local government bodies to be funded and the amounts of the grant each was entitled to over the life of the Standard Program.

**2.15** As at 30 June 2009 (the nominated end date for the AusLink R2R Standard Program), funds under the AusLink Act had been paid to 722 recipients amounting to \$1 229 406 368.

### ***LGAs paid more than their registered allocation***

**2.16** Section 88 of the Act addresses the issue of replacement funding recipients where a recipient ceases to exist before it has received the full amount payable to it. A replacement body must be either a local governing body or a State. Over the life of the AusLink R2R Program, there were 12 Determinations registered on FRLI under section 88 of the Act for name changes, newly created LGAs or where a funding recipient ceased to exist.

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<sup>64</sup> Allocations were announced by the then Minister for Transport and Regional Services after the 2005–06 Budget and required formal determination after proclamation of the AusLink Act.

<sup>65</sup> The AusLink Act did not contain an equivalent provision to section 11 of the R2R Act. Section 11 provided that the Minister may publish Administrative Guidelines in relation to payments made under the R2R Act and in relation to the Funding Conditions determined under section 7 of the R2R Act.

**2.17** ANAO analysed the section 88 Determinations as registered, and the payments made to LGAs through the AusLink R2R Program. This analysis showed a number of occasions where an LGA had ceased to exist before it received its full funding, and its remaining funds were paid to another LGA. In addition, three instances were identified where a section 88 Determination in relation to the respective LGA was not registered on FRLI by DITRD LG, as illustrated in Table 2.1. Nevertheless, the payments made were the amounts intended for the LGAs that received them.

**Table 2.1**

**Replacement body in receipt of payment but no registered Determination**

Council	State	Total registered allocation (\$)	Total payments received (\$)	Difference (\$)
Maranoa Regional Council <sup>A</sup>	QLD	nil	2 923 817	2 923 817
Western Downs Regional Council <sup>B</sup>	QLD	nil	4 407 879	4 407 879
The Hills <sup>C</sup>	NSW	nil	766 351	766 351
<b>TOTAL</b>		nil	<b>8 098 047</b>	<b>8 098 047</b>
Notes: A. Maranoa replaced Roma Regional Council in July 2009. B. Western Downs was paid the remaining funds from Dalby Town (\$1 895 180), Chinchilla (\$191 844), Murilla (\$697 310), Tara (\$729 910) and Wambo (\$893 635). C. The Hills replaced Baulkham Hills Shire Council from October 2008.				

Source: ANAO analysis of DITRD LG records, FRLI, and QLD and NT local government boundary change documentation.

**2.18** In February 2010, DITRD LG advised ANAO that it was only necessary to determine new allocations where an LGA was abolished and its funding transferred to another LGA. However, ANAO noted that there were nine amendments to the list to reflect name changes between September 2005 and July 2008.

*LGAs paid less than their full allocation*

**2.19** Three LGAs were paid less than their life of program allocation. The first was Mornington Council in QLD. It had a shortfall of \$397 112.<sup>66</sup>

<sup>66</sup> Mornington Council also had a shortfall of \$30 354 under the initial Roads to Recovery Program because it had failed to submit an R2R Annual Report for 2003–04. See ANAO Audit Report No. 31 2005–06, op. cit., p. 100, paragraph 3.19.

Mornington had a life of program allocation of \$617 112. It failed to submit R2R Annual Reports for 2006–07 and 2007–08 and did not submit a March 2009 Quarterly Report.<sup>67</sup>

**2.20** The second LGA that was not paid its full allocation was Cherbourg Aboriginal Shire Council, also in QLD. It had an allocation of \$104 534. Notwithstanding repeated requests from DITRDLG, Cherbourg did not submit any work schedules. Accordingly, it did not receive any payments under the program.

**2.21** The third LGA that was not paid its full allocation was East Arnhem Shire Council in NT. It had a shortfall of \$91 986. Angurugu Community Government Council failed to submit R2R Annual Reports for 2006–07 and 2007–08. This council was abolished in July 2008 and responsibility for providing its annual reports passed to East Arnhem Shire Council. The Council advised DITRDLG that the records at Angurugu were not adequate for this purpose and repaid \$91 986 by offset against its May 2009 payment.

**2.22** In addition, three other LGAs formed by amalgamations in QLD and NT repaid amounts of initial R2R Program funding which the new LGAs stated they could not acquit due to inadequate records of their precursor councils, as follows:<sup>68</sup>

- Northern Peninsula Area Regional Council (QLD) repaid \$6 418 provided to Seisia Island Council;
- Torres Strait Island Regional Council (QLD) repaid a total of \$5 575 provided to Mabuiag Island Council and Ugar Island Council; and
- Central Desert Council (NT), by offset against its May 2009 payment, repaid \$60 610 provided to Lajamanu Community Government Council.<sup>69</sup>

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<sup>67</sup> This was the last opportunity for LGAs to receive a payment under the AusLink R2R Standard Program.

<sup>68</sup> Funding Condition 8 provided that if a funding recipient had failed to comply with the Act or to fulfil any of the Conditions, when notified in writing by DITRDLG it must repay to the Commonwealth the amount specified in the notice.

<sup>69</sup> ANAO noted that, as at 30 June 2008, six LGAs had still not acquitted funds totalling \$154 456 received under the initial R2R Program, which ended on 30 June 2005, being: Burke Shire Council \$34 714, Gatton Shire Council \$17 267, Napranum Aboriginal Shire Council \$37 159, New Mapoon Aboriginal Council \$55 167, Saibia Community Council \$5 433, and Ugar Island Council \$4 806. In April 2010, DITRDLG advised ANAO that these funds had been acquitted or repaid, except for New Mapoon Aboriginal Council and Saibai Community Council, which had both been abolished. The Department further advised that it had written to the relevant new councils in relation to these funds.

## Funding Conditions

**2.23** The AusLink R2R Program operated under funding conditions determined by the then Minister for Local Government, Territories and Roads under section 90 of the Act. They were signed by the then Minister on 2 August 2005. The Conditions were registered on FRLI on 15 August 2005 and tabled in the House of Representatives and the Senate on 5 September 2005. The Explanatory Statement advised that:

There was extensive consultation with stakeholders, especially with the Australian Local Government Association, in the development of the AusLink Roads to Recovery Program, of which the Funding Conditions are part.

**2.24** The funding conditions specify the legal obligations with which LGAs must comply to receive funding under the program. The key conditions were:

- money received under the program must be used for roads expenditure;
- money received under the program must be properly accounted for;
- money received under the program must be spent within six months;
- all money received under the program must be spent by 31 December 2009;
- any interest received on R2R payments must be spent on roads;
- funded projects must comply with published technical standards and guidelines, (including the National Code of Practice for the Construction Industry—for large projects only);
- an LGA must maintain the level of roads expenditure which it funds otherwise than under the AusLink Act;
- an LGA must comply with public information conditions, including erecting signs acknowledging the Commonwealth's role in respect of all works funded under the Act;
- an LGA must provide a schedule of works to DITRD LG in the form specified in the Conditions, before a payment can be paid under the Act, and thenceforth the schedule of works must be kept up to date;
- an LGA must provide quarterly reports to DITRD LG on the expenditure of funds provided under the Act, in the form specified in the Conditions; and

- no later than 31 October each year, an LGA must provide an Annual Report to DITRDLG, in the form specified in the Conditions.

**2.25** The Act provided the Minister with the power to revoke or vary any of these conditions, as well as exempting LGAs from any of the conditions. On 30 March 2006, the then Minister for Transport and Regional Services varied the funding conditions, as follows:

- any interest received on R2R payments in one financial year was required to be spent on roads during the next year, and the LGA was required to be able to demonstrate that this was done;
- LGAs with a total allocation of less than \$1 million were no longer required to spend any interest they earned from R2R funds on roads; and
- the requirement for rigid compliance with technical standards was amended to require compliance *as appropriate* with these standards, in recognition that standards relevant to roads were mostly guidelines from which LGAs chose those elements appropriate for the project and their circumstances. Thus the decisions on the standards to be adopted would be left up to LGAs in accordance with the general principle underlying Roads to Recovery that LGAs were best placed to manage all aspects of the projects to be undertaken.

**2.26** Granting of exemptions from the funding conditions is discussed in Chapter 3 and Chapter 4.

## **Notes on Administration**

**2.27** The purpose of the Notes on Administration was to explain how the AusLink R2R Program worked. The Notes stated they were designed to provide LGAs with a description of the operations of the program, including the requirements that LGAs must meet to obtain their funding, and the ongoing obligations LGAs have toward the Australian Government for the funding provided. The Notes were divided into eleven parts:

- Background;
- General requirements for AusLink R2R projects;
- AusLink R2R criteria;
- Nomination of work programs;
- Approving a work program;



- Payment and acquittal arrangements;
- Reporting requirements;
- Expenditure maintenance requirements;
- National Code of Practice for the Construction Industry;
- Information and recognition; and
- Program monitoring and evaluation.

**2.28** Three versions of the Notes were published over the life of the AusLink R2R Program. The Notes were initially published on 3 August 2005.<sup>70</sup>

**2.29** Revised Notes were issued in June 2006. This version incorporated guidance on the operation of the Supplementary R2R Program. As well, it amended the Notes to reflect the March 2006 changes made to the funding conditions for the Standard Program. Other amendments included:

- updated contact information;
- instructions on using the withdrawn project facility (introduced in December 2005);
- enabling all LGAs to draw down up to \$250 000 per annum, with up to \$400 000 with justification in any one year<sup>71</sup>; and
- correcting an error referring to the reallocation of funds not spent by some councils to others that can use them. The intention was that funds still held by the Commonwealth and not drawn down by LGAs would be reallocated, not funds paid to LGAs that remained unspent by them.

**2.30** A further revised set of Notes was published in October 2006. DITRDLG's records stated that:

The Notes are a 'user's guide' for use by councils. (They contain) a series of amendments to bring them completely up to date and to explain issues which seem to give councils difficulty so as to make them, as far as possible a 'one stop shop' for councils using the program. A number of the issues have arisen

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<sup>70</sup> Although dated 1 July 2005, the Notes were first circulated by email as an attachment to R2R Circular 2005/9 issued on 3 August 2005. LGAs had been advised by R2R Circular 2005/5 issued on 1 July 2005 that the Notes on Administration could not be issued until the AusLink Act had been proclaimed, which at that time was not expected to occur until late July or early August 2005.

<sup>71</sup> Previously, LGAs with a life of program allocation of \$250 001 had an effective annual allocation cap of \$62 500.

since the last amendment and the proposed amendments have been issued by circular already.

**2.31** The areas of substance that differed between the June 2006 and October 2006 Notes were:

- clarification that bores for water for road building were eligible for inclusion in costs of complying projects;
- an expanded list of excluded items, mainly related to various components of LGA overheads;
- acceptable methods for capturing, quantifying and apportioning labour costs for projects completed by councils' workforce;
- in relation to work schedules:
  - an explanation of why projects should not be deleted at the end of each year or when the projects are completed;
  - updated types of information required to be included in the schedules; and
  - the need to update the figures in the schedules quarterly;
- inclusion of the method most LGAs would use to demonstrate compliance with the interest rule;
- explanation of the terms 'expended to end of quarter', 'forecast expenditure next quarter', 'cumulative expenditure' and 'projected expenditure'; and
- clarification of 'own source expenditure', and widening of the definition of 'roads' to include any definition of roads used in an LGA's general accounts.<sup>72</sup>

## **R2R Circulars**

**2.32** In January 2002, the department began issuing circulars to LGAs. A total of 58 *Roads to Recovery Circulars* were subsequently issued in relation to

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<sup>72</sup> The Notes also advised LGAs that if they wished to use another definition (other than as stipulated in the Act or as used in Council's general accounts) they should write to DITRD LG. However, ANAO did not identify any instances where an LGA requested approval of an alternate definition.

the AusLink R2R Program.<sup>73</sup> Recent circulars are available on the Nation Building R2R website.

**2.33** The information contained in the circulars usually related to day-to-day administrative matters. Examples included: the requirement to update information in the works schedules prior to submitting the relevant quarterly report; reminding LGAs that Quarterly and Annual Reports were to be submitted; and staff changes within the DITRDLG R2R team.

**2.34** In addition, sometimes the circulars addressed more strategic issues. This included advice about the extension of the R2R Program.

## Eligible projects

**2.35** In order to provide an effective control over expenditure regarding R2R funds on allowable works, there needed to be a shared understanding between DITRDLG and the funding recipients of the meaning of 'road project' under the Act.

**2.36** On 1 July 2005, the first day of the AusLink R2R Program, DITRDLG issued *Roads to Recovery Circular 2005/5*. Among other things, this circular provided the following advice on eligible projects:

...while projects eligible for funding will largely be as for the previous program, there will be some tightening of compliance requirements in terms of funding eligibility for bicycle paths (only when directly associated with a road) and footpaths (only when constructed as part of a road construction or road upgrade project).

Capital equipment purchases, street sweeping, rehabilitation studies, off road car parks, street furniture, generic transport planning studies and staff training will not be funded under the new program.<sup>74</sup>

## Reporting arrangements

**2.37** As part of the then Government's commitment to e-commerce, from the outset the R2R Program was designed to operate via the internet with data

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<sup>73</sup> Thirteen Circulars were issued in 2005, twenty in 2006, eleven in 2007, eight in 2008 and six in 2009.

<sup>74</sup> This information was also in the Notes on Administration.

entered into a secure website. In addition, most communication from the department to LGAs was intended to be via email.<sup>75</sup>

**2.38** Access to the website was controlled by password. In this context, the secure website had a number of sections, including:

- payee details which included contact details for the relevant LGA as well as banking details for electronic transfer of funds;
- a works schedule listing and describing AusLink R2R projects including their estimated cost and start and completion dates;
- Quarterly Report of actual and forecast expenditure on each of the projects included in the works schedule; and
- a change password facility.

**2.39** On 1 July 2005, six 'Quick Guides' were issued by DITRDLG to explain the project mapping requirements and assist LGAs in the use of the website. These were amended in July 2005 to reflect the relocation of DITRDLG's R2R website to a new server and to update guidance on work schedules. Quick Guides 4-6 (Work Schedules, Mapping Requirements and Quarterly Reports respectively) were revised and reissued in December 2005 as an attachment to R2R Circular 2005/16.

**2.40** Quarterly Reports submitted by LGAs provided the basis on which R2R payments were made to LGAs. As part of this performance audit, ANAO analysed the quarterly reports submitted by those LGAs selected in an audit sample of 41 LGAs. In this context, Chapter 3 includes ANAO's analysis of payment controls and cash management issues.

## **Works schedules**

**2.41** The then Government considered LGAs best placed to make decisions on road investment at the local level. Successive R2R Programs have reflected this by giving LGAs the freedom to use the funds as they wished, as long as it was for expenditure on roads (as defined by the Act).

**2.42** While LGAs could decide the projects that they would deliver using the R2R funds, certain information requirements, as set out in the funding conditions, were to be submitted to DITRDLG before a payment could be

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<sup>75</sup> Part 3: Report on Performance, DOTARS Annual Report 2000–01, p. 155.

made. This included a works schedule. The Notes defined 'works schedule' as a listing of projects proposed for funding under the program.

**2.43** The works schedule form was on the secure website and could be lodged electronically through the website. The works schedule was to contain information on the location and nature of the proposed works and the problems to be addressed by the works. In keeping with the requirement in Funding Condition 4.6 that a funding recipient must keep its work schedule current, the schedules could be amended at any time. However, in practice many LGAs in the ANAO sample only updated their work schedules when they were preparing to submit a quarterly report.

#### *Importance of works schedules*

**2.44** The works schedules were relied upon by DITRD LG in making payments to LGAs. Specifically, they provided details to enable DITRD LG to assess whether proposed works were eligible under the Act. Works schedules were also a public accountability mechanism for the program.<sup>76</sup> In this respect, *Roads to Recovery Circular 2002/16* stated that:

Copies of council work schedules plus their completion status are displayed on the (department's) public website. The website is a public accountability mechanism and is frequently used by the office of the Minister for Transport and Regional Services.

**2.45** On 19 May 2005, LGAs were advised in relation to the (then) soon to commence AusLink R2R Program that:

Work schedules will again be available to the public so please provide enough information in the project descriptions to allow the average person to understand what the project is about.<sup>77</sup>

**2.46** In November 2007, DITRD LG reinforced to LGAs the importance of works schedules being kept up to date.<sup>78</sup> This message was also reinforced

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<sup>76</sup> Quarterly Reports and R2R Annual Reports submitted by LGAs to DITRD LG are not public documents.

<sup>77</sup> R2R Circular 2005/3 issued on 19 May 2005. R2R Circular 2005/5 issued on 1 July 2005 stated that project information needed to be 'concise but accurate' and reiterated that projects needed to be described in a way that the average person understands. It also advised that: 'Most councils have been realistic about the amount of project detail that they have provided but AusLink R2R staff will be coming back to councils where the information provided is inadequate.' The Notes on Administration (section 4.1) also stated that: 'Work schedules are listed on the department's website for perusal by the public and it is the responsibility of LGAs to keep them up to date.'

<sup>78</sup> R2R Circular 2007/9 issued on 13 November 2007 included the following:

Footnote continued on the next page...

when DITRDLG staff conducted compliance monitoring inspections of the works undertaken by LGAs (see Chapter 4). However, ANAO's examination of a sample of 41 LGAs revealed that, in many instances, the works schedules did not reflect the required information, or were inaccurate.

### *Location of works*

**2.47** The location of the proposed works being funded by the AusLink R2R Program, as reported in the works schedule, was inadequate for more than 47 per cent of the projects inspected by ANAO, as follows:<sup>79</sup>

- the most common discrepancy involved LGAs not specifying the location, for example, by identifying: the nearest suburb or town; primary road; or relevant crossroads or chainage where the project involved work on a section of the identified road rather than the entire road;
- there were also instances where the location descriptions were so broad as to make identification of the works themselves difficult; and
- in other instances, the works schedule description was simply inaccurate.

### *Problem to be rectified and works proposed*

**2.48** To fairly reflect the outcomes of the AusLink R2R Program, it was important that reports to the Australian Government accurately reflected the full extent of the work undertaken with R2R funds. In addition, as mentioned above, works schedule descriptions of the problem and works proposed provided necessary information for DITRDLG to assess the eligibility of LGAs' proposed use of R2R funds.

**2.49** The funding conditions stated that the works schedule should contain a description of the project and the funding recipient's reasons for undertaking each project in the schedule. However, in this regard the Notes stated that the information required from the LGA included: a clear description of the

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The figures entered on both the Standard and Supplementary Program work schedules under 'Total project cost' and 'cost to Roads to Recovery Program' need to be regularly updated. These figures start as your best estimate when the project begins and should be refined as the project progresses so that, when it is completed, the figures shown are the actual outturn cost.

<sup>79</sup> NSW 71.0 per cent, VIC 24.8 per cent and WA 64.8 per cent. ANAO also noted that projects delivered by Wellington Council (VIC) were listed on the website as projects delivered by Wellington Shire Council (NSW).

problem being addressed for each proposed work, to the satisfaction of DITRD LG; and the work proposed to address the problem. Accordingly, the format of the on-line works schedules included fields for LGAs to enter information on the nature of the works proposed and the problems to be addressed by the works. In this respect, 65 per cent of projects examined by ANAO included both the problem and an adequate description of the proposed works solution. However, the remaining 35 per cent of projects did not include the nature of the works proposed and/or the solution being employed.<sup>80</sup>

**2.50** Quick Guide 4 instructed LGAs that they needed to provide road lengths in kilometres and road widths in metres when completing the field on 'Work Proposed'. On 16 January 2006, DITRD LG also sent an email to all 63 LGAs that had not yet submitted their December 2005 quarterly reports, which reiterated that 'Works Proposed...must include length and width of the road works'. In relation to the ANAO sample of LGAs, 14 per cent of projects did not include the road length and width where applicable.<sup>81</sup>

**2.51** ANAO considers that there would be improved compliance by LGAs with this requirement if DITRD LG added a mandatory field in IMS to capture this information separately in the work schedule, rather than it being included as part of the narrative description of the works proposed.<sup>82</sup> Similarly, inclusion of an additional mandatory field to record the date that signs were installed may also assist LGAs to better comply with the signage requirements.

**2.52** In addition to shortcomings in the works schedules submitted to DITRD LG, ANAO project inspections highlighted that a number of projects were not undertaken as reported. Some were understated (in that more work had been done than indicated in the works schedule description) while, more often, others were overstated. Overstatement can also occur where projects are only part-funded by the R2R Program, but this is not reported in the field provided within IMS. However, often LGAs did not identify in their works schedules that projects were jointly funded.

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<sup>80</sup> NSW 30.0 per cent, VIC 26.3 per cent and WA 60.7 per cent.

<sup>81</sup> NSW 19.0 per cent, VIC 7.7 per cent and WA 21.9 per cent.

<sup>82</sup> This field would not be mandatory for small projects under \$10 000.

### *Start and completion dates*

**2.53** Start and completion dates could affect the timing of payments to the LGA.<sup>83</sup> The Conditions specified that AusLink R2R signs be erected at each end of the works when work began, and be maintained for one year after the project was finished. Accordingly, start and completion dates were also relevant to the R2R signage requirements.

**2.54** The approach to determining start and completion dates was not defined in the R2R governance documents.<sup>84</sup> ANAO noted during the previous performance audit that inconsistent practices had been adopted by LGAs.

**2.55** In February 2006, as part of the previous audit, DITRDLG advised ANAO that it was not possible for the terms ‘start date’ and completion date’ to cover all the possibilities of the meaning that exist. Consequently, DITRDLG proposed that when the AusLink information technology system was updated, the information collected would be expanded to include commencement of planning; commencement of construction; completion of construction; and financial completion. However, DITRDLG subsequently decided not to record the commencement of planning and financial completion.

**2.56** On 8 June 2006, LGAs were requested by R2R Circular 2006/10 to note that the start and completion dates for projects on both the Standard and Supplementary Program websites are those of construction. LGAs were reminded that financial completion is not shown on the website.

**2.57** R2R Circular 2005/15 issued on 6 December 2005 also addressed project start and completion dates, as follows:

Where projects depend on the weather and the availability of contractors and equipment, the start and completion dates can reflect the window within which the job is planned. This needs to be updated regularly and noted in the project description in the work schedule that the dates are indicative and not firm.

**2.58** During the current audit, a number of instances were identified where the start and completion dates reported to DITRDLG were incorrect.<sup>85</sup> ANAO

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<sup>83</sup> For example, on occasion, DITRDLG reduced forecast expenditure figures submitted in Quarterly Reports where it was apparent that the project was not scheduled to be undertaken in the ensuing three months.

<sup>84</sup> However, section 4.1 of the Notes stated that physical, not financial, start and completion dates were required.



also noted instances in late 2008 where the project details on the website indicated projects still had a status of 'under construction', notwithstanding that the completion date was shown as 2005.

### *Maps*

**2.59** AusLink R2R funding was conditional on LGAs providing clear project descriptions and location information for each project specified in the works schedule, including mapped project location details for use in DITRD LG's Geographical Information System.<sup>86</sup>

**2.60** Quick Guide 5 provided LGAs with detailed instructions and examples to enable LGAs to satisfy the requirement to provide adequate maps to the department. Amongst other things, it advised that maps should be sent to DITRD LG within a few days of the project being listed on the website. It also advised that if satisfactory maps were not received within seven days of the end of the quarterly reporting period, this would result in funding for the un-mapped projects being withdrawn.

**2.61** ANAO examined whether satisfactory maps had been provided by the 41 LGAs in the ANAO sample. This was undertaken as a 'point in time' exercise in late 2008. ANAO downloaded details of all projects listed on the DITRD LG website for the sample LGAs. This included the map for the project, if a map had been posted on the website. ANAO gave the benefit of the doubt to projects with no maps if the project had an 'In Planning' status shown on the website (notwithstanding that, in many cases, details of these projects were posted to the website more than seven days before the ANAO download, as indicated by the date 'project details last updated' on the website).<sup>87</sup> ANAO also took into account that maps were not required for projects expected to cost less than \$10 000.

**2.62** In summary, there was no map posted on the website for 71 of the 1145 projects (6.2 per cent) where a map was required.<sup>88</sup> As a general observation, ANAO also found that over 40 per cent of the maps examined had

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<sup>85</sup> Overall, six per cent of projects inspected by ANAO had incorrect start and/or completion dates (NSW 2.0 per cent, VIC 10.6 per cent and WA 1.9 per cent).

<sup>86</sup> Funding Condition 4.2(c).

<sup>87</sup> For example, a number of projects were shown as 'In Planning' as at 28 November 2008, whereas the project details had been last updated more than three months earlier, on 7 August 2008.

<sup>88</sup> NSW 6.5 per cent, VIC 2.2 per cent and WA 11.9 per cent.

multiple projects shown, to the extent that, in ANAO's view, it would be difficult for members of the general public to identify on the map the particular R2R project of interest.

**2.63** Although LGAs that did not provide suitable maps were not complying with the funding conditions, it was not evident to ANAO that DITRDLG was aware of these cases or had adequate mechanisms in place to alert it in relation to projects where maps were not provided. In addition, ANAO did not identify any instances where exemptions (waivers) in relation to the provision of maps had been granted by DITRDLG.

**2.64** ANAO suggested that an additional field be created in IMS to record the date that DITRDLG uploads the project map to its website. Regular automated reports could then be generated to identify projects with missing maps requiring follow up.

#### *Project costs*

**2.65** Project costs had not been updated by LGAs in 18.7 per cent of the projects inspected by ANAO (NSW 33.3 per cent, VIC 10.8 per cent and WA 9.9 per cent). In addition, six of the projects inspected had costing errors not associated with a failure to update the costs of the project.

**2.66** It was not uncommon for LGAs to cover any cost over-runs on individual R2R projects with funds from the LGA's own resources. Having done so, however, LGAs often then neglected to record that the project was jointly funded and update the total cost of the project shown on the works schedule. Instances were also noted where the cost of the project was less than that shown on the work schedule.

## **Financial audits**

**2.67** In April 2006, one month after the previous ANAO performance audit report was tabled, DITRDLG engaged a contractor to conduct an independent

financial audit across seven LGAs nominated by the department.<sup>89</sup> The scope included assessments of the 2004–05 financial records on the following matters:

- the extent to which administrative overheads had been accounted for and included in the LGA's estimates of program/project cost;
- the level of compliance with the department's expenditure maintenance requirements;
- the adequacy of the financial and management systems used by LGAs in managing the program; and
- to ascertain if the funds allocated to, and spent by LGAs in 2004–05 were expended on complying projects (that is, classified as 'eligible expenditure').

**2.68** The firm was also tasked with assessing whether year to date funding in 2005–06 had been spent on eligible projects; and expenditure information provided in quarterly reports was based on sufficient documentation and reflected a true and fair estimate of the actual reported position in those reports.

**2.69** In respect to the seven sampled LGAs, the audit found that:

- five LGAs were correctly not including administrative overheads in project or program costing;
- only one LGA complied with the 2004–05 expenditure maintenance requirements;
- three LGAs complied with the 2005–06 expenditure maintenance requirements;
- five LGAs had robust financial management system;
- six LGAs had not spent funding on ineligible activities;

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<sup>89</sup> The department selected one LGA in each State/Territory excluding the ACT. LGAs were advised that the ANAO audit identified a number of issues in the operation of the program, both in DITRD LG and in councils, which needed to be addressed. DITRD LG therefore planned to undertake an ongoing series of audits of the R2R Program in various councils. The findings would give DITRD LG a better idea of how the program is run by councils with a view to better administration of the program by DITRD LG and councils. The work would be undertaken over the life of the AusLink R2R Program, with the first audits in May-June 2006 forming a pilot study for the larger task.

- all LGAs had anomalies in their 2004–05 and 2005–06 quarterly reports; and
- three LGAs submitted quarterly reports which were consistent with the AusLink website works schedule.

**2.70** The audit report recommended that DITRDLG:

- review its payout procedures: if final funding payments occur midyear, the LGA should be required to submit an additional acquittal on how that final payment was spent;
- provide a centralised training program for LGAs;
- explore the possibility of including compliance with the expenditure maintenance requirements in the scope of the audit opinion required with R2R Annual Reports;
- consider including a formal dual sign off, from Engineering and Finance sections of LGAs, on all quarterly reports;
- require LGAs to maintain separate bank accounts for management of R2R funds, given the requirement to re-invest interest earnings on surplus funds as own source expenditure; and
- categorically define the ‘directly attributable’ items of expenditure on which DITRDLG is comfortable allowing LGAs to use Commonwealth funding.<sup>90</sup>

## **Ongoing program of financial audits**

**2.71** LGAs were advised in February 2007, as follows:

The Australian National Audit Office has highlighted the need for improved accountability for *Roads to Recovery* funds. In consequence, the department is planning further audits of councils. It is proposed to audit about 100 councils during the current program. The first seven councils were audited in 2006, with 24 to be audited in the first half of 2007.<sup>91</sup>

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<sup>90</sup> In June 2006, another firm was also engaged to conduct a follow-up review of R2R funding for the Papanya Community Council and Mornington Shire Council. This firm had conducted initial reviews of these LGAs in 2005.

<sup>91</sup> R2R Circular 2007/1 issued on 22 February 2007.

**2.72** The terms of reference required the contracted firm conducting the audits<sup>92</sup> to assess:

- (a) the adequacy of the financial and management systems used by Councils in running the program;
- (b) the accuracy of the financial information in the Annual Reports submitted, including compliance with the expenditure maintenance requirements as set out in the funding conditions;
- (c) whether the expenditure information provided in quarterly reports was based on adequate documentation and was a true and fair estimate of the actual position; and
- (d) whether there was consistency between the information used as a basis for the quarterly reports and that used as a basis for the annual reports.

**2.73** Each year, DITRDLG selected the LGAs to be audited. In total, 52 LGAs were audited, including four LGAs that were audited in 2007 and re-audited in 2009. Table 2.2 illustrates the break-up of the audits across States and years. The total of 56 audits (plus the original seven) means that only 63 per cent of the target number of audits that had been advised to LGAs was conducted over the life of the AusLink R2R Program.

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<sup>92</sup> This was not the same firm that conducted the first audit of seven LGAs or the firm that conducted the June 2006 review of two LGAs.

**Table 2.2****Number of financial audits of LGAs conducted by contractor for the period 2007 to 2009**

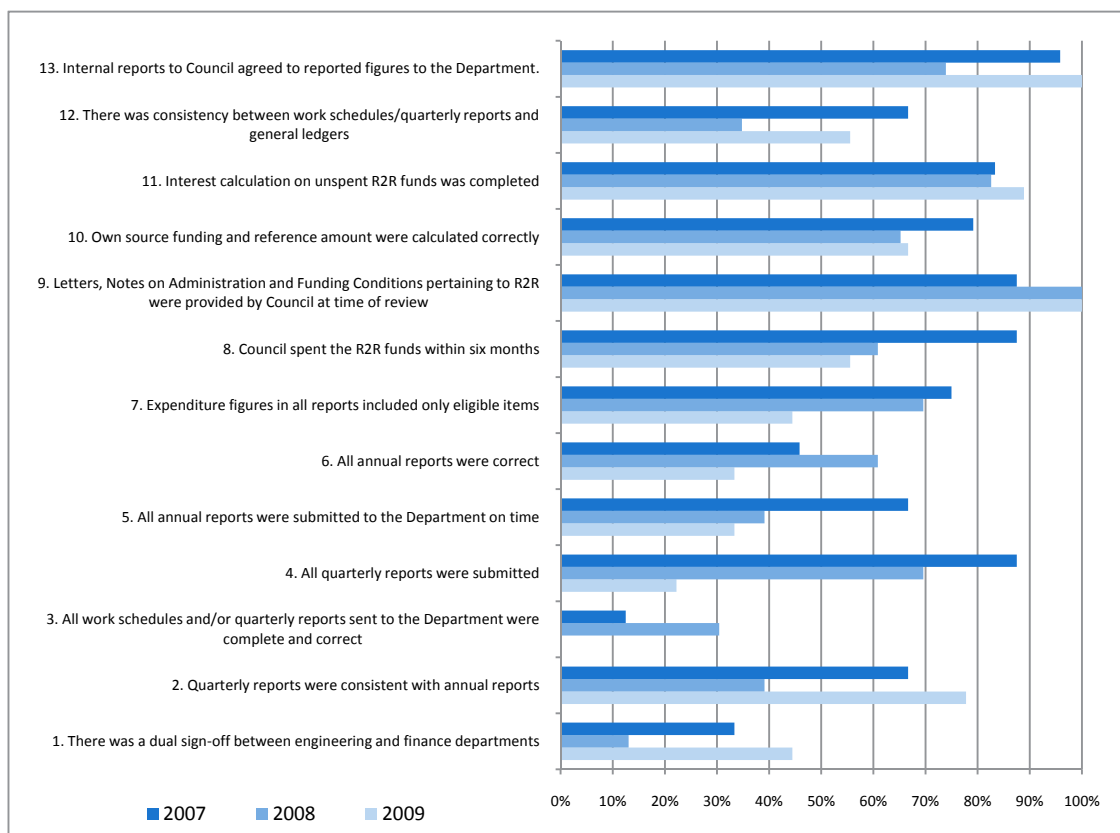
State	2007	2008	2009	TOTAL
NSW	7	5	2	14
QLD	5	4	2	11
SA	2	5	1	8
TAS	1	1	-	2
VIC	5	4	1	10
WA	4	4	3	11
<b>TOTAL</b>	<b>24</b>	<b>23</b>	<b>9</b>	<b>56</b>

Source: ANAO analysis of contractor's financial audit reports to DITRDLG.

**2.74** Overall, the results of the 56 audits conducted by the contractor indicated that, on average, LGAs complied with 62 per cent of the requirements. Figure 2.1 shows the percentage of LGAs that complied with each audit criterion. It shows that most LGAs had difficulties submitting correct works schedules and quarterly reports (not one of the LGAs audited in 2009 had error-free works schedules and quarterly reports—see Criterion 3 in Figure 2.1). In addition, relatively few LGAs had implemented a process of obtaining dual sign off between the Engineering/Technical Section and the Finance Section when preparing their quarterly reports.<sup>93</sup>

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<sup>93</sup> This was considered important to ensure that reporting to DITRDLG was accurate, particularly in terms of distinguishing physical completion of roadworks from financial completion, identifying actual costs of roadworks and preparing estimates of forward expenditure.

**Figure 2.1****Percentage of audited LGAs that complied with the audit criteria during the period 2007 to 2009**

Source: ANAO analysis of Contractor's financial audit reports to DITRDLG.

**2.75** The final report issued by the contractor in May 2009 concluded that:

- (a) the financial and management systems governing the R2R Program for LGAs appeared to lack key control elements, namely, systematic reconciliations of key reporting sent to the department;
- (b) while the financial systems for each of the LGAs appeared to be operating effectively in capturing costs, the delivery and accuracy of this information provided to the department was not being performed correctly;
- (c) the errors and anomalies appeared to be due to the LGAs' lack of knowledge of the key guidance information contained in the funding conditions and Notes;

- (d) it appeared that LGAs' auditors of Annual Report information may not be aware of the specific guidance in relation to the program; and
- (e) LGAs that had adequate systems for control in place appeared to be more compliant with the key aspects of the program legislation and guidance.<sup>94</sup>

**2.76** ANAO's suggestions for addressing items c) and d) above are included in Chapter 3. ANAO also suggested that there would be benefits in DITRD LG conducting periodic reconciliations of key project specific information provided to it by LGAs.

## Risk management

**2.77** Risk management should be a fundamental element of the governance framework in place for administering any Australian Government grants program. In this regard, DITRD LG was unable to provide ANAO with any risk assessments or risk management plans covering the AusLink R2R Program or its precursor and successor programs.<sup>95</sup> Accordingly, a systematic and comprehensive examination of risks and identification of risk treatments appears overdue.

## Program evaluation

**2.78** Along with risk management, program evaluation has long been recognised as an important element in good (or better practice) governance frameworks. In late 2002, the initial Program was the subject of a joint review by DOTARS and the Australian Local Government Association (ALGA).<sup>96</sup>

**2.79** ANAO recommended in the previous performance audit that DITRD LG analyse the costs and benefits of projects so as to inform consideration of any further extension of the R2R Program. Notwithstanding it agreed to this recommendation at the time, to date the department has not

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<sup>94</sup> Contractor's Final Audit Report—Roads to Recovery Program, May 2009, p. 5.

<sup>95</sup> This was the case notwithstanding that a November 2004 report by the department's then outsourced internal audit provider concluded that: 'The risks associated with the Roads to Recovery Program appear to have been identified and appear to be proactively managed through appropriate control strategies.'

<sup>96</sup> The joint review reported in February 2003. ANAO was critical of certain aspects of the joint review—see ANAO Audit Report No. 31 2005-06, op. cit., pp. 64-65.



conducted such an exercise or planned an evaluation of the program. In June 2009, DITRD LG advised ANAO that:

The analysis was originally scheduled to begin in November 2007 but following a 2007 election commitment, the Government made a policy decision to extend the program for a further five years.<sup>97</sup>

**2.80** Rigorous cost-benefit analysis to support funding decisions and supported by ex-post evaluation and review is also an approach advocated in the 2008–09 Budget Papers for infrastructure projects broadly:

Only public infrastructure projects which at least meet a minimum benchmark social rate of return—determined through rigorous cost-benefit analysis, including ex post evaluation and review—should be funded, and relative social rates of return above the minimum benchmark should be used to prioritise the funding of projects.

...Where governments invest in infrastructure assets, it is essential that they seek to achieve maximum economic and social benefits, determined through rigorous cost-benefit analysis including ex post evaluation and review.

...Efficient public infrastructure investment requires the development of coordinated, objective and transparent processes for decision-making based on thorough and rigorous cost-benefit analysis.<sup>98</sup>

**2.81** Against this background, ANAO does not see the decision to continue with the R2R Program as preventing the conduct of an evaluation of the program. Indeed, an evaluation potentially could identify areas for enhancing the effectiveness of the program and improving its administration, to the benefit of all parties.

## Recommendation No.1

**2.82** ANAO *recommends* that the Department of Infrastructure, Transport, Regional Development and Local Government strengthen the governance framework for the Roads to Recovery Program, including by:

- (a) better resourcing the existing program of contracted financial audits of Local Government Authorities so that the program of audits is able to be fully delivered; and

<sup>97</sup> However, in December 2008, the DITRD LG Audit Committee had been advised that: 'the analysis will now be undertaken after June 2009 to gain a view of the whole program.'

<sup>98</sup> Budget Paper No.1, 2008–09, pp. 4-6, 4-13 and 4-15.

- (b) giving greater emphasis to structured risk management and program evaluation.

**DITRDLG Response**

**2.83** Part (a) Agree. The department will prepare a limited program of financial audits to be undertaken from 2010–11 to 2013–14 along with Terms of Reference for these audits. The program of financial audits is expected to be risk based, taking into account the audited financial statements of councils and overall compliance under previous Roads to Recovery programs.

**2.84** Part (b) Agree.

### 3. Financial Management

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*This chapter examines appropriation and budgeting arrangements, payment principles and the accuracy and reliability of financial data submitted by LGAs on which payments were based. It also includes ANAO's estimate of the cost to the Commonwealth of payments being made to LGAs more than three months in advance of need.*

#### **DITRD LG discretion to pay LGAs more than their annual allocation**

**3.1** Payments to LGAs under the AusLink R2R Program were funded from one of DITRD LG's administered annual appropriations. In this respect, \$307.5 million per annum between 2005–06 and 2008–09 was budgeted in administered expenses within DITRD LG's Outcome 1 ('A better transport system for Australia') for the formula component payments to LGAs.<sup>99</sup> Annual allocations to individual LGAs were based on the Annual Appropriations.

**3.2** DITRD LG aimed to draw up to, but no more than, the estimated expenses for each Annual Appropriation. As some LGAs had insufficient works to warrant being paid their full annual allocation in some years, in order to enable the full amount of estimated expenses to be realised each year, DITRD LG offered LGAs that had more works than their annual allocation the opportunity to be paid some or all of the following year's allocation in advance.

**3.3** The Notes on Administration stated (at clause 6.2) that payments in each financial year to each LGA would be capped at its annual allocation, except:

- LGAs with a life of program allocation of \$250 000 or less may receive their full life of program allocation on an 'as required' basis, on submission of quarterly reports providing details of actual and projected expenditure. Like the initial Program, this arrangement for accelerated funding to LGAs with a relatively small allocation was

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<sup>99</sup> With the exception that the 2005–06 PBS showed \$340.57 million for 2005–06, \$343 million for 2006–07 and \$330 million for 2007–08 and 2008–09 respectively.

intended to enable those LGAs to undertake 'sensible projects within a reasonable timeframe';

- limited flexibility was available to allow large projects to be undertaken in one or two financial years or where substantial savings would arise from undertaking particular works in a short timeframe; and
- where LGAs underspend in the last quarter of any financial year, the underspend may be reallocated to other LGAs at DITRDLG's discretion. Both the timing and amount of such reallocations were at the discretion of DITRDLG.

**3.4** In March 2006, as the end of the first financial year of operation of the AusLink R2R Program was approaching, DITRDLG advised LGAs that:<sup>100</sup>

If you do not draw down your full allocation this financial year, we cannot guarantee to make up the shortfall next year. You are not guaranteed the money until 2008–09.<sup>101</sup>

**3.5** DITRDLG also advised LGAs of the criteria it would use in exercising its discretion to reallocate funds, as follows:<sup>102</sup>

Based on our experience, some councils will not draw down their full allocation this financial year. Any funds not drawn down by these councils will be made available to other councils capable of using additional funds by 30 September.

The additional funds will be provided to councils seeking them in order from those with the smallest life of program allocations to the largest.

If this step still does not utilise available funds, a further call for projects will be made.<sup>103</sup>

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<sup>100</sup> R2R Circular 2006/3 issued on 14 March 2006.

<sup>101</sup> Section 6.2 of the Notes stated that: 'In any one year, the full allocation is available to the LGA'. In April 2010, DITRDLG clarified that: 'the shortfall was not guaranteed in the next financial year (2006–07), but the full (nominal annual) allocation remained available.'

<sup>102</sup> R2R Circular 2006/3 issued on 14 March 2006.

<sup>103</sup> This last sentence was omitted from similar R2R Circulars (2007/2 and 2008/2) issued on 13 March 2007 and 19 March 2008 respectively.

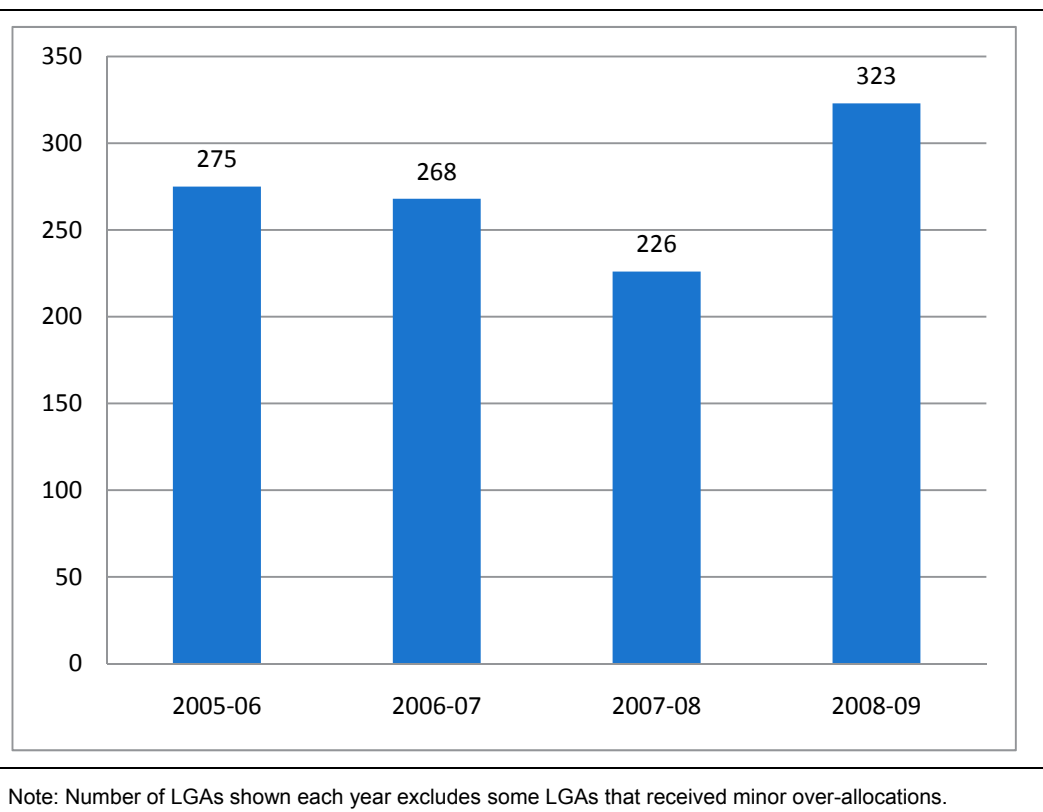
### *ANAO analysis*

**3.6** While DITRDLG was successful in encouraging LGAs to collectively claim the full amount of the annual R2R allocation (\$307.5 million per annum) during 2005–06, only \$304.4 million was claimed in 2006–07 and \$262.5 million in 2007–08. Accordingly, more than \$48 million in unspent program funds was transferred to 2008–09. In February 2010, DITRDLG advised ANAO that the movement of funds from 2007–08 occurred for two main reasons: the impending LGA amalgamations in QLD and NT meant that expenditure by many LGAs was reduced, and there was major flooding, particularly in QLD, which meant that R2R projects ceased while urgent repair work was undertaken with funding from sources other than the R2R Program.

**3.7** The number of LGAs that received more than their annual allocation during the life of the program is illustrated in Figure 3.1. While it would normally be expected that the quantum would decline each year as progressively more LGAs received their full program allocations, Figure 3.1 shows that this trend was reversed in the final year of the program.

**Figure 3.1**

**Number of LGAs that received more than their annual allocation during the period 2005–06 to 2008–09**



Source: ANAO analysis of DITRDLG data.

**3.8** Although some caution should be exercised when interpreting Figure 3.1 due to the impact of new and abolished LGAs (as commented by DITRDLG), Figure 3.1 does reflect the fact that during the final year of the program, around one-half of all LGAs were in ‘catch-up’ mode and needed to increase their R2R expenditure.

**3.9** In addition, Table 3.1 provides examples of LGAs with a final payout under the program that represented a significant proportion of their life of program allocation.<sup>104</sup> None of these LGAs are in NT and only two are in QLD.

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<sup>104</sup> DITRDLG provided explanations for the late draw down of funds for the three LGAs at the top of Table 3.1, as follows:

Footnote continued on the next page...

**Table 3.1****Examples of LGAs with significant final payout of AusLink R2R Standard Program funds**

LGA	State	Date of final payment	Life of Program allocation (\$)	Amount of final payment (\$)	Per cent of allocation
Coober Pedy	SA	18/5/09	139 831	124 856	89
Dundas	WA	18/5/09	663 244	535 197	81
Hopevale	QLD	2/3/09	217 790	163 343	75
Menzies	WA	18/5/09	1 298 522	769 360	59
Cue	WA	2/3/09	730 970	428 228	59
Wyndham East Kimberly	WA	18/5/09	2 031 529	1 168 729	58
Carrathool	NSW	2/3/09	3 640 994	1 801 240	49
Nannup	WA	2/3/09	2 021 968	971 482	48
Gosnells	WA	18/5/09	4 129 143	1 852 607	45
Tamworth	NSW	18/5/09	6 429 232	2 569 793	40
Mount Alexander	VIC	18/5/09	2 528 959	943 331	37
Townsville	QLD	2/3/09	3 728 554	1 301 715	35
Moorabool	VIC	18/5/09	3 213 175	1 043 206	32

Source: ANAO analysis of DITRDLG data.

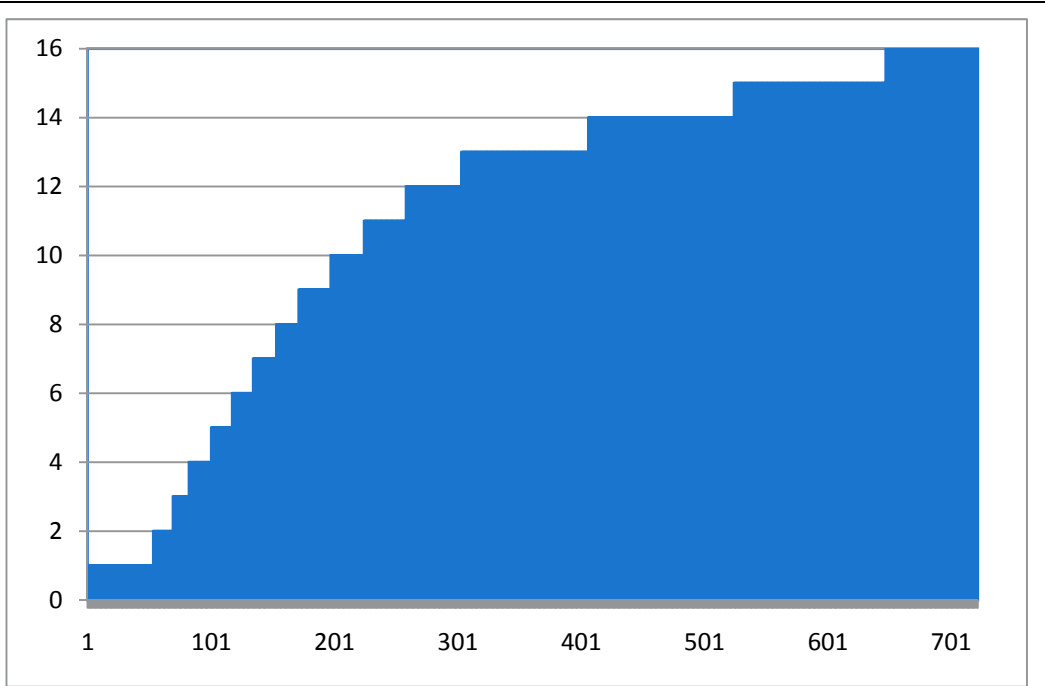
**3.10** Further in this respect, Figure 3.2 illustrates the duration from an LGA's first payment to their final payment for each of the 722 LGAs paid under the program. For example, 53 LGAs received their full entitlement in a single payment (that is, in one quarter), whereas 75 LGAs, or more than ten per cent, took the maximum duration of 16 quarters to claim all their payments.<sup>105</sup>

- Coober Pedy did not acquit its initial R2R Program funds until 13 March 2008. Funds were withheld until the acquittal was provided so that all funds had to be drawn down in the last payment of 2007–08 (\$14 975) and in 2008–09 (\$124 856);
- Dundas had a single major project which had been planned for completion earlier but was subject to a series of operational delays; and
- Hopevale received two payments, one for \$54 447 in December 2005 and another for \$163 343 in March 2009. However, this does not represent the timing of work done. The January 2009 expenditure report showed that much of the work charged against R2R was undertaken in 2006–07 and 2007–08.

<sup>105</sup> Figure 3.2 also shows, for example, that 123 LGAs took 15 quarters to claim all their payments, 118 took 14 quarters and 103 took 13 quarters.

**Figure 3.2**

**Duration of 722 LGAs' first to last AusLink R2R payment (in quarters)**



Note: Number of quarters duration does not reflect number of payments (many LGAs were not paid every quarter).

Source: ANAO analysis of DITRD LG data.

**3.11** The above analysis indicates that, notwithstanding there was funding certainty and LGAs had four years in which to plan their roadworks and undertake the expenditure of funds, the life of program allocations for many LGAs exceeded their capacity to spend, on eligible roadworks, the funding provided.<sup>106</sup> This situation should also be considered in the context of the relatively high incidence of LGAs that have difficulty maintaining their own source expenditure on roads at the same time as spending their R2R allocation.<sup>107</sup> ANAO suggests that both the quantum in the pool of potentially

<sup>106</sup> ANAO Audit Report No. 31 2005-06 also noted that there was a disproportionately large payout of program funds to LGAs in the final year of the initial R2R Program.

<sup>107</sup> In addition, in March 2009, ALGA wrote to the Minister for Infrastructure, Transport, Regional Development and Local Government requesting that consideration be given to widening the definition of 'roads' to include 'other transport infrastructure' as: 'A number of councils in urban areas have identified other transport infrastructure being of a higher priority than roads and have raised the possibility of using their R2R Program funding for those priorities'.



eligible roadworks within individual LGA area boundaries, and the LGA's capacity to undertake the required roadworks projects, should be factors taken into consideration when determining funding. Other relevant factors include the capacity of LGAs and/or contractors to increase the program of road works.

**3.12** Further, end-of-program lags in expenditure by LGAs may potentially be a compounding problem. As mentioned, LGAs had an additional six months after the Standard Program ended on 30 June 2009 to spend their program funds. In June 2009, DITRDLG advised LGAs that, in relation to funding provided under the Nation Building R2R Program:

... we will normally expect councils to spend their old program money before they spend their new program money.

**3.13** Final acquittal of AusLink R2R Program funds and exemptions granted by DITRDLG to LGAs that did not spend all their funds by the specified deadline are discussed later in this chapter.

**3.14** Against this background, in February 2010 DITRDLG commented to ANAO that:

Our consultations with LGAs and their approaches to government indicate that more funding is needed. We also believe that there is strong support among LGAs for the existing formula and the set life of program allocation as this provides certainty of funding. It would also be impossible to *[revise the allocation formula]* until after 2013–14 as the allocations for the Nation Building Roads to Recovery program have already been determined. Any decision to change the formula is a matter of government policy not an implementation matter.

## Payment principles

**3.15** DITRDLG recognised that it was important to time payments to LGAs so that they could undertake R2R works without transferring funds from their normal road activities.<sup>108</sup> At the same time, DITRDLG recognised that payments should not be made too far in advance of need as this would incur a cost to the Commonwealth, as well as adversely impacting on accountability.

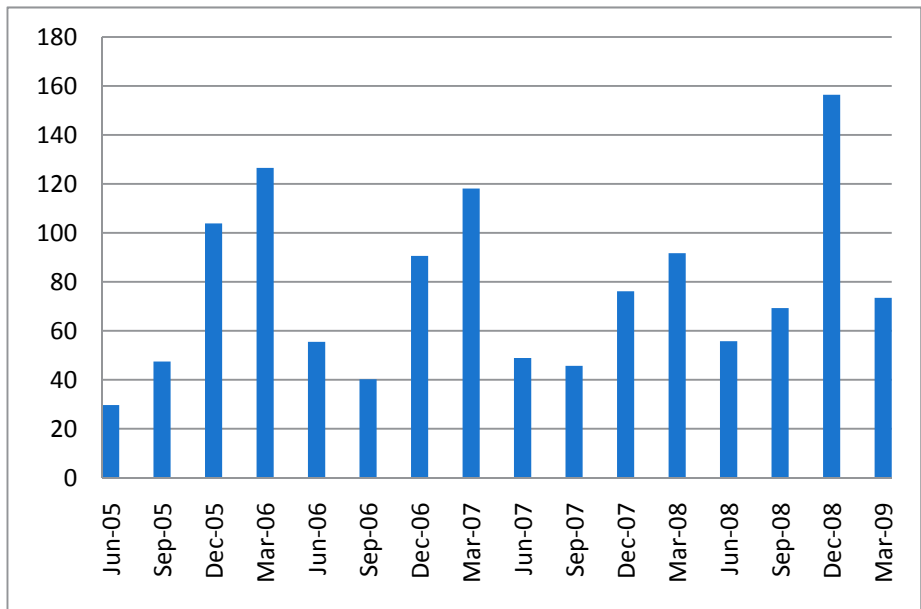
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<sup>108</sup> In this regard, in March 2006, DITRDLG advised the then Minister for Local Government, Territories and Roads that payments three months in advance was adopted for the initial R2R Program and AusLink R2R Program because the Government recognised that many councils might have had difficulty fully participating in the programs had they been required to fund projects themselves and seek reimbursement later, due to shortage of working capital.

**3.16** Accordingly, the practice that was adopted for the Standard Program involved paying LGAs quarterly in advance, based on quarterly reports that included data on expenditure to date and forecast expenditure for the next quarter. In this context, Figure 3.3 illustrates the total amounts paid each quarter over the life of the Standard Program.

**Figure 3.3**

**Total quarterly payments made over the life of the AusLink R2R Standard Program (\$ million)**



Source: ANAO analysis of DITRD LG data.

**3.17** The Notes stated that payments would be made on the 15th day of August, November, February and May each year.<sup>109</sup> However, for all except one of the 16 quarterly payments made during the life of the program, DITRD LG had difficulty in adhering to this schedule, as illustrated in Table 3.2.

<sup>109</sup> However, R2R Circular 2005/15 issued on 6 December 2006 advised LGAs that: 'As many people will be on leave in early January, we will extend the reporting period until 15 February. The next payment will be made in late February or early March.'

**Table 3.2****Timeliness of AusLink R2R Program quarterly payments**

Scheduled payment date	Actual payment date	Days late (early)
15/08/2005	22/09/2005	38
15/11/2005	2/12/2005	17
15/02/2006	17/03/2006	30
15/05/2006	19/05/2006	4
15/08/2006	18/08/2006	3
15/11/2006	23/11/2006	8
15/02/2007	1/03/2007	14
15/05/2007	31/05/2007	16
15/08/2007	17/08/2007	2
15/11/2007	22/11/2007 <sup>1</sup>	7
15/02/2008	4/03/2008	18
15/05/2008	20/05/2008	5
15/08/2008	13/08/2008	(2)
15/11/2008	19/11/2008	4
15/02/2009	2/03/2009	15
15/05/2009	18/05/2009	3
Note 1: A small number of the payments due on 15 November 2007 were made on 14 November 2007 (three per cent by value).		

Source: ANAO analysis of DITRDLG data.

**3.18** As mentioned, under the Supplementary Program, each eligible LGA also received a once-only payment on 27 June 2006 equivalent to one quarter of its total allocation under the Standard Program.<sup>110</sup>

## Cash management

**3.19** ANAO's Administration of Grants Better Practice Guide states that cash management principles should be considered when paying grants in advance.<sup>111</sup> In this regard, the Department of Finance and Deregulation has

<sup>110</sup> Twenty one smaller LGAs received Supplementary Program payments (totalling \$437 621) but did not receive any payments under the Standard Program. In comparison, 41 LGAs that received Standard Program payments did not receive a Supplementary Program payment.

<sup>111</sup> ANAO, *Administration of Grants Better Practice Guide*, May 2002, p. 31.

issued a number of Finance Circulars over the years stating that early payment of public monies should only be considered where there is a financial benefit to the Commonwealth.<sup>112</sup> Specifically, Finance Circular 2004/14, states that:

Efficient, effective and ethical management of Commonwealth resources includes making payments no earlier than necessary having regard to program and service delivery objectives. As such, prepayments and early payments should only be made where there is a benefit to the Australian Government after taking all costs and risks into account.

If agencies pay suppliers or contractors earlier than required, the interest on the Australian Government's money held centrally with the Reserve Bank of Australia is reduced. Agencies should take this whole of government impact into consideration when assessing prepayments and early payments.

**3.20** It was intended that R2R Program funds would be provided to LGAs quarterly in advance (subject to annual allocation caps) based on the information submitted by LGAs in quarterly reports (cumulative expenditure and forecast expenditure). This meant that, by design, the program included allowance for LGAs to hold funds for up to three months before being used. This was seen as necessary so that LGAs could undertake R2R works without transferring funds from their normal road activities.

**3.21** Payment three months in advance provided a potentially significant financial advantage to LGAs at the expense of the Commonwealth. ANAO estimates that the cost to the Commonwealth of payments quarterly in advance would have been up to \$16.3 million, had funds been held by LGAs for the full three months prior to being spent on road works. The data obtained by DITRDLG from LGAs do not enable a precise calculation to be undertaken. If all funds had been used by LGAs within one and a half months of payment by DITRDLG, the estimate would reduce to \$8.1 million.

**3.22** DITRDLG also scheduled R2R payments for around the middle of the relevant quarter. Accordingly, LGAs that spent the full amount of their forecast expenditure effectively were not paid in advance.

**3.23** In addition to the intended benefit of payments up to three months in advance of need, ANAO's examination of a sample of LGAs revealed many

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<sup>112</sup> See Finance Circular 1995/3 *Cash Management: Timing of Payments Contractors and Traders, Lease Versus Buy*; Finance Circular 1997/09, *Payment of Accounts—Auditor-General's Report No.16 1996–97*; and Finance Circular 2004/14, *Discounts for prepayment and early payment*.

instances of LGAs being paid more than three months in advance of the expenditure of R2R funds. This resulted from:

- accelerated funding during the last quarter of each financial year (so as to fully expend the annual program allocation) notwithstanding that these payments did not reflect LGA cash flow needs;
- overstated expenditure reported by some LGAs in their quarterly reports (see paragraphs 3.42 to 3.34);
- unreliable expenditure forecasts submitted by some LGAs in their quarterly reports (see paragraphs 3.45 to 3.46); and
- non compliance with the six months rule (and in some cases delays on projects resulting in waivers of the six months rule) (see paragraphs 3.63 to 3.78).

## Accelerated funding

**3.24** During the first two years of the program, almost 300 LGAs each year received accelerated funding totalling \$43.3 million and \$57.8 million respectively.<sup>113</sup> In this context, throughout the life of the program, LGAs were able to receive accelerated payments in four circumstances.

### Accelerated funding to smaller recipients

**3.25** The first type of accelerated funding involved LGAs with a small total allocation. Specifically, the Notes provided that LGAs with an entitlement to receive \$250 000 or less in total grants over the life of the program could receive their total allocation on an 'as required' basis. In such cases, LGAs needed to include sufficient works to support full payment. During the first two years of the program, 28 LGAs qualified for this treatment.

**3.26** The second type of accelerated funding involved LGAs with a total allocation of \$250 000 to \$1 million. Up to \$250 000 in any one year could be received, or up to \$400 000 'in exceptional cases with detailed justification.' In total, five LGAs qualified for this treatment during the first two years of the

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<sup>113</sup> R2R Circular 2005/12 issued on 20 September 2005 advised LGAs that: 'The last payment to councils (first payment under the AusLink R2R Program) totalled only \$30 million, only ten per cent of the 2005-06 appropriation. Councils will need to accelerate their use of R2R funds to ensure that the funding available is fully drawn down by the end of the financial year, so I would appreciate your attention to this matter.'

program (including two that were paid more than the designated \$400 000 limit, receiving \$587 220 and \$482 000 respectively).

### **Accelerated funding to other recipients**

**3.27** The third type of accelerated funding involved LGAs with large projects to be undertaken in one or two financial years or where substantial savings would arise from undertaking particular works in a short timeframe. DITRDLG was unable to advise ANAO which LGAs had received accelerated funding under this provision of the Notes (section 6.2(c)). In this regard, in April 2010 DITRDLG advised ANAO that a register of requests for accelerated funding under the equivalent provision for the Nation Building Program is being maintained.

**3.28** The final category under which LGAs could obtain accelerated funding was in relation to DITRDLG's discretionary reallocation of funds unspent in the last quarter of each financial year. Where surplus funds remained available after allowing for redistributions under the first three types of accelerated funding, DITRDLG reallocated these funds to LGAs that had indicated in their work schedules that they had sufficient projects planned to enable expenditure of the additional funds within three months, or if funds were still not exhausted, within six months. The majority of reallocations (by both number and value) were of this type.

#### ***2006–07 funds reallocations***

**3.29** R2R Circular 2007/2 issued on 13 March 2007 stated that the quarterly reporting site will reopen on 1 April 2007 and close on 30 April 2007. This Circular also advised LGAs about the possibility of bringing forward funding above nominal annual allocations, as follows:

Each LGA has a nominal annual allocation which normally forms the cap for that LGA each financial year. However, some LGAs might not seek their full allocation this financial year. Any funds not provided to the LGAs will be made available to other LGAs capable of using the funds via the following process:

- (a) unallocated funds will be reallocated to LGAs capable of spending them in the period to 31 July 2007; and
- (b) if there are still unallocated funds, these will be reallocated to LGAs capable of spending them in the period to 30 September. If you wish to benefit from this redistribution, you should enter into your (March) Quarterly Report

projects capable of utilising extra money by 30 September (2007), ensuring that you are realistic about the timeframe you specify.

The additional funds will be provided to LGAs seeking them in order from those with the smallest life of program allocations to the largest.

Please note that this will bring forward funds from later years. It will not be an increase in your life of program allocation.

**3.30** The March 2007 Quarterly Reports submitted by LGAs were printed by DITRDLG on 8 May 2007 and placed on the respective LGAs' files. Handwritten adjustments to a number of the reports were subsequently made by DITRDLG staff between 16 and 21 May 2007 to increase the amounts to be paid. These amendments were approved by the delegate on 26 May 2007. Nevertheless, there is a risk to the transparency of the processes used when quarterly reports submitted by LGAs are amended after the cut-off date (when in theory they had been 'locked in', following the closure of the reporting site).

**3.31** Four LGAs where this occurred were included in the ANAO sample, for which the increases totalled \$2 593 512 (see Table 3.3). In each case, the increases were supported by revised LGA work schedules. However, there were a number of instances where ANAO's analysis of accelerated payments revealed that works were not undertaken as proposed by LGAs when they requested accelerated funding. As a result, funds remained unused with the LGAs for a considerable period of time. This provided the relevant LGAs with a financial benefit, at the expense of the Australian Government.

**Table 3.3**

**Increased payments for adjusted March 2007 Quarterly Reports**

LGA	Payment due as per submitted Quarterly Report (\$)	Revised payment following departmental adjustment (\$)	Increase (\$)
Blacktown	693 577	1 962 378	1 268 801
Baw Baw	35 408	845 258	809 850
East Gippsland	1 116 881	1 416 881	300 000
Yarra Ranges	663 844	878 705	214 861

Source: ANAO analysis of LGAs March 2007 Quarterly Reports and DITRDLG records.

## Analysis of Quarterly Reports

**3.32** Quarterly Reports submitted by LGAs provided details on actual and forecast expenditure for each project listed in the works schedule. The Notes

included a proforma of the Quarterly Report. This proforma was also on the secure website for LGAs to complete.<sup>114</sup>

**3.33** Based on quarterly reports submitted by LGAs, DITRDLG produced a report with details of projects nominated by LGAs for R2R funding. This report included works details from the works schedule together with cumulative expenditure and forecast expenditure submitted by the LGA in its most recent quarterly report.

**3.34** Subject to its overall allocation and the annual payment cap, the following calculation determined the amount that was to be paid to each LGA:<sup>115</sup>

Reported expenditure to date (for all R2R Standard Program projects)  
Plus: Reported forecast expenditure (for all R2R Standard Program projects)  
Less: Total payments previously made  
Equals: Payment to be made.

**3.35** In this context, it was important that LGA quarterly reports included:

- accurate figures for total expenditure to date (that is, the sum of cumulative expenditure on each project); and
- reliable expenditure forecasts.

**3.36** ANAO found that this was often not the case for a number of LGAs, as outlined below.

## **Analysis of cumulative expenditure**

**3.37** LGAs were required to include in their quarterly reports the cumulative expenditure on each project. As outlined above, DITRDLG used the aggregate cumulative expenditure figure for all projects as part of its calculation of the amount, if any, to be paid to each LGA. DITRDLG did not, however, have systems and procedures in place to analyse the cumulative

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<sup>114</sup> While the term 'Quarterly Report' suggests that reports were required to be submitted quarterly by LGAs, many times they were not. Instead, LGAs often only submitted Quarterly Reports when they sought further funds.

<sup>115</sup> DITRDLG's Payment Calculation Form also required departmental officers to, after calculating the amount payable, satisfy themselves that all projects were road projects and that a satisfactory R2R Annual Report had been submitted.



expenditure reported against each project in the current quarterly report against:

- previous quarterly reports;
- R2R Annual Reports; and/or
- any other information submitted by LGAs.

**3.38** In this context, as part of this performance audit, ANAO analysed the quarterly reports submitted to DITRD LG over the life of the AusLink R2R Program.

#### *Reductions in cumulative expenditure*

**3.39** ANAO analysis of quarterly reports identified that many LGAs reported reductions in cumulative expenditure for one or more projects. As a result of these 966 reductions in project expenditure, 100 LGAs had their total cumulative expenditure for the program fall in one or more quarters. The aggregate reduction was \$11.8 million.

**3.40** As cumulative expenditure is a cash figure, reductions in these figures generally should not, in the absence of reporting errors, occur. Accordingly, after this issue was raised by ANAO, the department sought advice from a selection of LGAs on the identified anomalies, with the following results:

Of the first 16 projects with reductions in cumulative expenditure (of 966 instances) shown on the ANAO spreadsheet:

- one was withdrawn (Townsville);
- seven were data entry errors i.e. no figure was entered in the relevant Quarter against the project (Brisbane, Burke [twice], Litchfield, and Murchison [twice]) or the wrong figure was entered (Loxton Waikerie). The entry of a wrong or low figure directly generated the reduction; and
- the rest were errors of various kinds where councils entered figures above the actual figures.

The system is set up so that errors such as these can be corrected in later reports and, in each of the above cases, they were. Further, some of the errors (e.g. where a cumulative expenditure figure was entered in excess of the R2R component), are now not possible under IMS which has checks in place to stop this happening.

A check of (several) cases where overall council cumulative expenditure fell indicates that a reduction in cumulative expenditure on an individual project flowed through to the overall council figure.

**3.41** For the case group referred to DITRDLG, ANAO identified more than 120 instances (13 per cent) where the LGA simply omitted to include the figure for cumulative expenditure, notwithstanding that the LGA had previously reported expenditure for the same project. Notwithstanding that DITRDLG had already implemented one system check to reduce preventable errors (referred to above), ANAO suggested that the feasibility of further enhancing IMS system checks and associated warning messages (to LGAs and DITRDLG) should be explored.

#### *Cumulative expenditure compared to R2R Annual Reports*

**3.42** ANAO analyses also involved comparing the data included in the quarterly reports to the financial data in the R2R Annual Reports.<sup>116</sup> Specifically, ANAO compared expenditure reported by LGAs in their R2R Annual Report at 30 June each year to cumulative expenditure reported in each June R2R Quarterly Report. In this respect, the cumulative amounts reported in R2R Annual Reports as having been expended as at 30 June should have been equal to the amounts reported in the June Quarterly Report for the corresponding year.<sup>117</sup>

**3.43** This analysis revealed anomalies for a number of LGAs, as shown in Table 3.4.

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<sup>116</sup> The Annual Report was the authoritative document submitted by LGAs to account for the use of R2R funds and certify that the conditions of the R2R Program had been complied with.

<sup>117</sup> However, some minor differences may be expected, because after 31 December 2006, LGAs had the option of reporting on either a cash or accruals basis for quarterly reports, but throughout the life of the program were required to only use cash accounting in R2R Annual Reports. There was no mechanism for LGAs to advise DITRDLG which option had been adopted in their quarterly reports. The quarterly reports submitted from July 2005 to September 2006 were required to be prepared on a cash basis.

**Table 3.4****Analysis of LGAs June Quarter reported cumulative expenditure (percentage of instances)**

Financial Year	June Quarterly Report expenditure to date higher than Annual Report cumulative expenditure	June Quarterly Report expenditure to date lower than Annual Report cumulative expenditure	June Quarterly Report expenditure to date equal to Annual Report cumulative expenditure
2005–06	28%	28%	45%
2006–07	25%	44%	31%
2007–08	36%	25%	39%
<b>Total</b>	<b>29%</b>	<b>32%</b>	<b>38%</b>
Note: This table excludes 2008–09 results, which are not comparable to other years because a number of Annual Reports had not been submitted at the completion of audit fieldwork (as at 31 December 2009).			

Source: ANAO analysis of LGA documentation (Quarterly and Annual Reports) submitted to DITRDLG.

**3.44** LGAs that overstated their cumulative expenditure in their quarterly reports obtained a financial benefit at the expense of the Australian Government. That is, the receipt of program funds occurred earlier than was intended under the program funding conditions. ANAO analysis indicated that the total amount overstated in June Quarterly Reports across the first three years of the program for LGAs in the sample was \$7.3 million.<sup>118</sup> Table 3.5 shows examples of LGAs where expenditure was overstated by more than \$250 000.

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<sup>118</sup> Excludes 2008–09.

**Table 3.5****Examples of overstated June Quarter reported cumulative expenditure**

State	LGA	Financial year ended	Annual Report cumulative expenditure (\$)	June Quarter reported cumulative expenditure (\$)	Total of overstated expenditure (\$)
ACT	TAMS	Jun-06	8 972 323	13 972 363	5 000 040
VIC	Pyrenees	Jun-08	1 925 500	2 673 412	747 912
QLD	Toowoomba Regional	Jun-08	965 238	1 636 947	671 709
QLD	Gold Coast City	Jun-06	6 008 765	6 571 066	562 301
VIC	Casey	Jun-08	2 878 933	3 406 571	527 638
VIC	Wyndham	Jun-08	1 034 000	1 551 000	517 000
VIC	Baw Baw	Jun-07	2 448 821	2 911 311	462 490
WA	Narembeen	Jun-06	326 128	788 530	462 402
QLD	Bulloo	Jun-07	843 580	1 289 390	445 810
NSW	Coffs Harbour	Jun-08	1 743 725	2 184 387	440 662
VIC	Mornington Peninsula	Jun-08	2 128 832	2 496 576	367 744
VIC	Moreland	Jun-08	1 081 956	1 432 505	350 549
SA	Campbelltown	Jun-08	667 489	992 500	325 011
VIC	Casey	Jun-06	712 933	1 034 000	321 067
WA	Murchison	Jun-06	315 000	625 232	310 232
NSW	Brewarrina	Jun-07	316 415	609 819	293 404
Note: LGAs other than Baw Baw and Casey were not included in the ANAO sample.					

Source: ANAO analysis of LGA documentation (Quarterly and Annual Reports) submitted to DITRD LG.

## Expenditure forecasts

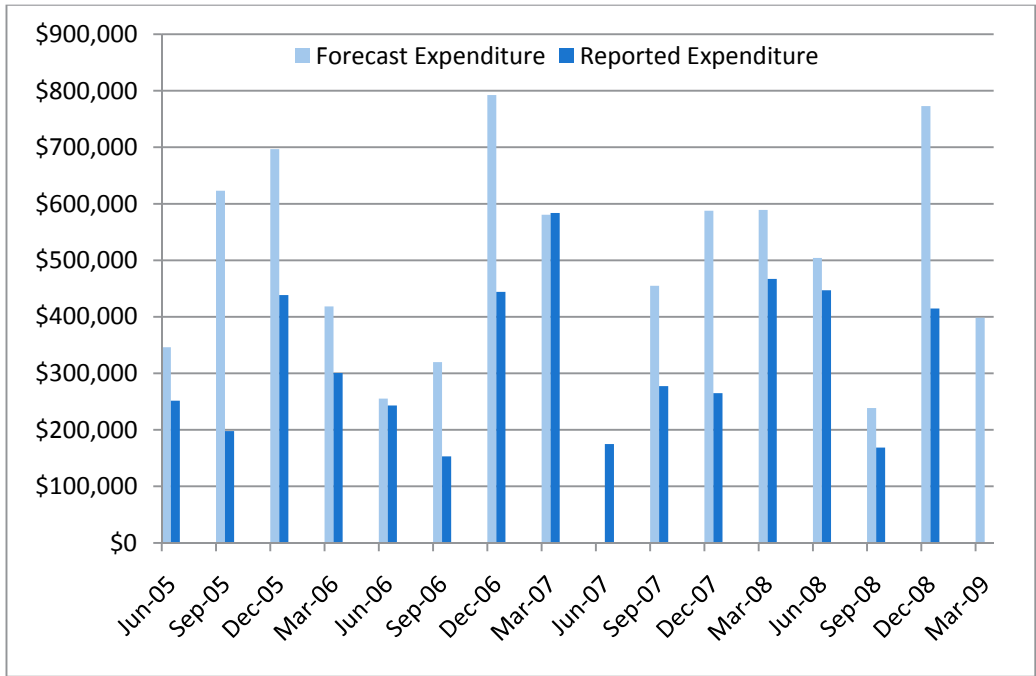
**3.45** In addition to reported expenditure to date, payments under the Standard Program were made to LGAs by DITRD LG based on the forecast expenditure reported by the LGA in its quarterly reports.

**3.46** In the above context, it was important that the forecasts made by LGAs of the expenditure they expected to incur in the following period were accurate. However, ANAO analysis identified that three out of every four

LGA in the sample had forecast expenditure reported in one or more quarterly reports but where little, or no, expenditure was reported in the following quarterly report.<sup>119</sup> This raised questions about the veracity of the forecasts. Figure 3.4 and Figure 3.5 show examples where LGA expenditures were often significantly different to that which had been forecast.

Figure 3.4

Clarence Valley (NSW) reported forecast and actual expenditure

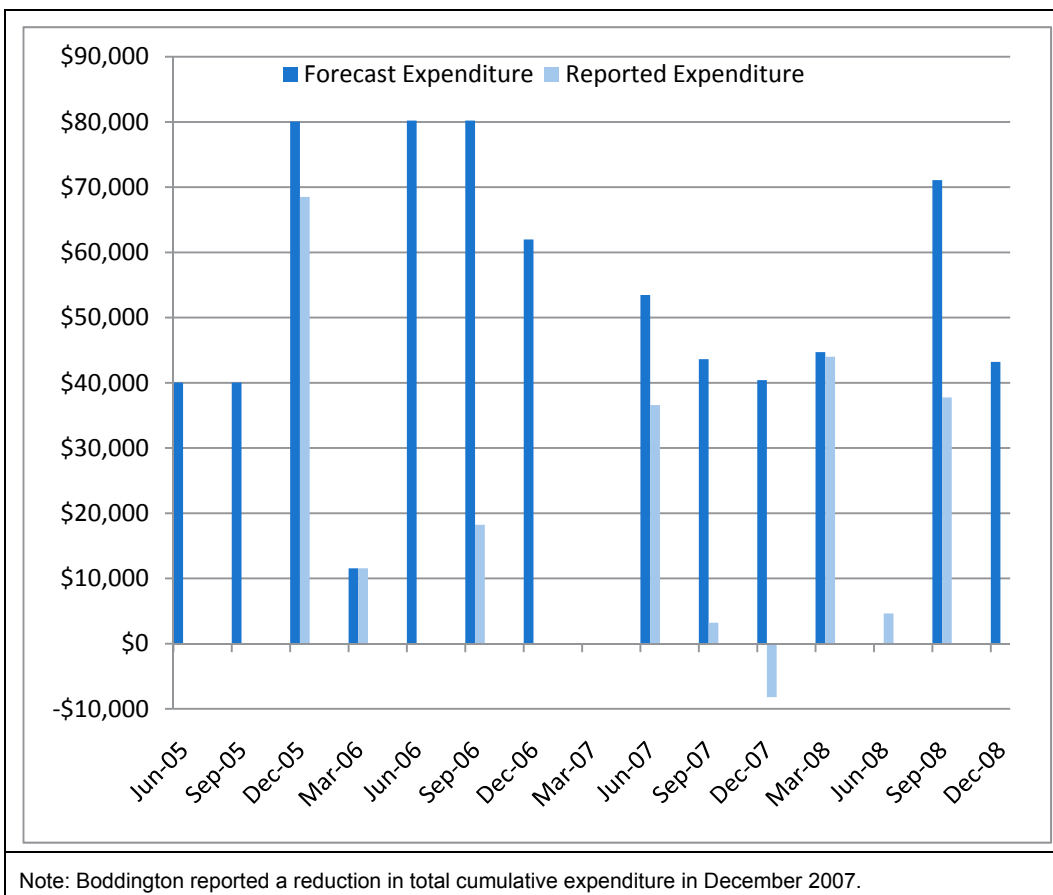


Source: ANAO analysis of Clarence Valley Quarterly Reports.

<sup>119</sup> This figure comprised LGAs where ten per cent or less of a quarter's forecast expenditure was spent in the subsequent quarter.

**Figure 3.5**

**Boddington (WA) reported forecast and actual expenditure**



Source: ANAO analysis of Boddington Quarterly Reports.

## Payments in arrears

**3.47** As mentioned, the AusLink R2R Program was designed to pay LGAs in advance. In this regard, R2R Circular 2005/14 issued on 10 November 2005 advised LGAs that:

Some councils appear to believe that only expenditure already incurred can be claimed. This is not so. The Government intends that councils will not be out of pocket as a result of this program and there is explicit provision in the funding conditions (clause 4.10) to allow councils to claim their estimated expenditure for the three months from the beginning of the reporting period...as well as expenditure already incurred. It is recognised that estimates are always subject to change as projects progress.

**3.48** Notwithstanding that payment in advance was intended to be the norm, ANAO found that, over the life of the program, 90 per cent of LGAs (650 of 722) were reimbursed in arrears in one or more quarters, after expending their own funds on their R2R projects. Some 54 per cent of all R2R payments made under the Standard Program were reimbursements to LGAs (2 682 of 4 976), comprising one in every three quarterly reports submitted to DITRDLG (2 682 of 8 086).

## **Requirement to submit quarterly reports**

**3.49** LGAs were required to submit a quarterly report before their first payment could be made. It was also generally expected that LGAs would continue to submit these reports quarterly throughout the life of the program, but there was no requirement to submit any further reports after an LGA received its final Standard Program payment. LGAs had up to four weeks after the close of the quarterly reporting period in which to electronically submit their reports (six weeks for December Quarterly Reports).<sup>120</sup>

**3.50** On 16 January 2006, LGAs that had not submitted their December 2005 Quarterly Report were reminded by a DITRDLG email that all quarterly reports were mandatory under the AusLink R2R Program. However, on 7 June 2006, the Notes (at section 7.1) were amended to advise LGAs that there is no breach of the funding conditions if LGAs fail to lodge a quarterly report.<sup>121</sup> Notwithstanding, the amended Notes stated that the quarterly reports provide one means for DITRDLG to monitor expenditure of R2R funds and that they are a requirement of the program.

**3.51** Analysis by ANAO indicated that, overall, eight per cent of the quarterly reports required<sup>122</sup> during the life of the Standard Program (707 of 8 793) were not submitted. Figure 3.6 shows that LGAs' performance in

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<sup>120</sup> Notes on Administration section 6.10. However, in section 7.1, the December quarter due date was stated as end January each year.

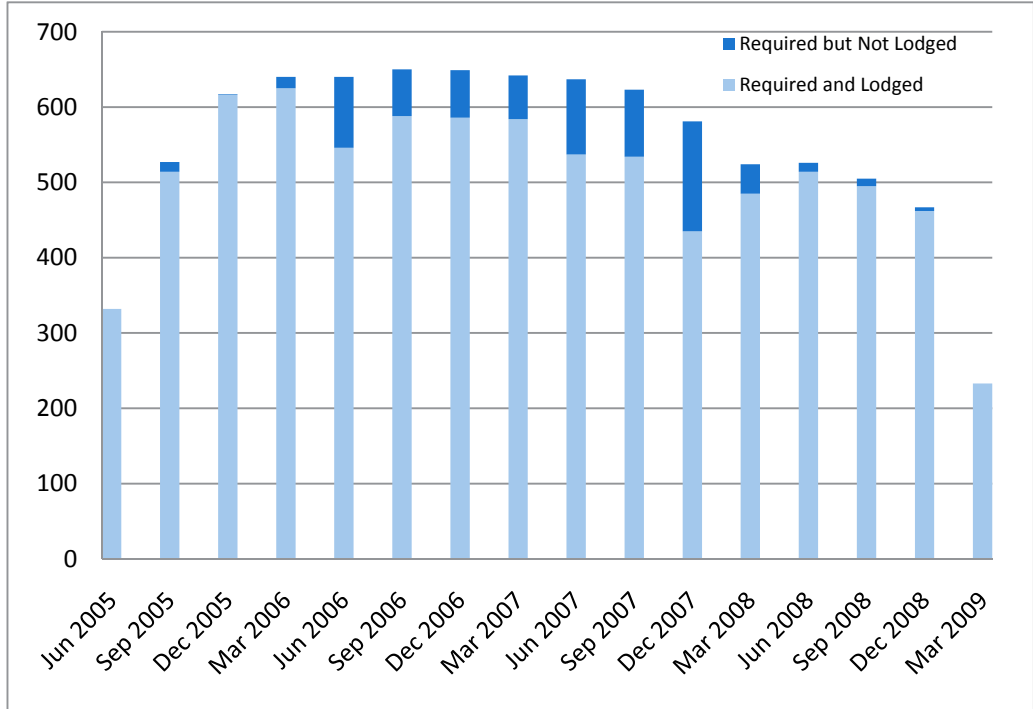
<sup>121</sup> LGAs were also advised in R2R Circular 2006/9 issued on 7 June 2006. In June 2006, the following paragraph was deleted from section 7.1 of the Notes:

LGAs are required to submit quarterly reports until all funds allocated for projects are expended. LGAs in breach of this requirement will be in breach of the funding conditions and will not receive funding until the next quarterly report is submitted.

<sup>122</sup> In this context, 'required' means that a report was required in each quarter from when the LGA first submitted a report, through to the report submitted by the LGA that resulted in their final AusLink R2R payment.

submitting quarterly reports varied during the program. For example, more than 25 per cent of the required reports were not submitted for the December 2007 quarter. Across the 41 LGAs in the ANAO sample, 15 LGAs failed to submit 28 quarterly reports required for the Standard Program (NSW three per cent, VIC three per cent and WA eight per cent).<sup>123</sup>

**Figure 3.6**  
**Number of Quarterly Reports required and submitted for the period June 2005 to March 2009**



Source: ANAO analysis of DITRDLG data.

### Supplementary Program Quarterly Reports

**3.52** Inconsistent advice was provided by DITRDLG to LGAs on the requirement for quarterly reports for the Supplementary Program. Specifically:

- on 15 May 2006, DITRDLG advised LGAs that Supplementary Program quarterly reports were required under the funding conditions approved by the then Minister;

<sup>123</sup> Six were not submitted for five NSW LGAs, five were not submitted for four VIC LGAs, and 17 were not submitted for six WA LGAs.



- a little over one year later, LGAs were advised in an R2R Circular<sup>124</sup> that these reports were not required at this time and that a reporting module would be included in an upgraded computer system to be implemented shortly; however
- three months later, on 28 August 2007, the then Minister did not agree to DITRDLG's proposal to delete the sections of the Supplementary Program funding conditions that required LGAs to submit quarterly reports.<sup>125</sup>

**3.53** Accordingly, on 10 September 2007, DITRDLG advised LGAs that the previous advice was incorrect and that the reports were still required.<sup>126</sup> LGAs were requested to submit hardcopies of the reports for each quarter in 2006–07 and the first quarter of 2007–08, pending availability of the electronic lodgement facility, which was then expected to be operational by mid-December 2008. Reports due after December 2008 were to be submitted electronically. Any LGAs that did not submit quarterly reports for the Supplementary Program would be in breach of the funding conditions<sup>127</sup> (which was a more stringent approach than the Standard Program where, as mentioned, the obligation was to submit 'required' quarterly reports).

**3.54** In relation to the 41 LGAs in the ANAO sample, 15 LGAs (37 per cent) did not submit their Supplementary Program September 2006 to September 2007 inclusive quarterly reports (required to be submitted with LGAs' 2007-08 Supplementary Program Annual Reports). No follow-up by DITRDLG was evident on the relevant LGAs' files. For the remaining 26 LGAs in the sample, one-half of the LGAs submitted the Supplementary Reports by the due date and one-half were late.

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<sup>124</sup> R2R Circular 2007/3 issued on 28 May 2007.

<sup>125</sup> Section 3.2 stated: 'To enable the department to monitor the expenditure of the Supplementary Roads to Recovery funds, it is required that funding recipients submit expenditure reports in the form specified by the department showing the expenditure for each quarter, beginning with the quarter ending on 30 September 2006 as follows:

- (a) In respect of the quarter 1 January to 31 March: by the following 30 April;
- (b) In respect of the quarter 1 April to 30 June: by the following 31 July;
- (c) In respect of the quarter 1 July to 30 September: by the following 31 October; and
- (d) In respect of the quarter 1 October to 31 December: by the following 31 January.'

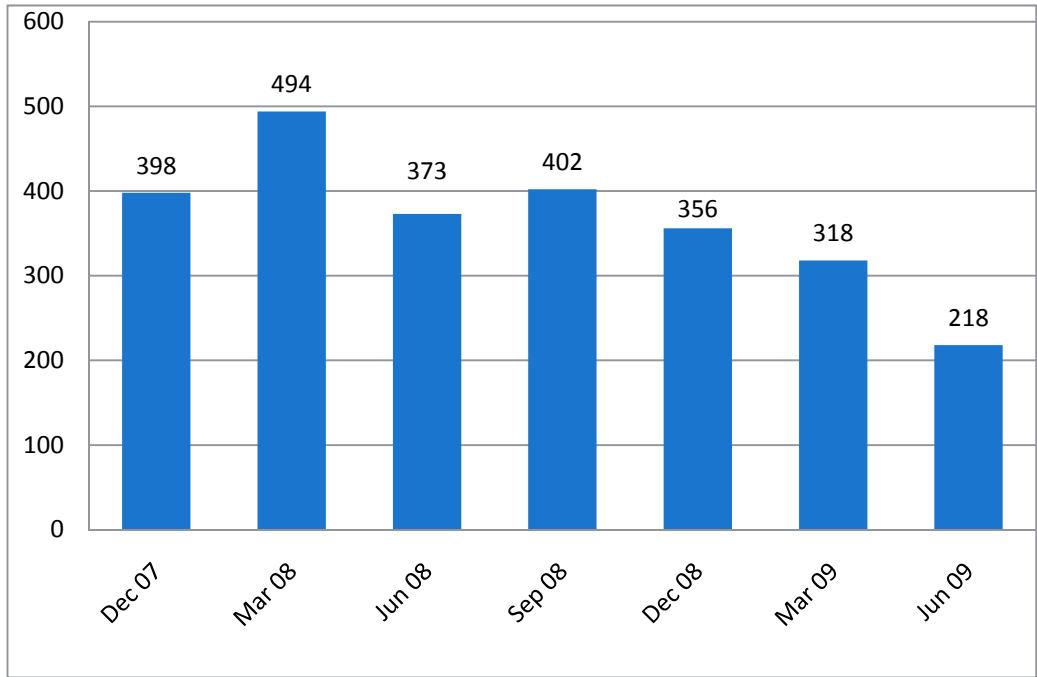
<sup>126</sup> R2R Circular 2007/7 issued on 12 September 2007 also advised of the requirement to submit Supplementary Program quarterly reports.

<sup>127</sup> Notwithstanding, DITRDLG did not issue exemptions (waivers) under section 91(1) of the AusLink Act.

**3.55** One or more Supplementary Program quarterly reports to be submitted electronically from December 2007 were not lodged (where required) by ten LGAs in the ANAO sample (six per cent of required reports). Figure 3.7 shows the number of reports submitted electronically by all LGAs for the period December 2007 to June 2009.

**Figure 3.7**

**Number of Supplementary Program quarterly reports submitted electronically for the period December 2007 to June 2009**



Source: ANAO analysis of DITRDLG data.

**3.56** On 11 May 2009, written procedures for quarterly report follow up were approved by DITRDLG. These procedures require quarterly reports to be submitted for all R2R funding recipients that have not fully spent their funds. In this regard, the procedures also state that, where an LGA that should have submitted a report fails to do so, it will be contacted by letter.<sup>128</sup>

**3.57** Table 3.6 shows aggregate expenditure reported by LGAs for each year of the R2R Supplementary Program.

<sup>128</sup> The Procedures were approved after the deadline for submitting final AusLink R2R Program quarterly reports (30 April 2009).

**Table 3.6****Supplementary Program annual expenditure by LGAs for the period 2006–07 to 2008–09**

	Amount (\$)	Per cent	Progressive per cent
2006–07	111 687 917	36.3	36.3
2007–08	81 363 969	26.5	62.8
2008–09	70 350 358	22.9	85.7
<b>Total</b>	<b>263 402 244</b>	<b>85.7</b>	

Source: ANAO analysis of DITRDLG data.

**3.58** Up to 31 December 2009, some 33 LGAs had reported to DITRDLG that their Supplementary Program funding had not been fully expended by 30 June 2009. The amount carried forward totalled just over \$5.9 million.<sup>129</sup> In April 2010, DITRDLG advised ANAO that all but two LGAs had spent their supplementary funds.

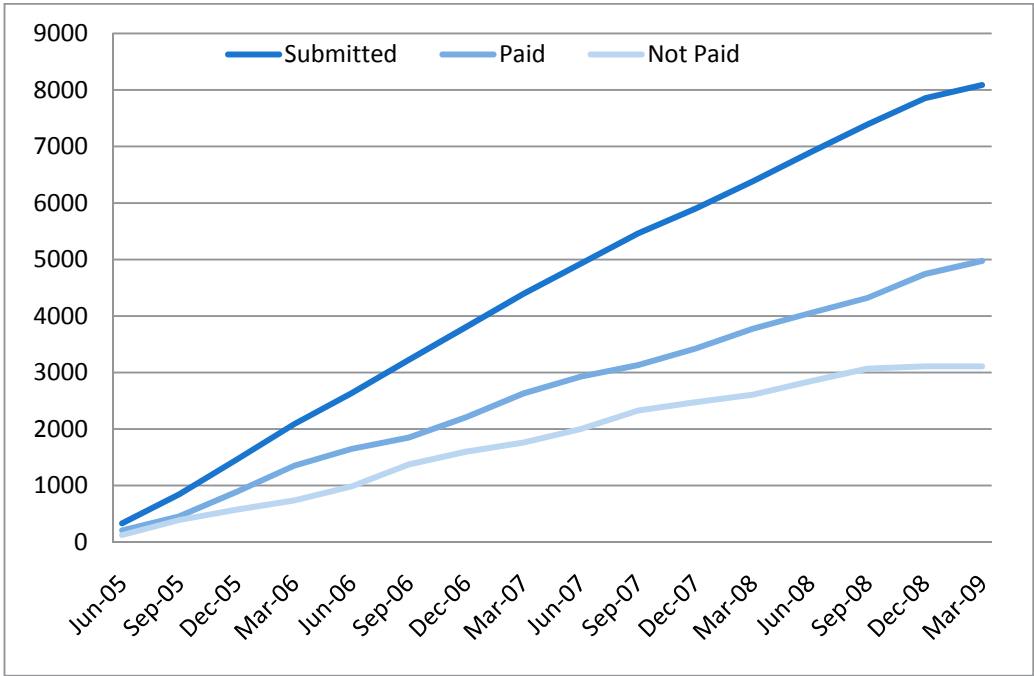
*Payments based on Quarterly Reports*

**3.59** ANAO analysis of payments made under the Standard Program indicated that only 62 per cent of the quarterly reports that were submitted to DITRDLG resulted in a payment to the LGA. This is illustrated in Figure 3.8. In those instances where a report was submitted but no payment made, this was because no R2R funds were required by the LGA at the time in 68 per cent of cases. In the remaining 32 per cent of cases, the LGA was not paid for various other reasons, including because an Annual Report was outstanding. In this respect, there would be benefit in DITRDLG developing a series of standard codes to capture data on the range of reasons why LGAs were not paid.

<sup>129</sup> Of the remaining balance of Supplementary Program funds (just over \$38 million), it was not possible to determine how much remained unspent at 30 June 2009 because a number of LGAs had outstanding 2008-09 Annual Reports.

Figure 3.8

Number of quarterly reports submitted (paid and not paid)

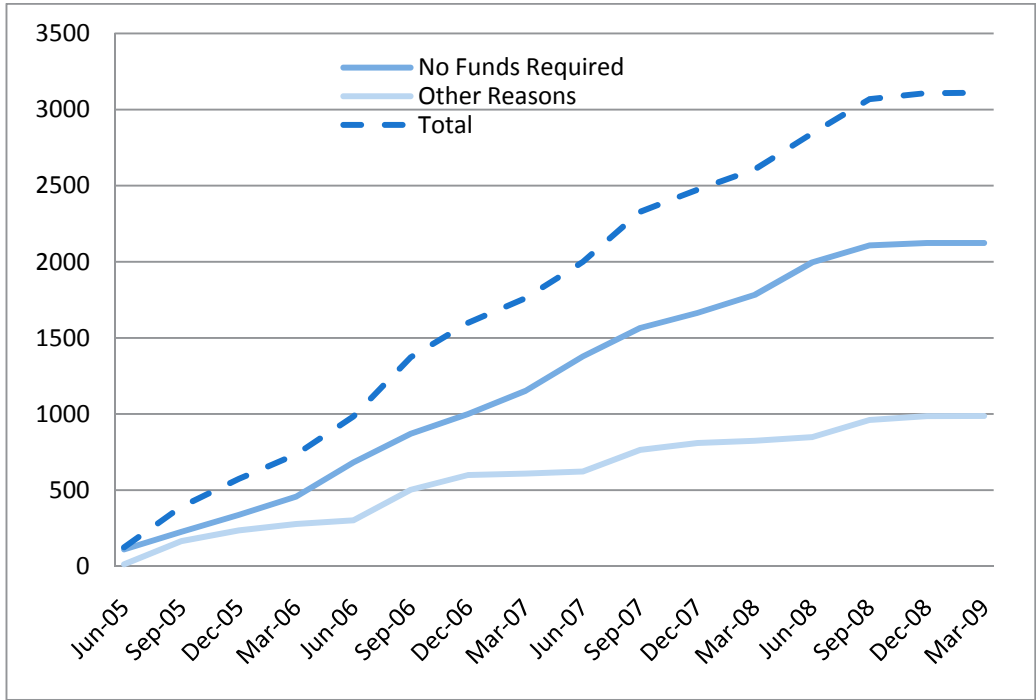


Source: ANAO analysis of DITRDLG data.

**3.60** Figure 3.9 illustrates the trends in the number of reports submitted that did not generate a payment, either because no funds were required by the LGA, or DITRDLG had a reason to withhold the payment.

Figure 3.9

Quarterly reports submitted with no consequent payment made



Source: ANAO analysis of DITRDLG data.

Small value payments

**3.61** ANAO noted that 295 payments (six per cent of all payments made) were in the range \$1 to \$10 000. There were 18 payments under \$100 and a total of 62 payments under \$1 000.

**3.62** In September 2009, ANAO suggested to DITRDLG that a suitable threshold be introduced to avoid making small payments. In this regard, DITRDLG advised ANAO that:

Consideration will be given to amending the Internal Operating Procedures to cover IMS calculated payments of less than \$50. Small payments which form part of the last payment run in each financial year will not be able to be adjusted but we will assess the merits of adopting a procedure whereby councils are asked whether they wish to receive a payment of less than \$50.

Six months rule

**3.63** Clause 1.4 of the Funding Conditions stated that funding recipients must ensure that payments made under the Standard Program are spent

within six months of receipt of the payment (although Condition 1.4 also noted that the Minister has the power to waive this and any other conditions).

**3.64** In terms of the timely expenditure of funds, the Notes on Administration stated that:

LGA expenditure will be monitored and LGAs holding substantial Commonwealth funds for extended periods will be asked to explain. LGAs should advise the department in writing of any extenuating circumstances.

**3.65** The Notes also explicitly recognised that there were circumstances where it may not be possible for funds paid to LGAs to be used within six months of receipt. Examples noted were delays in obtaining State Government planning permission, problems with contractors, early onset of the wet season and drought.<sup>130</sup>

**3.66** R2R Circular 2006/4 issued in March 2006 also advised LGAs that the reasons for delays in expending funds were required to be entered by LGAs in the comments box in their quarterly reports.<sup>131</sup> It also advised that, where an explanation was not provided or was unsatisfactory, further funding may be withheld until the R2R funds (held by an LGA for more than six months) were spent or a satisfactory explanation was provided.

**3.67** While LGAs were expected to self-assess their compliance with the six months rule, and advise DITRDLG when breaches occurred and the reasons, the quarterly reports submitted by LGAs included information that could also be used by DITRDLG to monitor compliance. In particular, LGAs were required to report their cumulative expenditure on R2R projects as at the end of each quarter.<sup>132</sup>

**3.68** Where satisfactory reasons for not spending R2R funds within six months were provided and a waiver was issued, DITRDLG advised the

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<sup>130</sup> Other reasons identified by DITRDLG in R2R Circular 2006/4 included: problems with equipment; and technical issues which emerge in detailed planning or after construction begins.

<sup>131</sup> In 73 per cent of those cases in the ANAO sample of LGAs where a waiver had been issued, there was no evidence in the quarterly reports or other documentation on the LGA's departmental file indicating that the reasons why R2R funds remained unspent for more than six months had been provided to DITRDLG in writing. As reasons were submitted to delegates approving the waivers, ANAO can only assume that these explanations were conveyed to DITRDLG by telephone.

<sup>132</sup> IMS identifies six months rule breaches and does not allow an expenditure report to be completed until the reason for a breach is provided. Manual checks for breaches were undertaken prior to the introduction of IMS,

LGA in writing. ANAO observed only one instance where DITRD LG refused a request from an LGA for a waiver in relation to a breach of the six months rule.<sup>133</sup>

**3.69** Letters informing LGAs that a waiver had been approved typically advised the LGA that:

You should seek to comply with funding condition 1.4 but if this is not achieved, you should again provide reasons for delays in your subsequent quarterly reports.

**3.70** These letters also stated that a copy of the instrument of exemption was attached as required by section 91(1) of the AusLink Act. However, ANAO noted that:

- copies of the instruments were retained on 'Payment Issues' files but not on the respective LGAs' departmental files<sup>134</sup>;
- section 91 of the Act required that an LGA be advised in writing, but did not specify that a copy of the instrument must also be provided;
- DITRD LG's practices were inconsistent, as DITRD LG did not provide copies of the instruments when notifying LGAs in relation to waivers of various other funding conditions approved under section 91<sup>135</sup>; and
- by providing LGAs with copies of the instruments, DITRD LG had in effect advised each LGA listed on the instrument (up to 42 LGAs on some instruments) of the names of all LGAs included in that particular approval, which is unnecessary.

**3.71** In December 2009, ANAO suggested that DITRD LG also document its procedures in relation to issuing waivers, as this topic was not included in the Internal Operating Procedures issued in May 2009. DITRD LG subsequently advised ANAO that it had started updating the procedures to include the issue of six months rule and expenditure maintenance waivers in particular, with the

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<sup>133</sup> In May 2009, Mornington Shire Council (QLD) advised DITRD LG that it could not track any more than \$68 807 of the \$220 000 in AusLink R2R funds paid to it in the period up to 30 September 2008. See comments on withheld payments for Mornington Shire Council at paragraph 2.19.

<sup>134</sup> However, approved instruments were retained on DITRD LG's 'Roads to Recovery Payment Issues' files.

<sup>135</sup> Including waivers of the: expenditure maintenance requirements; requirement to submit an R2R Annual Report; requirement for separate Annual Reports on WA bridge and Aboriginal access road projects; and the requirement for precursor and new councils involved in QLD and NT council amalgamations to provide Part 3 (expenditure maintenance statement) of their R2R Annual Reports.

aim of ensuring that there is a consistent approach over the life of the Nation Building R2R Program.

### *ANAO analysis*

**3.72** ANAO's analysis of IMS data identified a total of 435 instances of non compliance by LGAs with the six months rule, up to the time of completing the audit fieldwork. An additional 53 potential instances were also identified. There was insufficient information in DITRDLC's records to assess whether funds had been expended within six months in these latter cases, as the respective LGAs had not submitted their quarterly reports for the relevant periods.<sup>136</sup>

**3.73** As illustrated in Figure 3.10, the total amount of unspent R2R funds held by LGAs for more than six months as at the end of each quarter (March 2006 to March 2009) ranged from \$0.4 million up to \$6.9 million (average \$3.1 million, median \$3.0 million). ANAO estimated that the minimum amount of interest foregone by the Commonwealth where LGAs had held unused R2R funds for more than six months was \$0.6 million.

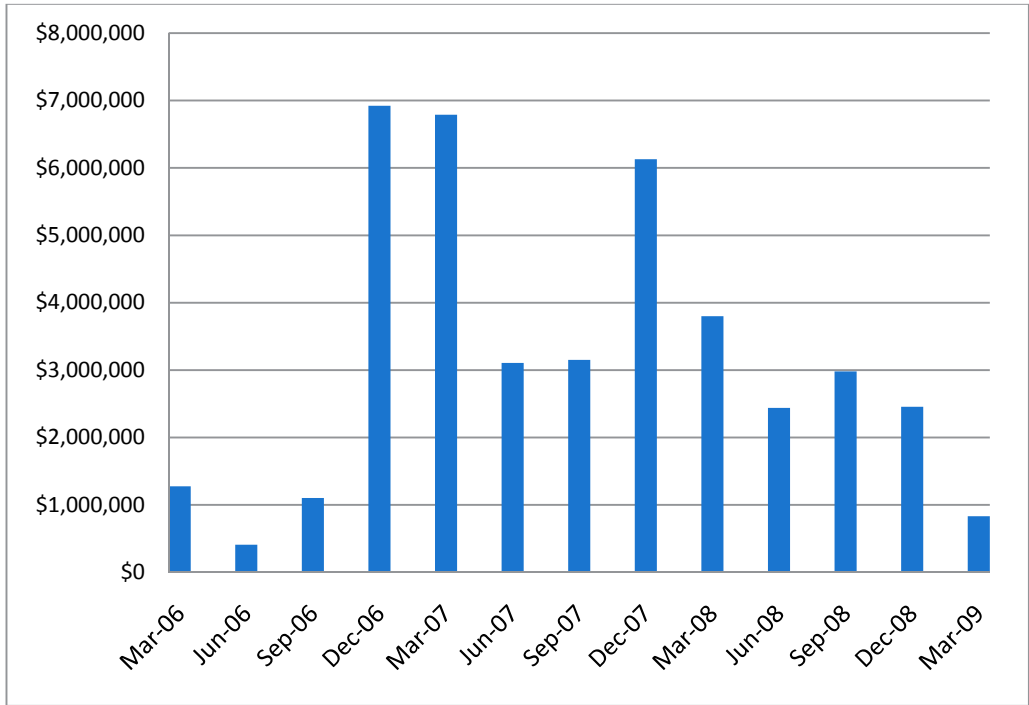
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<sup>136</sup> In effect, LGAs could avoid incurring a breach of the six months rule being recorded by simply not reporting to DITRDLC during the quarters in which they breached the requirement to spend funds within six months.



Figure 3.10

Aggregate reported R2R funds unexpended after six months



Source: ANAO analysis of DITRDLG data.

**3.74** In relation to the 435 instances of non compliance with the six months rule, 189 cases (43 per cent) required a waiver to be issued before the next quarterly R2R payment could be made to the LGA. The remaining 53 per cent of cases did not require a waiver, as no R2R payment was made to the respective LGA at the time the non compliance occurred.<sup>137</sup> However, in total, DITRDLG issued 272 waivers, of which only 175 were required (because an R2R payment was made at the time). The remaining 97 waivers were issued by DITRDLG, although they were not required (because no payment was made at the time).

<sup>137</sup> That is, although the latest quarterly report submitted by the LGA at the time indicated that it had not fully expended the cumulative R2R funds received by it more than six months ago, in relation to the latest quarterly report lodged, the LGA was either not seeking an R2R payment (for example, because funds on hand exceeded planned expenditure for the next quarter) or the LGA was not entitled to a payment (for example, because an R2R Annual Report was overdue).

**3.75** A total of 109 LGAs (96 per cent of all LGAs that did not comply with the six months rule) incurred multiple instances of non compliance (up to seven times).<sup>138</sup> Thirty seven LGAs required multiple waivers (up to five waivers). Further, DITRDLG made 14 payments to LGAs totalling \$2 372 211 which should not have been made, because the LGAs were not complying with the funding conditions at the time and had not been issued with waivers (see Table 3.7).

**Table 3.7**

**AusLink R2R payments made without required six months rule waivers**

Quarter Ended	State	LGA	Amount (\$)
Mar-06	WA	Shire of Bridgetown Greenbushes	36 758
Mar-07	WA	Shire of Beverley	232 882
Mar-07	WA	Shire of Christmas Island	140 040
Jun-07	QLD	Bowen Shire Council	45 114
Jun-07	SA	Clare and Gilbert Valleys Council	3997
Jun-07	NT	Darwin City Council	783 994
Jun-07	TAS	King Island Council	32 597
Jun-07	VIC	Moorabool Shire Council	330 040
Jun-07	SA	Northern Areas Council	2044
Jun-07	WA	Shire of Quairading	81 958
Jun-07	NSW	Willoughby City Council	71 590
Sep-07	SA	City of Tea Tree Gully	247 541
Dec-07	NSW	Berrigan Shire Council	143 656
Dec-07	WA	City of Gosnells	220 000

Source: ANAO analysis of DITRDLG data.

**3.76** In October 2009, DITRDLG advised ANAO that:

Checking for breaches of the six months rule was done manually prior to the introduction of IMS. Twelve of the cases raised by ANAO were from this period and in each of these cases the expenditure report submitted by each council was incorrectly marked as complying.

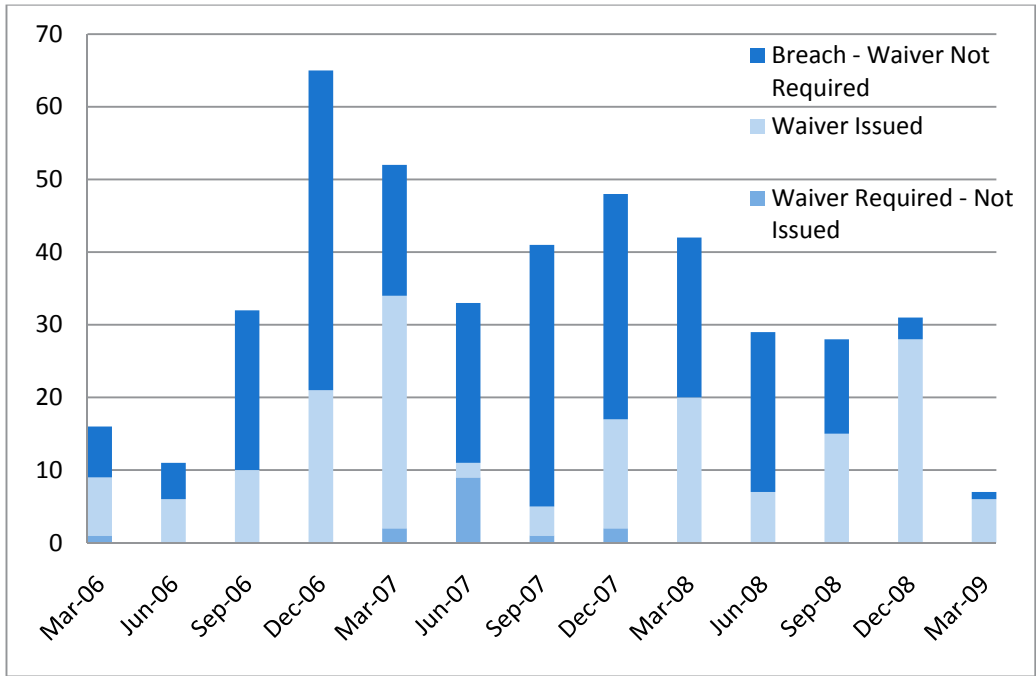
<sup>138</sup> Over the period covered by the audit: five LGAs incurred one breach; 51 LGAs had two breaches; 32 LGAs had three breaches; 13 LGAs had four breaches; eight LGAs had five breaches; four LGAs had six breaches; and one LGA had seven breaches.

Two of the cases raised by ANAO occurred in the first reporting/payment period after the introduction of IMS. In both cases an explanation for the breach was required by IMS and was provided by the council as part of their expenditure report but the councils concerned were not included in the relevant waiver instrument as they should have been. DOTARS believes that these two cases were due in part to the process of moving to the new computer system and that breaches of the six months rule are now effectively monitored and actioned under IMS.

3.77 Figure 3.11 illustrates the occurrence of non compliance with the six months rule and whether waivers were required and issued.

Figure 3.11

Number of instances of non compliance with the six months rule for the period March 2006 to March 2009



Source: ANAO analysis of DITRD LG data.

3.78 While the largest dollar value waiver issued by DITRD LG for non compliance with the six months rule was in respect of a shortfall of more than

\$1 million<sup>139</sup>, waivers were also issued for unexpended amounts that were as low as \$1.<sup>140</sup> The median shortfall for all instances of non compliance with the six months rule by LGAs was \$49 817.<sup>141</sup> In this respect, ANAO suggested to DITRDLG that there would be benefit in DITRDLG examining the feasibility of introducing a threshold amount for waivers or an alternative, more practical, mechanism for dealing with low-value expenditure shortfalls.

## Program wind-up

**3.79** Each of the 41 LGAs in ANAO's sample was paid its full R2R allocation. The total amount paid to these 41 LGAs was \$134.1 million (Standard Program) and \$33.5 million (Supplementary Program). Of these amounts:

- \$7 076 200 (Standard Program) and \$2 291 852 (Supplementary Program) had not been accounted for (as of 30 June 2009) because nine LGAs (Standard Program) and eight LGAs (Supplementary Program) had not submitted an R2R Annual Report for 2008–09 by 31 December 2009;
- 25 LGAs (Standard Program) and 29 LGAs (Supplementary Program) reported to DITRDLG that their full allocation had been spent by 30 June 2009; and
- seven LGAs (Standard Program) and four LGAs (Supplementary Program) reported that \$2 974 505 (Standard Program) and \$1 661 166 (Supplementary Program) had not been spent by 30 June 2009.<sup>142</sup>

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<sup>139</sup> Department of Planning and Infrastructure (NT) was issued with a waiver in November 2008 because it had not spent \$1 083 719 of \$13 522 792 in R2R funds received in the period up to 31 December 2007. Reasons for the waiver stated: 'Work on several projects affected by sacred site issues. These have now been resolved'.

<sup>140</sup> For example, the September 2008 quarterly report for Guyra Shire Council (NSW) reported cumulative R2R expenditure of \$1 134 011. Council had received payments totalling \$1 134 012 up to 31 March 2008 and therefore had an underspend of one dollar. A waiver was issued on 18 November 2008. Reasons for the waiver stated: 'Amount trivial, Council claims shortfall is a rounding error'. Maribyrnong City Council (VIC) and Mingenew Shire Council (WA) were each also issued with a waiver for one dollar in November 2006 and February 2007 respectively. In addition, consecutive waivers were issued to Pittwater Council (NSW) in August 2008 and November 2008. In both instances the shortfall was \$13.

<sup>141</sup> Includes LGAs that did not require a waiver.

<sup>142</sup> Note: LGAs had until 31 December 2009 to spend their Standard Program funding.

## Payout of R2R allocations

**3.80** At the end of February 2008, DITRDLG encouraged LGAs to undertake status reviews of their roadworks programs. R2R Circular 2008/1 advised LGAs that after the payment to be made in March 2008:

...there are only five payments remaining...and many councils are well behind pro rata in drawing down funds. Councils are encouraged to review their position and to plan their programs to ensure there are no problems late in the program.

**3.81** Submissions to the departmental delegate for payments made during 2008–09 also stated that:

As we are in the last year of the program, councils will be paid out where this is warranted.

**3.82** In December 2008, DITRDLG wrote to LGAs that had not received their full allocation up until this time. DITRDLG advised such LGAs that:

There are only two payments remaining under the current *Roads to Recovery* Program. These payments are due following the (December 2008 and March 2009) quarterly reporting periods, subject to the receipt of quarterly reports. Although the Government has announced that there will be another *Roads to Recovery* Program commencing on 1 July 2009, this will be a new program and there will be no capacity to carry over unclaimed funds from 2008–09 to 2009–10.

In June 2006, the Government provided some \$307.5 million to councils as a one off payment under the Supplementary Roads to Recovery Program. Councils were given until 30 June 2009 to spend these funds. I am advised that your council has also not yet fully spent the supplementary funds and I would encourage council to plan for their full expenditure by the specified deadline.<sup>143</sup>

I am aware that the recently announced funding for councils under the *Regional and Local Community Infrastructure* Program may place additional pressure on council resources and it is important that councils plan effectively so that they are able to fully access their Roads to Recovery funding.

**3.83** As a result of the DITRDLG advice, many LGAs significantly increased the funds sought. Indeed, the total amount paid to LGAs based on December 2008 and March 2009 quarterly reports was \$229.9 million, or almost

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<sup>143</sup> This paragraph was not included for LGAs that had fully spent their Supplementary Program funds.

19 per cent of total program funds. As illustrated in Figure 3.3, the December 2008 payment was higher than at any other time during the life of the AusLink R2R Program.

### ***Deadline for use of funds***

**3.84** As mentioned, DITRDLG advised LGAs that:

- funds received under the Standard Program needed to be spent by 31 December 2009; and
- funds received under the Supplementary Program needed to be spent by the end of that program on 30 June 2009.

**3.85** The different deadlines had potential to cause some confusion for LGAs. On 15 June 2009, LGAs were also advised that if it became clear that either target will not be achieved, LGAs should write to DITRDLG to explain the situation and seek an extension.<sup>144</sup>

**3.86** Supplementary Program quarterly reports for the period ended 30 June 2009 indicated that 35 LGAs had unspent Supplementary funds, ranging from \$1267 to \$1 028 111 and totalling \$4 532 427. In this regard, DITRDLG advised ANAO in October 2009 that it had agreed to (an unspecified number of) requests from LGAs (normally by email) for an extension of time in which to fully spend their Supplementary funding.

### **Interest received on invested R2R funds**

**3.87** As mentioned, clause 1.6 of the Funding Conditions initially stated that, if a funding recipient received an amount as interest in respect of an AusLink Roads to Recovery payment, the recipient must spend an amount equal to that amount on the construction or maintenance of roads.

**3.88** In the previous performance audit, ANAO raised concerns that there was a risk that the approach taken in the funding conditions to identifying and calculating the benefit to LGAs (and cost to the Commonwealth) of funds not being used in a timely manner may be administratively complex for LGAs.<sup>145</sup> It also flagged that there were also circumstances where it may be difficult for

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<sup>144</sup> R2R Circular 2009/5.

<sup>145</sup> ANAO Audit Report No. 31 2005-06, op. cit., p. 155, paragraph 4.84.

DITRDLG to identify whether LGAs have earned interest on Commonwealth funds and, if so, the amount of interest.<sup>146</sup>

**3.89** As also mentioned, in March 2006, clause 1.6 of the Funding Conditions was amended to state as follows:

If a funding recipient receives an amount as interest in respect of an AusLink *Roads to Recovery* payment in one financial year, the recipient must spend an amount equal to that amount on the construction or maintenance of roads in the next financial year and must be able to demonstrate that it has done so. This condition does not apply to councils which are to receive total funding of less than \$1 million according to the list determined by the Minister under section 87(1) of the Act.

Note: Interest earned in respect of an AusLink Roads to Recovery payment is own source funds for the purposes of Part 2 of these conditions.

**3.90** R2R Circular 2006/5 issued on 18 April 2006 advised LGAs of the changes and noted that 'All councils should be able to comply with this requirement.' The Notes (section 6.5) also stated that 'provided a council's own source expenditure on roads is more than the interest earned on *Roads to Recovery* funds, the council is complying.'<sup>147</sup>

**3.91** Although 418 LGAs had a life of program allocation exceeding \$1 million, it was inconceivable that any of these LGAs could generate sufficient amounts of interest on invested R2R funds in a single year to exceed their annual reference amount. For example, Brisbane City Council had a Standard Program allocation of \$28 626 116, the highest of all LGAs in the program. In comparison, the annual reference amount was 6.6 times higher at \$188 600 992. If Council were to invest its annual allocation at five per cent interest per annum, it would take more than 41 years to accumulate enough in interest payments to meet its annual reference amount. In addition, during each year of the AusLink R2R Program, own source expenditure by the Brisbane City Council exceeded the reference amount by more than its life of program allocation.<sup>148</sup>

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<sup>146</sup> Money is fungible, meaning that each unit is identical to, and therefore interchangeable with, another.

<sup>147</sup> The Notes stated that, in relation to the Supplementary Program, the same conditions generally apply except that the interest earned must only be spent by 30 June 2010.

<sup>148</sup> For all LGAs with a life of program allocation of more than \$1 million, the range was 3.6 years (Central Highlands Council, TAS) to 73.5 years (Ipswich City Council, QLD) assuming five per cent per annum compound interest.

**3.92** Accordingly, as currently worded<sup>149</sup>, the interest provision in the funding conditions is redundant. In accordance with the original intention to keep the processes for R2R grant payments to LGAs as simple as possible, ANAO suggested to DITRDLG that there would be benefit in consideration being given to deleting this condition. This would be particularly the case if the program requirement for payments in advance was revisited.

## **Recommendation No.2**

**3.93** ANAO *recommends* that, in light of the experience to date with the program, the Department of Infrastructure, Transport, Regional Development and Local Government review and advise Ministers on program design arrangements that will promote timely local government expenditure of Roads to Recovery funding on road work that is additional to that which would have otherwise occurred.

### **DITRDLG Response**

**3.94** Agree. The department will review administrative arrangements during the life of the Nation Building Roads to Recovery Program, provide advice to the Minister on appropriate program design arrangements and amend the program guidelines as required.

## **Council Compliance Information Package**

**3.95** In late 2005, in addressing issues arising from the previous ANAO audit, DITRDLG recognised that there was a 'need to be more proactive in ensuring that councils are left in no doubt as to their responsibilities in administering the program effectively.' According, DITRDLG proposed to engage a consultant to develop:

- an informative and concise presentation package setting out the key issues on council compliance with the AusLink Act, R2R funding conditions and Notes, for joint delivery by DITRDLG and Local Government Associations, to regional groups of councils; and

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<sup>149</sup> The same wording was retained in the Funding Conditions for the Nation Building R2R Program. However, the \$1 million threshold was increased to \$1.25 million per annum from 1 July 2009 for the duration of the Nation Building Program.



- a detailed information and reference resource for use by council staff responsible for AusLink R2R administration, to be made available in hard copy and accessible through the AusLink website.

**3.96** Tenders for providing the consultancy closed on 31 January 2006. Six firms lodged tenders. However, on 19 April 2006, DITRDLG advised these firms that it had been decided not to proceed with this tender.

**3.97** In December 2009, DITRDLG advised ANAO that:

It was decided not to proceed with this consultancy for a number of reasons:

- work was underway on the development of the AusLink Program Management System (APMS) and there were many amendments to how particular screens looked and operated. It was felt that a consultant would find it difficult to prepare a package which reflected the requirements of the computer system which was still being developed;
- the introduction of APMS itself would automate many aspects of the administration of the program and facilitate an increase in compliance;
- the user manual for APMS (to be developed by a professional firm) and the Notes on Administration would provide significant additional guidance;
- the program of financial audits to be commissioned by DITRDLG (and subsequently undertaken by contracted firms) would also improve compliance;
- site inspection visits and the face to face meetings with councils would also improve the understanding of the program's requirements; and
- presentations by departmental officers on the findings of the first ANAO audit of R2R and the ongoing responsibilities of councils were to be made at relevant conferences. Presentations were subsequently made at the ALGA Roads Congress (July 2006), SA Local Government Roads and Works Conference (August 2006) and Institute of Public Works Engineering Australia NSW Conference (October 2006).

**3.98** Notwithstanding that the R2R Program has now been in operation in one form or another for ten years, the findings of the current ANAO performance audit indicate that there is scope to further improve LGAs' understanding of, and compliance with, the R2R Program Funding Conditions. ANAO suggested that DITRDLG should develop a range of ongoing strategies to address this issue. Communication strategies targeting LGA staff newly interacting with the R2R Program should desirably form one component.

## **LGA Auditor Information Package**

**3.99** The findings of the current ANAO performance audit also indicate that LGA Auditor education is no less important than educating LGA staff about R2R Program requirements. In this regard, ANAO suggested that DITRDLG consider developing and distributing an information pack to LGA auditors that sets out the key requirements of the R2R Program and provides details of all R2R payments made to the LGA during the relevant year. This better practice approach has already been successfully employed by another Australian Government department that also administered a nationwide grants program.

**3.100** However, in February 2010, DITRDLG advised ANAO that the department already provides detailed instructions to LGAs through IMS and that every effort is made to ensure that relevant information is available to LGAs.

## 4. Program Outcomes and Accountability

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*This chapter examines the major outcomes from the \$1.5 billion AusLink Roads to Recovery Program and discusses the primary accountability mechanisms for the program. It also examines whether local government substituted Australian Government funds for its own expenditure on roads.*

### Accountability to the Parliament

**4.1** Accountability to the Parliament for the operation of the various R2R Programs was provided for in two main ways:

- similar to all Government programs, through performance indicators and performance reporting by DITRD LG in its Portfolio Budget Statements (PBS) and Annual Reports; and
- by virtue of the requirements of the R2R Act and the AusLink Act, an Annual Program Report to the Parliament.

### DITRD LG performance reporting

**4.2** The foundation for agency accountability and transparency is performance information presented initially in PBSs, with results being reported later in annual reports.<sup>150</sup>

**4.3** In each year between 2005–06 and 2007–08, the Transport and Regional Services Portfolio PBS included effectiveness, quality, and cost performance indicators for the AusLink R2R Program. The three indicators were:<sup>151</sup>

- effectiveness: local councils use funds to maintain and improve land transport infrastructure;
- quality: payments are made in line with AusLink legislation; and
- cost: \$340.6 million in 2005–06, \$307.5 million in 2006–07, and \$307.5 million in 2007–08.

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<sup>150</sup> ANAO Better Practice Guide, *Performance Information in Portfolio Budget Statements*, May 2002, p. 1.

<sup>151</sup> In 2006–07 and 2007–08, a Quantity indicator was also included; which stated that: ‘approximately 700 councils are eligible for funding’.

**4.4** In 2008–09, the Infrastructure, Transport, Regional Development and Local Government Portfolio PBS included the key performance indicator of ‘efficient and effective management’ of the AusLink R2R Program. The 2008–09 target identified for this indicator was that the program be ‘administered in accordance with relevant legislation, published guidelines and ANAO guidance’.

**4.5** Effectiveness indicators demonstrate the extent to which outputs and/or administered items make positive contributions to specified outcomes. In general, targets should be set for effectiveness indicators.<sup>152</sup> Targets provide a basis for performance assessment and, from an accountability perspective, help Parliament to assess if a program and the administering agency are delivering to expectations. Targets can also encourage agency performance. In this respect:

Targets express quantifiable performance levels or changes of level to be attained at a future date, as opposed to the minimum level of performance. They may be a range or an absolute number, but they should never be vague or unmeasurable. They should focus on factors that managers can influence and may relate to either the overall outcome or output performance or the factors that lead to success. It may be necessary to have multi year targets which address the achievement of intermediate outcomes leading to achieving overall outcomes in a specified number of years. However, targets should not become the focus of achievement in their own right at the expense of overall performance.<sup>153</sup>

**4.6** At no stage have effectiveness targets for the Roads to Recovery Program been set, or reported against, by DITRD LG. Rather, in departmental Annual Reports presented for the years 2005–06 to 2007–08 inclusive, reporting of actual performance consistently included information on how many LGAs were eligible to receive funding, total payments made, number of projects funded as well as how LGAs were using the funds provided. In the context of a program introduced with the stated purpose of renewing local roads to meet social and economic needs, it is significant that the reporting of performance has not addressed the extent to which the program has contributed to an improved standard of local roads. As outlined below, a key issue in this regard

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<sup>152</sup> ANAO *Better Practice Guide—Performance Information in Portfolio Budget Statements*, op. cit., p. 25.

<sup>153</sup> ANAO Audit Report No. 18 2001–02, *Performance Information in Portfolio Budget Statements*, Canberra, 1 November 2001, p. 51.

within the design of the program was that local government should maintain its own expenditure on local roads such that program funding would represent additional spending on local roads. Accordingly, an effectiveness target for the program could reasonably relate to any changes in local government own-source expenditure on roads.

**4.7** In addition to not setting and reporting against an effectiveness target for the program, little, if any, information was reported in any year as to whether recipients complied with the program funding conditions (that is, the quality indicator).<sup>154</sup> This was notwithstanding the continuing evidence to DITRDLG of LGA non-compliance with various aspects of the funding conditions including the timely and complete submission of Annual Reports concerning their R2R funding, the recognition of the provision of Commonwealth funding (both through the requirement for signs at each end of works and opportunities for the Commonwealth to participate in opening ceremonies) and LGAs not maintaining their own spending on roads.

**4.8** DITRDLG's 2008–09 Annual Report represented a contraction from the types of information disclosed in preceding years. It reported that a total of \$355 million was paid under the program to local councils, three state governments, the Northern Territory Government and the Indian Ocean Territories.<sup>155</sup> The only additional performance information reported in relation to the R2R Program<sup>156</sup> was that:<sup>157</sup>

The Department administered funding for a range of purposes, including road work, bridge work and the installation of traffic lights. Councils were required to lodge audited financial statements stating how they spent the program funds.

**4.9** DITRDLG's 2008–09 Annual Report was silent on whether the department had met the recently introduced performance indicator concerning the administration of the program (see paragraph 4.4).

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<sup>154</sup> No information was included in the 2005–06, 2006–07, 2007–08 or 2008–09 Annual Reports on whether or not LGAs had complied with the Program Conditions. In relation to the Quality indicator, the 2006–07 and 2007–08 Annual Reports stated that the department administered payments under the program in line with Part 8 of the AusLink Act.

<sup>155</sup> *op. cit.*, p. 28.

<sup>156</sup> The 2008–09 Annual Report noted that: 'Programs previously administered under the name 'AusLink' were renamed as Nation Building Programs in 2008–09.'

<sup>157</sup> *op. cit.*, p. 22.

## Annual Program Reports to the Parliament

### 4.10 Section 10 of the R2R Act required that:

As soon as practicable after the end of each funding year, the Minister must cause a report to be tabled in each House of the Parliament on the operations of this Act during that funding year.

4.11 Similarly, under section 94 of the AusLink Act, the Minister was required to table an Annual Report on the operation of that Act, including Part 8 which relates to the AusLink R2R Program.

4.12 As of December 2009, nine Annual Reports on the R2R Program had been tabled in the Parliament. These were reports covering the years 2000–01 to 2008–09. Each report was prepared for the Minister by the department.

4.13 Table 4.1 summarises when the Annual Reports were tabled in the House of Representatives and the Senate. It shows that there has been significant variability in the timeliness with which Annual Reports have been provided to the Parliament. By way of comparison, DITRD LG requires LGAs to submit their R2R annual reports within four months of the end of the financial year.

**Table 4.1**

### Timeliness of tabling of Initial R2R Program and AusLink R2R Program Annual Reports

Annual Report Year	House of Representatives	Senate
2000–01	13 March 2002 (8½ months)	19 March 2002 (8½ months)
2001–02	Same day: 15 October 2002 (3½ months)	
2002–03	Same day: 9 September 2003 (2 months)	
2003–04	Same day: 9 February 2005 (7 months)	
2004–05	1 June 2006 (11 months)	13 June 2006 (11½ months)
2005–06	Same day: 13 June 2007 (11½ months)	
2006–07	Same day: 24 June 2008 (12 months)	
2007–08	2 February 2010 (19 months)	3 December 2009 (17 months)
2008–09	Same day: 16 November 2009 (4½ months)	
Note: The 2008–09 AusLink Annual Report was included in the 2008–09 DITRD LG Annual Report (received by the Senate on 30 October 2009).		

Source: ANAO analysis of House of Representatives Votes and Proceedings and Senate Journals.

**4.14** Each of the Annual Reports for the initial R2R Program provided the Parliament with a range of information on the operation of the program, as follows:

- the inaugural report, for 2000–01, provided background details on the program and its operation together with summary data on how the funds had been used and financial data on payments made to LGAs;
- the 2001–02 report also included background on the program and its operation together with a number of financial tables outlining allocations and payments made to 30 June 2002 as well as identifying those LGAs that had been paid in full. The report also included a number of project case studies from the review, along with information on the joint review of the program conducted by DOTARS and ALGA;
- the approach taken in the 2002–03 report was similar to that adopted for 2001–02 report, with updated financial data included within the report;
- the key differences in the 2003–04 report compared to the two prior years were that case studies were not included and information was included on the Government’s announcement of an extension to the program; and
- the 2004–05 report adopted a similar format to the previous year, including the announcement on the future of the program and information on LGAs that had been restructured.

**4.15** In comparison, the range of information provided to the Parliament on the operation of the AusLink R2R Program was less extensive. In 2005–06, 2006–07 and 2007–08, the program was included as one of the chapters in the AusLink Annual Report, comprising two or three pages each year (including photographs).<sup>158</sup> These reports provided background details on the program and its operation together with summary financial data on payments made to LGAs. There was no reporting on other aspects of the operation of the program such as, for example, summary reporting on waivers of the Funding Conditions that had been granted under section 91(1) of the AusLink Act.

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<sup>158</sup> By way of comparison, the 2004–05 Annual Report comprised 27 pages.

## Recommendation No.3

**4.16** ANAO *recommends* that the Department of Infrastructure, Transport, Regional Development and Local Government improve accountability to the Parliament for the Roads to Recovery Program by setting and reporting in its departmental Annual Report against an effectiveness target for the program.

### DITRDLG Response

**4.17** Agree. The department will develop an effectiveness target for the program as part of the review of administrative arrangements to be undertaken in response to Recommendation 2.

## Annual statement of accountability by funding recipients

**4.18** LGAs were required by the AusLink R2R funding conditions to submit Annual Reports to DITRDLG covering their use of R2R funds. For the Standard Program, these reports comprised four parts (with a fifth part required to be submitted for 2005–06 only):

- Part 1—a financial statement outlining the amount of AusLink R2R funds brought forward from the previous year, the amount paid to the LGA in the year, the total amount available for expenditure in the year, the amount of R2R funds spent in the year and any amount carried forward to the next year. This section of the Annual Report was also required to include an auditor’s report stating the financial statement was based on, and was in agreement with, proper accounts and records and the amount reported as spent was used solely on the maintenance or construction of roads (as defined in the AusLink Act);
- Part 2—a statement of accountability by the LGA’s Chief Executive Officer (CEO) that:
  - AusLink R2R funds had been used solely for roads expenditure (as defined in the AusLink Act);
  - the LGA had complied with the R2R signage and publicity requirements; and
  - the other conditions set out in the AusLink R2R Funding Conditions and Notes on Administration had been complied with;



- Part 3—a statement of expenditure maintenance by the CEO identifying the LGA's own source expenditure on roads and the reference amount<sup>159</sup>;
- Part 4—a statement of key outcomes achieved with the AusLink R2R Program funds during the year, and
- Part 5—(for 2005–06 only), details of the five-year (or three-year) reference period chosen by the LGA.<sup>160</sup>

**4.19** The Supplementary Program Annual Reports were in essence the same as the first three parts of the Standard Program reports<sup>161</sup>, except that the financial statement in Part 1 did not include provision for reporting the amount paid to the LGA in the year and the total amount available for expenditure in the year.<sup>162</sup>

**4.20** The Notes contained proformas of the AusLink R2R Standard Program and Supplementary Program Annual Reports.

## Submission of Annual Reports

**4.21** The AusLink R2R Standard Program and Supplementary Program Annual Reports were to be provided to DITRD LG no later than 31 October each year.<sup>163</sup> In this context, for the 41 LGAs in ANAO's sample, Table 4.2 shows that, in each year, a large proportion of Annual Reports were submitted late by LGAs. On 6 December 2006, DITRD LG emailed 178 LGAs that had overdue 2005–06 Annual Reports. However, email reminders were not sent in subsequent years.

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<sup>159</sup> Including for the previous year (or previous two years) if own source expenditure in the report year was less than the reference amount. The average of the LGA's own source expenditure during the report year and the previous year (or two years) was also required to be reported.

<sup>160</sup> This included specifying the amounts spent on roads using the LGA's own sources in 2000–01, 2001–02, 2002–03, 2003–04 and 2004–05.

<sup>161</sup> There were also some minor differences in the wording of the Auditor's report.

<sup>162</sup> These items were not applicable because all LGAs received a once-only payment of Supplementary Program funds on 27 June 2006. For administrative purposes, DITRD LG adopted the (reasonable) assumption that LGAs would not have time to spend any Supplementary Program funds before 30 June 2006. Accordingly, the first Supplementary Program Annual Report required to be submitted by LGAs was for the year ended 30 June 2007. Reports were then required annually until the expenditure of Supplementary Program funds was fully acquitted by the LGA.

<sup>163</sup> Under the initial R2R Program, the Annual Report due date was 30 September.

**Table 4.2****Date R2R Annual Report submitted to DITRDLG (for ANAO's sample)**

	Standard Program				Supplementary Program		
	2005–06 (%)	2006–07 (%)	2007–08 (%)	2008–09 (%)	2006–07 (%)	2007–08 (%)	2008–09 (%)
Submitted by 31 October	40	35	32	37	34	41	41
Submitted late <sup>1</sup>	60	65	68	63	66	59	59
Note 1: The 'submitted late' figure for 2008–09 includes nine LGAs for the Standard Program (26 per cent) and eight LGAs for the Supplementary Program (30 per cent) that had outstanding Annual Reports as at 31 December 2009.							

Source: ANAO analysis of DITRDLG records.

**4.22 In February 2010, DITRDLG advised ANAO that:**

The 31 October deadline stated in the funding conditions reflects the program's operational requirements. This date is the end of the October reporting period and therefore provides each LGA with as much time as possible under the program to submit an annual report and still qualify for a payment in November.

However, in some cases submission of annual reports by LGAs occurs because LGAs may not submit their R2R annual reports until they are ready to submit their main accounts to their auditors. The timing of this is usually associated with the requirements of state/NT legislation which specifies when council accounts must be ready e.g. in NSW, the accounts must be ready for consideration by council by 30 November each year.

The Department does not expect LGAs to change their practice of submitting their annual reports to their auditors in conjunction with their main accounts. LGAs that submit their reports late do not receive further payments until a satisfactory annual report is received.

**Accuracy of annual reports submitted by LGAs**

**4.23** DITRDLG's payment procedures required departmental officers to satisfy themselves as to whether a satisfactory Annual Report had been received prior to making further payments to an LGA. In this context, of the 529 quarterly reports processed by DITRDLG in relation to the ANAO's sample of 41 LGAs, in 30 instances (six per cent) payment was withheld from an LGA because an R2R Annual Report was not submitted. Up to the end of

the Standard Program on 30 June 2009, on only two occasions did DITRDLG make a payment when the required annual report had not been submitted.<sup>164</sup>

**4.24** The previous performance audit report noted that a satisfactory R2R Program Annual Report was considered by DITRDLG to be one where:

- the funds brought forward matched the carried forward figure in the previous Annual Report, or there was an adequate explanation for the difference;
- the amount reported as received in the year matched DITRDLG's payment records;
- the total available for expenditure was the sum of the funds brought forward and the amount received; and
- the amount carried forward to the next year was calculated by subtracting expenditure reported from the sum of funds brought forward and payments received.

**4.25** Accordingly, DITRDLG's procedures had focused on Part 1 of the Annual Report (the Financial Statement). The procedures at that time did not, however, address checking for completeness and accuracy of Part 2 (the Statement of Accountability) or Part 3 (the Statement of Key Outcomes) within the submitted Annual Reports.

**4.26** In May 2009, DITRDLG documented a number of its internal operating procedures for the R2R Program. This included procedures for checking Annual Reports.<sup>165</sup> In summary, staff were required to check each Part as follows:

- Part 1—figures in columns 1, 2, 3 and 5 agree with APMS records, and the CEO and auditor have signed;
- Part 2—CEO has signed (plus follow up any annotations made by LGA);

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<sup>164</sup> Specifically, payments of \$102 520 and \$95 788 to Torres Strait Island Regional Council (QLD) were made on 2 March 2009 and 18 May 2009 respectively, under a waiver issued on 10 February 2009. Outstanding annual reports for this new LGA and one of its predecessors were completed but awaiting audit.

<sup>165</sup> The procedures were to: 'have effect from the date of signature' (11 May 2009). However, DITRDLG advised ANAO that the procedures had been in place for a number of years.

- Part 3—correct reference amount and correct calculations for prior year averages have been provided;
- Part 4—totals add to 100 per cent and statement of outcomes has been provided; and
- Part 5—(for 2005–06 only), all required information is included and reference amount is properly calculated.

### *ANAO analysis*

**4.27** Analysis of Annual Reports submitted by ANAO’s sample of LGAs found that about 20 per cent of the reports for the Standard and Supplementary Programs contained errors that went undetected by DITRDLG. These included:

- important parts of the form (for example, the Statement of Accountability and the Statement of Outcomes) not being submitted or not being completed;
- the required CEO certification not being provided (this included incorrect years being specified for the expenditure maintenance certificate and arithmetic errors in calculating averages);
- the required audit certificate not being provided, or the wording of the submitted audit certification departing from that specified in the proforma; and
- reports being prepared on an accrual basis rather than cash accounting.<sup>166</sup>

**4.28** The percentage of Annual Reports that contained an error (excluding any date errors) is detailed in Table 4.3.<sup>167</sup>

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<sup>166</sup> As disclosed in the Audit Certificates submitted. ANAO also found instances where figures in the Annual Reports had been amended using correction fluid. It was not possible to determine whether these had been amended before or after the audit certification was made.

<sup>167</sup> It was also evident that the majority of LGAs completed Parts 3 (2) and 3 (3) unnecessarily—these parts were only required if expenditure reported at Part 3 (1) was less than the Reference Amount. Many LGAs also completed Part 5 unnecessarily during one or more of the last three years of the AusLink R2R Program. These frequent occurrences suggest that DITRDLG could make the requirements clearer to minimise unnecessary effort by LGAs.

**Table 4.3****Percentage of submitted Annual Reports containing errors (for ANAO's sample)**

	Standard Program				Supplementary Program		
	2005–06 (%)	2006–07 (%)	2007–08 (%)	2008–09 (%)	2006–07 (%)	2007–08 (%)	2008–09 (%)
Percentage of individual Annual Reports with errors	22	22	17	9*	34	15	7 <sup>A</sup>
Note A: The 2008–09 percentage results are not comparable to other years because a number of Annual Reports had not been submitted (as at 31 December 2009).							

Source: ANAO analysis of LGA AusLink R2R Program Annual Reports submitted to DITRD LG.

**4.29** Overall, the effectiveness of departmental checking of Annual Reports also appears to have improved. In the previous audit, ANAO found that 43 per cent of the reports submitted by sample LGAs during the initial Program contained errors.<sup>168</sup> Nevertheless, there remains room for further improvement. Accordingly, ANAO suggested that DITRD LG maintain a strong focus on continuous improvement of the quality of LGAs' annual reports given the important accountability role played by these documents. In this context, there would be benefit in the extent to which LGAs submit timely and complete annual reports being reflected in DITRD LG's performance reporting on the program.

## Project outcomes

**4.30** In addition to receiving funds direct from the Australian Government, the R2R Program enabled LGAs to nominate the projects to be funded from their allocation.<sup>169</sup> The ability of LGAs to nominate their own projects was subject to the requirement that the projects involve the construction, upgrade or maintenance of roads, as defined in the AusLink Act. Under the Act, the term 'road' was defined broadly. It included traffic lights and signs, street lights, vehicular ferries, bridges and tunnels and bike paths.<sup>170</sup> DITRD LG

<sup>168</sup> ANAO Audit Report No. 31 2005-06, op. cit., p. 71.

<sup>169</sup> Projects were nominated by LGAs in works schedules provided to DITRD LG.

<sup>170</sup> DOTARS, *Annual Report 2003–04*, p. 81. The definition of roads under the R2R Act remained unchanged in the AusLink Act.

records indicated that, of the 16 744 road projects funded over the life of the AusLink R2R Program:

- almost 51 per cent involved reconstruction, rehabilitation and widening of local roads;
- more than 17 per cent involved sealing along sections of gravel roads;
- close to 14 per cent involved sheeting and re-sheeting gravel roads with a new surface; and
- nearly eight per cent involved bridge or drainage works, with about 690 bridges and culverts replaced or repaired.

### **Reporting on outcomes by LGAs**

**4.31** As mentioned, the LGA R2R Annual Reports were required to include a Statement of Outcomes. This statement was to outline the key outcomes achieved by the LGA from its R2R expenditure in the relevant year. There was no guidance provided in the Conditions or Notes to assist LGAs to correctly attribute percentages across the 13 possible outcomes<sup>171</sup> included in Part 3 of the Annual Report proforma.

**4.32** According to the annual reports submitted to DITRD LG by LGAs up to 31 December 2009 (see Table 4.4), most of the funds provided under the Standard and Supplementary Programs respectively were spent on:

- achieving better asset management (28 per cent and 24 per cent);
- improving road safety (25 per cent and 23 percent); and
- improving access for heavy vehicles (11 per cent and 8 per cent).

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<sup>171</sup> As represented in Table 4.4.

**Table 4.4****Reported outcomes for the AusLink R2R Program**

Outcome	Estimated % of Roads to Recovery expenditure (all projects)	
	Standard Program	Supplementary Program
1. Road Safety	25	23
2. Regional economic development	6	4
3. Achievement of asset maintenance strategy	28	24
4. Improved access for heavy vehicles	9	8
5. Promotion of tourism	2	2
6. Improvements of school bus routes	5	4
7. Access to remote communities	3	3
8. Access to intermodal facilities	1	1
9. Traffic management	5	5
10. Improved recreational opportunities	1	1
11. Amenity of nearby residents	6	6
12. Equity of access (remote areas)	2	2
13. Other (or not specified)	5	16
<b>TOTAL</b>	<b>100</b>	<b>100</b>
Note: Figures shown have been rounded and do not add to 100 per cent.		

Source: ANAO analysis of DITRD LG Infrastructure Management System.

**Work standards and quality**

**4.33** In relation to specifying the technical standard of work to be undertaken with Australian Government funds provided under the AusLink R2R Program, the Notes stated that:

Projects undertaken using AusLink *Roads to Recovery* payments should comply as appropriate with standards and guidelines published from time to time by Austroads,<sup>172</sup> Standards Australia, the government of the State or Territory in which the project is undertaken or the Australian Road Research Board<sup>173</sup> which are applicable to the project.

#### ***ANAO site inspection observations***

**4.34** ANAO inspected the work undertaken by 41 LGAs on 563 R2R projects. The site visits involved a visual examination of the project and, if applicable, associated R2R signage. Measurements were taken, if relevant to the project, of the length and width of the applicable work. Photographs were also taken of the works.

**4.35** The ANAO site inspections did not extend to testing the structure or composition of the road. This was primarily because the invasive nature of such testing means it is best undertaken when the works are being done rather than after the works are completed. Such testing could have examined whether: the works in any technical specifications had been undertaken as planned; the road sub-base material was as expected for the proposed works solution; and the thickness of surface treatment applied was as reported and charged to the project.

**4.36** ANAO's site inspections indicated that the quality of the work undertaken with AusLink R2R funds varied considerably. For many projects, the work appeared to have been undertaken to a high standard. However, there were also instances where, from observation alone, it was apparent that the treatments applied were not adequate for the intended use of the road, or for the traffic conditions. Sometimes the deficiencies were such that work had to be re-done. In other instances, the relevant LGA advised ANAO that it would investigate the issue and undertake any necessary remediation work.

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<sup>172</sup> Austroads is the association of Australian and New Zealand road transport and traffic authorities. Members are the six Australian State and two Territory road transport and traffic authorities, DITRD LG, ALGA and Transit New Zealand.

<sup>173</sup> The Australian Road Research Board Group (ARRB Group) is a public company whose members are the Australian, State and local government authorities of Australia and New Zealand. ARRB Research, a not-for-profit entity within the ARRB Group, works in partnership with Austroads in the fields of pavements and materials, bituminous surfacings, asset management and road safety engineering.



## Recognition of Commonwealth funding

**4.37** In terms of recognising the Commonwealth funding of road works undertaken by local government, the AusLink R2R funding conditions stated that ‘the funding recipient must acknowledge and give appropriate recognition to the contribution of the Australian Government.’

**4.38** In this respect, the Notes stated that the Australian Government wanted to work closely with LGAs to inform the public about the projects and improvements being funded by the program. This was achieved in two ways. Firstly, LGA work schedules were publicly available through the DITRDLG web site. Secondly, the funding conditions included the following:

- LGAs were to consult with DITRDLG prior to releasing formal statements, media releases, displays or publications (including brochures) and advertising about any work funded by the program. This material was expected to acknowledge the Commonwealth’s contribution;
- R2R signs were to be placed at each end of the works<sup>174</sup> when the work began, and be maintained for one year after the project was completed. The signs were to be placed so that they were in plain view of passing motorists. An appendix to the Conditions detailed the specifications for the signs, including dimensions, contents and typefaces:
  - smaller signs could be installed where the usual speed limit on the road was 80 kilometres per hour or less; and
  - where an LGA carried out a number of projects where the total cost was, or was expected to be, less than \$10 000<sup>175</sup>, signs could be erected on major roads in the area and at entrances to communities rather than at each works location<sup>176</sup>; and
- LGAs were to advise DITRDLG of opening or completion ceremonies well in advance and organise joint ceremonies when requested

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<sup>174</sup> Except where the funded project related to a cul-de-sac or a one-way road.

<sup>175</sup> ANAO analysis indicated that there were 3 934 AusLink R2R projects where the total cost to R2R was \$10 000 or less. This represents about 24 per cent of all AusLink R2R projects.

<sup>176</sup> LGAs were advised by R2R Circular 2009/7 (issued on 3 August 2009) of revised signage specifications. References to ‘AusLink’ were replaced by ‘Nation Building Program’. New signs produced under the former specifications could still be used but could not be recycled to other projects. Once supplies had run out, LGAs were to commence using the new signs.

(Condition 3.7). Local Federal Members and/or Senators were to be invited to these ceremonies, plus others requested by the Minister. When a project was not to be officially opened, the possibility of a joint media statement was to be discussed with DITRDLG.

**4.39** DITRDLG did not maintain any records regarding non compliance by LGAs with Funding Condition 3.7. However, ANAO noted indications that non compliance frequently occurred. For example, nine R2R Circulars issued during the AusLink R2R Program included a reminder that LGAs should comply with this Condition, as follows:<sup>177</sup>

There have been cases recently where councils have held formal openings of *Roads to Recovery* projects without advising the *Roads to Recovery* team. It is a requirement, under clauses 3.7 and 3.8 of the funding conditions, that councils tell us about planned openings at least two weeks in advance. The Australian Government may wish to provide a representative at these events. It is a breach of the funding conditions not to advise us of planned openings.

## **Compliance with signage requirements**

**4.40** Compliance monitoring visits of R2R projects had been undertaken by the department since early 2004.<sup>178</sup> Visits conducted after mid-2005 under the AusLink R2R Program aimed to assess whether:

- the work on site matched the work descriptions shown in the work schedules;
- the status of work on site matched the reported start and finish dates shown on the work schedule; and
- the required signage had been installed.

**4.41** Absence of signage has been a recurring finding of these visits. In July 2004, DITRDLG reported that some LGAs had no signs installed and barely half of all LGAs visited had complied with the signage requirements.<sup>179</sup> This situation had not improved by 2005–06, when DITRDLG found that only

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<sup>177</sup> Wording varied slightly in some Circulars. The R2R Circulars were issued on: 8 February 2006, 2 July 2007, 18 September 2007, 7 December 2007, 19 March 2008, 19 June 2008, 23 September 2008, 15 December 2008, and 24 March 2009.

<sup>178</sup> *Roads to Recovery Program Annual Report 2003–04*, p. 8.

<sup>179</sup> *Roads to Recovery Circular 2004/10* issued 20 July 2004.

37 per cent of the LGAs visited were fully complying with the signage requirements.<sup>180</sup>

**4.42** DITRDLG records indicated that departmental staff undertook visits to 64 LGAs during the life of the AusLink R2R Program.<sup>181</sup> On average, 16 visits per year were undertaken and 8.5 projects per LGA were inspected. However, there was no documented visit program indicating the number of LGAs DITRDLG intended to inspect each year, how these LGAs would be selected and the timing of the visits.<sup>182</sup>

**4.43** Accordingly, while some States and Territories did not receive any coverage and the proportion of LGAs visited was low (two per cent per year on average), ANAO was unable to assess whether there was any shortfall between the number of planned and actual visits undertaken. Although each LGA was advised of their detailed visit findings upon completion of their visit, in contrast to the initial Program, DITRDLG did not conduct any statistical analyses and did not collate, summarise or disseminate visit results.

**4.44** Notwithstanding that individual LGAs were generally notified well in advance of the visits conducted by DITRDLG,<sup>183</sup> ANAO analysis of DITRDLG's correspondence to LGAs at the conclusion of these audits revealed that signage was reported as non compliant in 55 of the 548 projects inspected (ten per cent).<sup>184</sup> Although all required signage was present for the relatively small number of projects inspected in 2007–08, signage was found to be lacking during the inspections conducted in all other years of the program, as follows:

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<sup>180</sup> Joint Committee of Public Accounts and Audit (JCPAA) Report 412, paragraph 11.46, citing DOTARS Submission No.9, p. 4.

<sup>181</sup> Compliance monitoring audits were conducted at 23 LGAs in 2005–06 (NSW eleven, SA seven, VIC five), 26 LGAs in 2006–07 (NSW nineteen, QLD one, VIC six), six LGAs in 2007–08 (NSW three, VIC three) and nine LGAs in 2008–09 (all NSW). Thus two thirds of all audits were conducted in NSW.

<sup>182</sup> However, in June 2006, a departmental witness appearing before the JCPAA described it as: 'a program of site inspections and visits to local councils by officers of the department. It does not cover every council at all but it is a risk-based and randomly based—a share of each of those—visitation program.' Source: JCPAA Report No.412, p. 226, paragraph 11.31.

<sup>183</sup> There was no standard notification period. The notification provided ranged from a few days up to six weeks before the audits commenced. The average notification was 19 days.

<sup>184</sup> These records also indicated that seven per cent of projects inspected did not match the work description and ten per cent of projects inspected did not match the status of works shown in the work schedule.

2005–06 eight per cent, 2006–07 fourteen per cent, and 2008–09 sixteen per cent respectively.<sup>185</sup>

### *ANAO site inspection findings*

**4.45** ANAO site visits to a selection of projects undertaken by the sample of 41 LGAs included an assessment of compliance with the R2R signage requirements. For 57 per cent of inspected projects, R2R signs were not required to be in place at the time of ANAO's visit because the project had been completed more than one year prior to the visit. For the remaining projects, ANAO found that:

- R2R signs were in place for 78 per cent of projects that required them;<sup>186</sup> and
- the required R2R signs were not in place for 22 per cent of projects.<sup>187</sup>

**4.46** Non-compliance with signage requirements was slightly higher in WA (25 per cent) than NSW and VIC (both 21 per cent). Overall, these results suggest that compliance by LGAs had deteriorated towards the end of the AusLink R2R Program, after DITRD LG ceased conducting compliance monitoring visits.<sup>188</sup>

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<sup>185</sup> These results may understate the actual level of non-compliance, as DITRD LG's audit reports to LGAs, when rating a project as compliant, did not make the distinction between whether a sign was required or not at the time of the inspection.

<sup>186</sup> In some instances, it was apparent from physical inspection of the works that the R2R signs had been installed shortly prior to ANAO's visit rather than when work began (as required). One LGA installed signs during the ANAO inspection (notwithstanding that, for some of the projects signs were no longer required because the project had been completed more than one year before ANAO visited the site).

<sup>187</sup> ANAO had also notified sample LGAs in advance (up to three and a half months in some cases) that site inspections would be conducted as part of this performance audit. However, ANAO did not specify which particular projects would be inspected.

<sup>188</sup> DITRD LG's last monitoring visits under the Auslink R2R Program were conducted in NSW during November 2008. As mentioned, these found that 16 per cent of the projects inspected did not comply with signage requirements. DITRD LG advised ANAO in February 2010 that: 'Compliance monitoring visits were not undertaken after November 2008 as ANAO audit fieldwork was about to commence and the department did not wish to over burden councils. It is proposed to recommence compliance monitoring visits once the ANAO audit has been completed.' However, DITRD LG's decision to cease its own visit program until the completion of the ANAO audit was not discussed with ANAO and was not drawn to ANAO's attention until February 2010. DITRD LG could, for example, have continued to conduct monitoring visits in relation to any of the approximately 660 LGAs not included in the ANAO site visits.

## Acknowledgement of Supplementary Program Funding Conditions

**4.47** On 10 May 2006, the then Minister for Local Government, Territories and Roads wrote to LGAs outlining the conditions for the one-off grant under the Supplementary Program. Enclosed was a copy of the Supplementary Program funding conditions, together with an acknowledgement letter to be signed by the LGA if it accepted the Conditions. The then Minister requested that the acknowledgement be returned to the department within ten working days.

**4.48** As mentioned, DITRDLG made all payments to LGAs under the Supplementary Program on 27 June 2006, some five weeks after the acknowledgement letters were due to be returned. Notwithstanding, ANAO noted that 52 LGAs had not returned their acknowledgement by the time the payments to them (totalling more than \$10 million) were made. There was no evidence that DITRDLG had effective systems in place to follow up the outstanding acknowledgements in a timely manner.

**4.49** ANAO's review of DITRDLG files revealed that 46 LGAs sent an acknowledgement to the department over the ensuing 16 months. However, no acknowledgement letters were located for six funding recipients.<sup>189</sup>

## Aggregate local government spending on roads

**4.50** Cost shifting involving local government has been a significant issue for a number of years. In general, the concern has involved shifting of costs from the Australian and State/Territory Governments to local government.<sup>190</sup> However, in relation to the R2R Program, current and former governments have been concerned to address cost shifting in the other direction; that is, LGAs substituting Australian Government funds for their own expenditure on roads.

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<sup>189</sup> Binjari Community Government Council, Borroloola Community Government Council, Urapuntja Council Aboriginal Corporation, Bamaga Island Council, Hammond Island Council, and SA Department of Transport and Urban Planning.

<sup>190</sup> Reflecting this, on 30 May 2002, the then Minister for Regional Services, Territories and Local Government wrote to the House of Representatives Economics, Finance and Public Administration Committee asking it to inquire into the issue of local government and cost shifting. The main objective of the inquiry was to: 'tackle the serious problem of cost shifting onto local government and in doing so ensure that this sphere of government is appropriately financed to more effectively and efficiently serve the community'. The Committee reported in October 2003.

**4.51** In this context, the R2R Program was designed to address the problem that a significant amount of local government road infrastructure was reaching the end of its economic life and its replacement was beyond the capability of local government. It was for this reason that the funding provided, initially under the R2R Act and subsequently under the AusLink Act, was to be additional to existing road funding.<sup>191</sup> Accordingly, provisions were included in the respective Acts, funding conditions and administrative guidelines requiring LGAs to maintain their own source expenditure, rather than substituting Commonwealth funding for their own, in constructing, upgrading and maintaining roads.<sup>192</sup>

**4.52** In analysing the then available aggregate data during the previous performance audit, ANAO found indications that expenditure on roads by local government net of transfer of funds from higher levels of government (such as through the R2R Program) for each year between 1998–99 and 2002–03 (the last year included in the published data) may have actually fallen.

**4.53** The previous performance audit also found that, in the course of its administration of the initial Program, the department did not attempt to assess whether or not, in aggregate, local government spending on roads had been maintained since the introduction of the program. ANAO recommended that such periodic assessments be undertaken.<sup>193</sup> DOTARS agreed with the recommendation and advised that:

The department will assess aggregate spending to the extent of the available reliable information to augment the current analysis of individual councils that informs compliance with the funding conditions.<sup>194</sup>

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<sup>191</sup> See the R2R Act, Second Reading Speech, 5 December 2000 and clause 7 of the Explanatory Memorandum for the Bill.

<sup>192</sup> The requirement for LGAs to maintain their own source expenditure on roads is not only important for the AusLink Roads to Recovery Program. Specifically, under the Strategic Regional Program, announced by the then Government in 2004, LGAs that have Strategic Regional Program funded projects are required under clause 40 of the Funding Agreement to maintain their level of expenditure on roads over the financial years that they receive Strategic Regional Program funding. The definitions of *reference amount*, *own source of funds* and *reference period* are the same for Strategic Regional projects as they are for projects funded under the AusLink R2R Program.

<sup>193</sup> ANAO Audit Report No. 31 2005–06, op. cit., Recommendation No.2, p. 86.

<sup>194</sup> *ibid.*

### *Departmental analysis of aggregate spending*

**4.54** ANAO found no evidence that DITRDLG had analysed any of the (non-R2R Program generated) aggregate data on local government spending on roads that had been published since the last audit. DITRDLG's analyses of aggregated data provided by LGAs through the annual report requirement are discussed later in this chapter.

### *ANAO analysis*

**4.55** ANAO used data published by the Bureau of Infrastructure Transport and Regional Economics (BITRE) within DITRDLG covering the period 2000-01 to 2006-07.<sup>195</sup> This analysis indicated that national net expenditure on roads by local government was higher in each of the first four years of the R2R Program (2000-01 to 2003-04) than in any of the next three years (2004-05 to 2006-07).

**4.56** Further analysis by ANAO of unpublished BITRE data indicated that, collectively, LGAs in some States had been more successful than those in other States in maintaining their aggregate own source roads expenditure. Collectively, LGAs in no State had met the requirement in every year over the period 2000-01 to 2006-07. Although LGAs in VIC had, overall, maintained their aggregate spending in six of the seven years, SA (five years), and QLD and WA (four years), LGAs in NSW and TAS had not, collectively, maintained their expenditure in any year over this period (see Table 4.5).

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<sup>195</sup> Specifically, data from Bureau of Infrastructure Transport and Regional Economics, *IS29: Public Road-Related Expenditure and Revenue in Australia (2008 update)*, Table 1.

**Table 4.5****Aggregate expenditure maintained at pre-R2R levels for the period 2000-01 to 2006-07**

	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07
NSW	x	x	x	x	x	x	x
VIC	x	✓	✓	✓	✓	✓	✓
QLD	✓	✓	✓	✓	x	x	x
SA	✓	✓	✓	✓	x	x	✓
WA	✓	✓	✓	x	✓	x	x
TAS	x	x	x	x	x	x	x
Note: Excludes ACT and NT.							

Source: ANAO analysis of BITRE unpublished data.

**4.57** Three States had not made up for the cumulative shortfalls in their own source expenditure over the entire seven year period. The total shortfall as at 30 June 2007 was approximately \$1330 million (NSW \$823 million, WA \$288 million and TAS \$220 million). The data also indicated that, due to declining expenditure during the first four years, LGAs in both NSW and TAS had a lower aggregate expenditure maintenance requirement under the Standard Program than under the initial Program. In other words, the administrative arrangements for expenditure maintenance reward declining LGA own source expenditure levels through a reduced expenditure maintenance target.

**4.58** In contrast to the results for WA shown in Table 4.5, ANAO analysis of aggregate data published by the Western Australian Local Government Association (WALGA) indicated that LGAs in WA had collectively maintained their own source roads expenditure in every year from 2000-01 to 2007-08.<sup>196</sup> ANAO analysis of WALGA data in relation to own source expenditure by individual LGAs is discussed later in this chapter.

<sup>196</sup> WALGA *Report on Local Government Road Assets and Expenditure 2007-08*, Attachment 4, Sources of Road Funds—1998-99 to 2007-08, p. 94.



## Changes in the expenditure maintenance requirements

### *Initial R2R Program*

**4.59** The initial Program funding conditions stated that each LGA must maintain the level of roads expenditure which it funded otherwise than under the R2R Act, and provide a statement to DOTARS that it had done so. The format of this certification was included in the proforma Annual Report included in the R2R Administrative Guidelines. This proforma required that the CEO of each LGA certify that expenditure on roads from the LGA's own sources in the relevant year had been maintained at or above the average of the amounts expended on roads from those sources over the years 1998–99 to 2000–01.

**4.60** As noted in the previous audit, in order for DOTARS to rely on the LGA certifications, it was important that LGAs had analysed whether they had maintained their own source expenditure *prior* to certifying. However, in the course of the previous ANAO audit, it became apparent that a number of LGAs had not undertaken their own analyses of their roads expenditure in order to give proper consideration as to whether they had maintained their own expenditure prior to certifying that they had. This raised the possibility that a number of the certifications provided to DOTARS by LGAs had been made in error, as the financial analysis necessary to substantiate the certifications had not been undertaken.

**4.61** The previous audit also found that inconsistent approaches were taken by those LGAs that had undertaken their own analysis. This was a consequence of the lack of guidance provided to them, particularly in relation to what was meant by 'own source expenditure'. This term was not defined in the R2R Act, Funding Conditions, Administrative Guidelines or in any other guidance from the department to LGAs.<sup>197</sup>

### *AusLink Roads to Recovery*

**4.62** A number of changes were made to the expenditure maintenance requirements for the AusLink R2R Program.

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<sup>197</sup> The R2R Act and R2R Conditions (at Part 4) required the maintenance of expenditure: 'otherwise than under the R2R Act'. This suggested that roads expenditure from all sources other than the R2R Program was to be maintained. However, the R2R Conditions (at Part 10) and the R2R Guidelines used the term 'own sources', which implied a narrower scope of expenditure than the R2R Act.

**4.63** A key change was that the LGA certification was expanded to require LGAs to specify the amount spent using its own sources in each year (from 2000–01 onwards) together with the reference average amount.<sup>198</sup>

**4.64** The definition of own source expenditure was also addressed. Specifically, the AusLink R2R Notes stated that own source funds means the funds available to the LGA other than those provided by the Commonwealth, a State or Territory government. This provided some clarification. However, it meant that expenditure funded by developer contributions, for example, was included.<sup>199</sup>

**4.65** The third significant change involved providing greater flexibility in the expenditure maintenance requirements so as to take account of the fluctuating nature of LGA expenditure. In effect, the changes made the expenditure maintenance requirement less stringent by:

- enabling LGAs to reduce the standard five-year reference period 2000–01 to 2004–05 to a three-year reference period by excluding a year with abnormally high expenditure together with the year in which expenditure was the lowest<sup>200</sup>; and
- providing that an LGA that does not satisfy the requirement in any particular year will be taken to have met the expenditure maintenance requirement where:
  - the average expenditure in that year and the previous year, exceeded the reference average; or
  - the average expenditure in that year and the two previous years exceeded the reference average.

**4.66** Overall, these changes placed DITRDLG in a significantly improved position to monitor compliance by LGAs with their expenditure maintenance obligations. However, ANAO considers that, in this regard, DITRDLG would have been placed in an ever better position had it also required LGAs to report

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<sup>198</sup> Based on expenditure in the years 2000–01 to 2004–05.

<sup>199</sup> In this respect, some LGAs had advised ANAO during the previous audit that they excluded works funded by developer contributions on the basis that the level of such contributions, and therefore their ability to maintain expenditure made with these funds, was outside their control. However, DITRDLG considered that private developer contributions could be classified as LGA own source revenue.

<sup>200</sup> ANAO found that about 120 LGAs had elected to adopt a three year reference period. In aggregate, this reduced their reference amounts by about \$30.8 million annually.

their own source expenditure figures for the years 1998–99 and 1999–2000. This would have enabled DITRDLG to determine each LGA's reference amount under the initial Program and hence enable DITRDLG to monitor and quantify any cost shifting from LGAs to the Commonwealth since inception of the program.

**4.67** In February 2010, DITRDLG advised ANAO that when introducing LGA reporting of own source expenditure for the Standard Program, the department:

...took a forward looking approach and did not seek to undertake any retrospective analysis of LGAs under the initial R2R Program.

**4.68** Further changes made to the expenditure maintenance requirements for the Nation Building R2R Program are discussed later in this chapter.

### **Monitoring of R2R expenditure maintenance compliance**

**4.69** In July 2007, May 2008 and April 2009, DITRDLG briefed the General Manager responsible for the R2R Program on global compliance by LGAs with expenditure maintenance requirements for 2005–06, 2006–07 and 2007–08 respectively. Each brief made reference to the ANAO recommendation that the department monitor aggregate local government own source expenditure.

**4.70** Attached to each brief was a table setting out the own source expenditure total by state and year, together with the five-year and three-year reference amounts.<sup>201</sup> These figures were compiled from information provided by LGAs in Parts 3 and 5 of the Annual Reports received by DITRDLG up to the time each brief was prepared.<sup>202</sup>

**4.71** The briefs concluded that national compliance with the expenditure maintenance requirements had been achieved in each year and that each jurisdiction had exceeded the five-year and three-year reference amounts. However, ANAO noted that figures in the respective attachments indicated that QLD had in fact not met the five-year or the three-year reference amounts in 2006–07 and 2007–08. In addition, the figures indicated that, for the national aggregate, expenditure declined in 2006–07 and further declined in 2007–08

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<sup>201</sup> State figures were also totalled to provide national figures.

<sup>202</sup> In effect, figures for earlier years were progressively updated in subsequent years when outstanding annual reports were eventually received.

(although remaining above the national five-year and three-year reference amounts in 2005–06, 2006–07 and 2007–08 respectively).<sup>203</sup>

**Waivers of the expenditure maintenance requirements**

**4.72** Since commencement of the Standard Program, it has been DITRDLG’s practice to waive the expenditure maintenance requirements for non-complying LGAs where an adequate reason for the non compliance has been given.<sup>204</sup> These waivers are approved under delegation from the Minister.<sup>205</sup>

**4.73** After a waiver is approved, DITRDLG advises the LGA in writing. This advice draws the LGA’s attention to the need for compliance in the future. It also advises that the department will monitor the LGA’s own source expenditure for the remainder of the program and that the LGA is expected to make up the shortfall in due course.

*ANAO analysis*

**4.74** ANAO identified that, as at completion of the audit fieldwork, a total of 276 waivers of the expenditure maintenance requirements had been issued by DITRDLG. Table 4.6 shows the results of ANAO’s analysis.

<sup>203</sup> The Attachment to the April 2009 submission included the following figures:

	Five-year reference amount	Three-year reference amount	2005–06	2006–07	2007–08
QLD	\$615 906 363	\$620 874 861	\$810 244 790	\$595 162 094	\$528 640 145
AUS	\$1 814 093 920	\$1 801 028 702	\$2 369 249 097	\$2 221 712 087	\$2 165 121 651

<sup>204</sup> ANAO did not observe any instances where DITRDLG refused a request from an LGA for a waiver of the expenditure maintenance requirements.

<sup>205</sup> See section 93(1) of the AusLink Act and section 91(1)(a) of the Nation Building Act. The delegation has been made to Senior Executive Service officers in DITRDLG.

**Table 4.6****Breaches and waivers of expenditure maintenance requirements for the period 2005–06 to 2008–09**

	2005–06	2006–07	2007–08	2008–09	TOTAL
LGAs that did not comply with the expenditure maintenance requirements (before applying averaging provisions)	18% (109 of 608)	15% (93 of 604)	12% (61 of 518)	10% (38 of 394)	
Total deficiency	\$27.7m	\$37.0m	\$17.3m <sup>A</sup>	\$12.6m	\$89.6m
Largest single LGA deficiency	\$2.5m	\$3.8m	\$2.0m	\$3.0m	
Total surplus	\$564.5m	\$680.7m	\$632.2m	\$532.0m	\$2409.4m
Largest single LGA surplus	\$84.9m	\$61.0m	\$44.3m	\$49.9m	
LGAs that remained non compliant with the expenditure maintenance requirements (after applying averaging provisions)	49% (53 of 109)	44% (41 of 93)	33% (20 of 61)	32% (12 of 38)	
Total deficiency	\$18.0m	\$11.8m	\$9.4m	\$4.3m	\$43.5m
Waivers Issued (Departmental Record—IMS Waivers List)	49	27	14	0	90
Waivers Issued (identified by ANAO)	51	28	158 <sup>B</sup>	39 <sup>C</sup>	276
Waivers required but not issued (identified by ANAO)	3	9	6	12 <sup>D</sup>	30
Waivers not required as LGAs not paid in that year	4	3	1	-	8
Waivers issued but not required (identified by ANAO)	5	nil	1	-	6

**Notes:**

Some figures have been rounded.

Data for 2008–09 was incomplete as not all LGAs had submitted their annual reports at the time of the audit fieldwork.

A. Excludes QLD LGA amalgamations.

B. Includes 31 waivers associated with QLD LGA amalgamations and 113 waivers associated with QLD LGA abolitions.

C. Includes 31 waivers associated with QLD LGA amalgamations and eight waivers associated with NT LGA amalgamations.

D. No waivers were issued as LGAs' annual reports were received after the last AusLink R2R payment was made.

Source: ANAO analysis of DITRD LG data.

**4.75** The table shows that the number of LGAs that did not comply with the expenditure maintenance requirements reduced year-on-year over the life of the AusLink R2R Program. It also shows the effect of the averaging provisions. For example, two out of every three LGAs that did not meet the basic requirement to maintain their own source expenditure in 2007–08 were deemed to have met the requirement in that year. This was because they had expended sufficiently more than the reference amount in 2005–06 (or 2004–05 and 2005–06) to bring their average expenditure, over the two (or three) years, to a level that met or exceeded the reference amount.

**4.76** Table 4.6 also illustrates that the majority of LGAs reported that they had spent more than the reference amount, on roads, from their own resources, for each year of the Standard Program. Total surplus spending reported by these LGAs far exceeded the total deficiencies incurred by LGAs that had underspent on roads from their own resources. For example, in 2005–06, the total for LGAs with an expenditure surplus was \$564.5 million, whereas the total for LGAs with an expenditure deficiency was \$27.7 million (\$18.0 million after averaging provisions). Nevertheless, the requirement is for each LGA to maintain its own source expenditure at or above the reference amount. As such, surplus expenditure by one LGA does not offset under-spending by another LGA. It is for this reason that caution should be exercised in interpreting aggregate figures on local government spending on roads.

**4.77** As also indicated in Table 4.6, ANAO found that a greater number of expenditure maintenance waivers had in fact been issued than was reflected in DITRDLG's records extracted from IMS. The department acknowledged to ANAO that it did not maintain a central register of waivers issued during the AusLink R2R Program and the reason for those waivers.<sup>206</sup> In October 2009, DITRDLG advised ANAO that it would maintain a comprehensive register in future for waivers issued under the Nation Building R2R Program.

**4.78** ANAO identified a potential anomaly in the expenditure maintenance requirements, in that there was no obligation on LGAs to expend any funds on roads from their own sources, unless they received an AusLink R2R payment during the relevant year. There were eight instances where LGAs did not maintain their own source expenditure, including after applying the less

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<sup>206</sup> Approved expenditure maintenance waivers were retained on the respective LGA's departmental file.

stringent averaging provisions, but were not required to do so anyway because of the timing of their R2R payments.<sup>207</sup>

**4.79** Thirteen LGAs were issued with two expenditure maintenance waivers and one LGA was issued with three waivers.<sup>208</sup> Delegates approving waivers were not provided with information on the LGAs' previous compliance history. In February 2010, DITRDLG advised ANAO that this information is now included in waiver proposals.

**4.80** In addition, ANAO noted that one LGA<sup>209</sup> had been issued a waiver in November 2007 in relation to determining the Reference Amount, on the basis that the LGA claimed not to have reliable records for the years 2000–01 and 2001–02. DITRDLG agreed that the average of the LGA's own source expenditure for the years 2002–03, 2004–04 and 2004–05 would be used (notwithstanding that the LGA had reported own source expenditure to WALGA for 2000–01 and 2001–02).

#### *Making up for expenditure maintenance shortfalls*

**4.81** ANAO analysed whether the LGAs that had not complied with the expenditure maintenance requirements had made up for the identified shortfall in the following years, as expected by DITRDLG.<sup>210</sup>

**4.82** Of 53 LGAs that remained non compliant in 2005–06 (after applying the averaging provisions), eight LGAs were abolished and 18 LGAs again had shortfalls (after applying the averaging provisions) in one or more of the next three years.<sup>211</sup> Of these LGAs, 15 had not yet made up the cumulative shortfall, based on available data, at the time of the audit fieldwork.<sup>212</sup> Individual LGA

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<sup>207</sup> That is, the eight LGAs received one or more R2R payments in the preceding financial year or the following financial year. In addition, all small LGAs that were paid their full allocation in the first year of the program (up to \$250 000), also effectively had no obligation to maintain their own source expenditure during the following three years.

<sup>208</sup> Excludes multiple waivers issued in association with LGA amalgamations. Also excludes instances where a waiver was required but was not issued by DITRDLG. Three LGAs had their first and second waiver approved concurrently.

<sup>209</sup> Augusta–Margaret River (WA).

<sup>210</sup> The number of years over which the shortfall was expected to be rectified was not specified by DITRDLG.

<sup>211</sup> An August 2009 submission to the Delegate advised that 46 LGAs had breached the expenditure maintenance requirements in 2005–06. It reported that of these, seven LGAs were abolished and nine LGAs had not made up the shortfall by 30 June 2008.

<sup>212</sup> At this time a number of LGAs had not yet submitted their 2008–09 R2R Annual Reports.

deficiencies ranged from about \$7500 to some \$4.2 million. The total cumulative shortfall was approximately \$12.5 million.<sup>213</sup>

**4.83** Similarly, of 24 LGAs that had incurred their first shortfall in 2006–07, five LGAs were abolished and 12 LGAs had not made up the shortfall at the time of the audit. The largest single LGA deficiency was \$3.2 million. The total shortfall was approximately \$6.75 million.

## **Accuracy of reported own source expenditure**

**4.84** Although maintaining own source expenditure is a relatively simple concept, the practical application of this requirement has presented challenges for LGAs and DITRDLG.

**4.85** From around the time that the first R2R Annual Reports under the Standard Program were submitted, DITRDLG has been aware that the reporting by LGAs of their own source expenditure has been error prone. Furthermore, this situation did not improve significantly over the life of the program. For example, ANAO observed that:

- the own source expenditure figures are reported in Part 3 of the R2R Annual Reports ‘Statement on Expenditure Maintenance by Chief Executive Officer’. As such, these figures are not included within the scope of the independent audit, which covers Part 1 only;
- R2R Circular 2006/18 was issued by the department in November 2006 in response to many LGAs confusing FAGs with own source funds; and some LGAs viewing own source expenditure as only the LGA’s expenditure from its own sources on jointly funded R2R projects;
- each year DITRDLG wrote to numerous LGAs to clarify or correct apparent anomalies in reported expenditure figures for the current year or previous years;
- although unprompted by DITRDLG, many LGAs revised their previously reported expenditure figures (some even revised previous revisions);
- a series of financial audits of LGAs commissioned by DITRDLG and conducted by a contractor in 2007, 2008 and 2009 found that 29 per cent

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<sup>213</sup> Excludes abolished LGAs.



of the LGAs examined had misreported their own source expenditure for one or more years<sup>214</sup>; and

- in responding to ANAO's request for documentation supporting their calculated own source expenditure figures:
  - three LGAs in the ANAO sample sought to revise their previously reported expenditure;
  - 14 LGAs in the sample could not or did not provide any supporting data<sup>215</sup>; and
  - in relation to ten LGAs in the sample, ANAO was unable to satisfactorily reconcile the expenditure information provided in the supporting documentation to the expenditure figures reported to DITRDLG.

**4.86** It is also important that DITRDLG update its records where revisions to an LGA's expenditure maintenance figures are brought to attention. ANAO noted several instances where amendments did not occur, notwithstanding that audits commissioned by DITRDLG had reported corrected figures. Although these amendments, had they been made, would generally have had no impact on whether the respective LGAs met the requirement in the then current year<sup>216</sup>, they may potentially affect calculations in subsequent years, including under the averaging provisions for the remainder of the AusLink Program and determination of the reference amount under the Nation Building Program.

#### *ANAO analysis of statutory financial statements*

**4.87** For the LGAs in the sample, ANAO attempted to independently verify the own source expenditure figures reported to DITRDLG by analysing information disclosed in the LGAs' 2000–01 to 2007–08 statutory financial statements. This analysis was not possible for Victorian LGAs, as roads expenditure by LGAs in Victoria is aggregated with other types of expenditure

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<sup>214</sup> Independent financial audits of seven LGAs undertaken earlier for DOTARS by another contractor had found that only three LGAs had complied with the expenditure maintenance requirements in 2005–06.

<sup>215</sup> Only 17 LGAs provided supporting data for all relevant years.

<sup>216</sup> For example, although the actual expenditure determined during the financial audit was lower than previously reported by the LGA, the actual expenditure still exceeded the reference amount.

in the LGAs' financial statements. Accordingly, Table 4.7 outlines the results for the sample LGAs in NSW and WA only.

**Table 4.7**

**Analysis of own source expenditure derived from statutory financial statements of NSW and WA sample LGAs for the period 2000–01 to 2007–08**

Reported expenditure for the year was:	NSW		WA	
	Number	Per cent	Number	Per cent
Higher than calculated by ANAO	31	33	15	15
Lower than calculated by ANAO	52	56	84	82
Within + or – 5 per cent of ANAO calculation	10	11	3	3
<b>TOTAL</b>	<b>93</b>	<b>100</b>	<b>102</b>	<b>100</b>
Note: Excludes years where data not available or not comparable, for example, due to LGA amalgamations.				

Source: ANAO analysis of DITRDLG data and ANAO sample LGAs' statutory financial statements.

***ANAO analysis of WALGA own source expenditure data***

**4.88** WALGA has reported on WA road assets and expenditure annually since 1993–94. ANAO used data published by WALGA on own source roads expenditure by LGA covering the period 1998–99 to 2007–08.<sup>217</sup> This analysis indicated that the own source expenditure figures reported by WA LGAs to the department for the years 2000–01 to 2007–08 were:

- higher than reported by LGAs to WALGA in 32 per cent of instances;
- lower than reported by LGAs to WALGA in 45 per cent of instances; and
- the same as reported by LGAs to WALGA (or within plus or minus five percent) in 23 per cent of instances.

**4.89** ANAO also used the WALGA data to calculate the (notional) reference amounts for each LGA in WA under the initial Program and the Standard Program, as discussed below. In relation to the requirement to maintain own source expenditure at or above the reference amount under the initial Program, ANAO found that:

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<sup>217</sup> WALGA 2007–08. op. cit.

- 89 per cent of LGAs in WA (126 of 142) did not meet the requirement in one or more years over the period 2000–01 to 2007–08;
- three LGAs did not meet the requirement in any year during this period (see Table 4.8);
- 11 LGAs did not meet the requirement in seven of the eight years; and
- 30 per cent of LGAs had not made up the cumulative shortfall in their expenditure (approximately \$56 million as at 30 June 2008).

**Table 4.8**

**Number of years WA LGAs did not meet Initial R2R Program reference amount during the period 2000–01 to 2007–08**

Number of years requirement not met	None	One	Two	Three	Four	Five	Six	Seven	Eight
Number of LGAs	17	24	18	23	26	11	9	11	3
Per cent	12	17	13	16	18	8	6	8	2
Note: Some percentage figures have been rounded.									

Source: ANAO analysis of WALGA data.

**4.90** Furthermore, ANAO found that in relation to the reference amount under the Standard Program:

- 56 per cent (79 LGAs) did not meet the requirement in one or more years over the period 2005–06 to 2007–08;
- 27 per cent of LGAs had not made up the cumulative shortfall in their expenditure over this three year period (approximately \$32 million shortfall as at 30 June 2008); and
- 38 per cent (54 LGAs) actually had a lower reference amount under the Standard Program than under the initial Program (approximately \$9.9 million lower in total for affected WA LGAs).

*Definition of own sources*

**4.91** It is likely that the widespread inconsistencies apparent in the reporting of own source expenditure by LGAs arise from a variety of underlying causes. For example, there may be staff changes over time, or variations in the types of roads expenditures made by the LGA from one period to another. In this regard, in measuring their own source expenditure over the duration of the

R2R Programs, LGAs may not have shared (and possibly still do not share) a common and consistent understanding.

**4.92** Although the definition of 'roads expenditure' is relatively clear in relation to eligible funded R2R projects, the Notes (section 8.2) advised LGAs that, for the purposes of the program's expenditure maintenance requirements:

On the definition of 'roads expenditure', we will accept two definitions:

- (a) you can use the definition you use in your general council accounts; or
- (b) you can use the definition of roads used under the *Roads to Recovery* Program.

**4.93** In examining the documentation provided by LGAs in the audit sample in support of their expenditure maintenance calculations, ANAO observed that although practices varied, LGAs typically included a range of 'non-roads' expenditures in their calculations. These included items such as: footpaths; driveways; car parks; bus shelters; malls; general administrative expenses and overheads; and street furniture, presumably in accordance with the LGA's interpretation of the wider definition of roads expenditure permitted by DITRDLG under item a) above.

**4.94** In essence, own source expenditure is self-assessed by LGAs and is largely open to individual interpretation. It is therefore not surprising that amounts reported by LGAs vary.

## **Nation Building R2R Program**

**4.95** On 9 September 2009, new funding conditions for the Nation Building R2R Program were approved by the Minister. These set the new five-year reference period for determining an LGA's own source expenditure as the period commencing on 1 July 2004 and ending on 30 June 2009. While retaining the previous two methods for determining reference amounts (five-year average or three-year average), section 3.1 (iii) of the Conditions was also amended to provide LGAs with a new option. This allowed LGAs to select their Standard Program reference amount as at 30 June 2009, increased by a factor of 11.5 per cent, if this method provided a lower figure than using either the five-year average or the three-year average.

**4.96** DITRDLG advised the Minister that the adjustment factor of 11.5 per cent was in line with the Australian Bureau of Statistics producer price index relating to construction for the period 2004-05 to 2008-09. However, ANAO analysis found that an error had been made when calculating the

adjustment factor (effectively halving the increase). In addition to the mathematical error, there are questions about whether a methodology employing three base years was appropriate in the circumstances, given that it is more common to inflate/deflate all figures to the same base year. In this respect, available indices show that prices had increased over the relevant period (June 2001 to June 2009) by some 25 per cent if using the ABS Consumer Price Index, or by some 45 per cent if using the ABS Roads and Bridges Construction Producer Price Index.

**4.97** In addition to the abovementioned changes to the Conditions, the definition of own source funds was amended to exclude private sector funds from these calculations. DITRDLG advised the Minister that this change was required because:

There is an anomaly in the current conditions which means that if, in a particular year, a developer makes a large payment to a council in relation to a project it is undertaking, that payment is included in the council's own source expenditure. This can, depending on the year in which the payment is made, result in an abnormally high reference amount or enable a council to comply with the expenditure maintenance requirements when it has spent little of its own funds on roads.

**4.98** There was also one other significant change introduced with the Nation Building R2R Program. It was not reflected in the new funding conditions, but was addressed in the new program guidelines. It involved an amendment to the definition of roads expenditure to allow depreciation of LGAs' plant and equipment as a recoverable R2R road cost.

## Recommendation No.4

**4.99** ANAO *recommends* that, given the importance to both the Roads to Recovery and Strategic Regional Programs of Local Government Authorities maintaining their own level of expenditure on roads, the Department of Infrastructure, Transport, Regional Development and Local Government:

- (a) obtain greater assurance over the accuracy of own source roads expenditure reported to it by Local Government Authorities by requiring these figures to be included in the scope of the Audit Certificate included with each Authorities' Annual Report on the use of program funds; and
- (b) develop a more effective range of sanctions to apply in circumstances where own source expenditure has not been maintained, with a

particular focus on those Local Government Authorities that frequently fail to maintain their annual expenditure and/or that do not make up shortfalls in later years.

#### **DITRDLG Response**

**4.100** Part (a) Agree.

**4.101** Part (b) Agree. The department will include own source expenditure requirements in the review of administrative arrangements to be undertaken in response to Recommendation 2.

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Ian McPhee

Auditor-General

Canberra ACT

22 April 2010

# Appendices





## Appendix 1: Representative sample of 41 LGAs

LGA	ACLG Category <sup>1</sup>	Population Change Rate	Total AusLink R2R Standard Program Allocation (\$)	AusLink R2R Supplementary Program Allocation (\$)	Number of Standard Program Projects Examined	Number of Supplementary Program Projects Examined
<b>ACT</b>						
TAMS <sup>2</sup>	-	0-5% growth	20 000 000	5 000 000	1	1
<b>Subtotal for State</b>			<b>20 000 000</b>	<b>5 000 000</b>	<b>1</b>	<b>1</b>
<b>NSW</b>						
Blacktown City	UDV	10-20% growth	4 793 615	1 198 404	11	2
Bombala	RAM	10-20% decline	1 126 016	281 504	7	1
Clarence Valley	URM	0-5% growth	5 225 105	1 306 276	22	6
Gunnedah	RAV	5-10% decline	2 481 436	620 359	21	7
Maitland	URM	>20% growth	1 894 713	473 678	6	2
Mosman	UDS	0-5% growth	403 778	100 945	8	2
Shoalhaven City	URL	10-20% growth	4 977 049	1 244 262	4	2
Singleton	URS	10-20% growth	1 873 423	468 356	11	3
Tamworth Regional	URM	5-10% growth	6 429 232	1 607 308	25	1
Tweed	URL	>20% growth	4 112 438	1 028 110	5	3
Walcha	RAM	0-5% decline	1 392 148	348 037	6	1
Warrumbungle	RAV	0-5% decline	3 833 408	958 352	13	2
Wollondilly	UFM	>20% growth	2 172 962	543 241	10	5
<b>Subtotal for State</b>			<b>40 715 323</b>	<b>10 178 832</b>	<b>149</b>	<b>37</b>
<b>VIC</b>						
Baw Baw	URM	10-20% growth	4 815 094	1 203 774	22	8
Campaspe	URM	5-10% growth	7 082 243	1 770 561	29	4
Casey	UFV	>20% growth	3 406 571	851 643	7	1
East Gippsland	URM	5-10% growth	9 224 114	2 306 029	18	6
Greater Bendigo	URL	10-20% growth	5 146 521	1 286 630	10	2
Greater Dandenong	UDV	0-5% decline	2 327 333	581 833	12	2
Hume	UFV	>20% growth	2 882 762	720 691	7	1
Kingston	UDV	5-10% growth	1 966 083	491 521	8	2
Strathbogrie	RAL	0-5% growth	3 558 567	889 642	20	2
Towong	RAL	0-5% decline	2 598 212	649 553	16	4
Yarra Ranges	UFV	0-5% growth	5 914 931	1 478 733	24	7

LGA	ACLG Category <sup>1</sup>	Population Change Rate	Total AusLink R2R Standard Program Allocation (\$)	AusLink R2R Supplementary Program Allocation (\$)	Number of Standard Program Projects Examined	Number of Supplementary Program Projects Examined
<b>Subtotal for State</b>			<b>48 922 431</b>	<b>12 230 610</b>	<b>173</b>	<b>39</b>
<b>WA</b>						
Armadale	UFM	0-5% growth	1 720 925	430 231	2	6
Beverly	RAS	5-10% growth	808 114	202 029	12	6
Boddington	RAS	10-20% decline	321 415	80 354	6	3
Brookton	RAS	5-10% growth	564 568	141 142	7	2
Cuballing	RAS	0-5% growth	597 372	149 343	13	3
Gosnells	UFL	>20% growth	4 129 143	1 032 286	9	1
Joondalup	UFV	0-5% growth	3 737 056	934 264	13	4
Mandurah	URM	>20% growth	1 564 088	391 022	1	1
Narrogin Town	URS	10-20% decline	287 357	71 839	10	-
Peppermint Grove	UDS	0-5% decline	33 078	8 270	2	1
Rockingham	UFL	>20% growth	2 391 952	597 988	7	3
Swan	UFL	>20% growth	3 446 883	861 721	9	-
Victoria Park	UDS	5-10% growth	628 374	157 094	8	1
Wanneroo	UFL	>20% growth	2 880 905	720 226	7	1
Waroona	RAM	10-20% growth	632 477	158 119	8	3
Wickepin	RAS	>20% decline	886 570	221 643	13	1
<b>Subtotal for State</b>			<b>24 630 277</b>	<b>6 157 571</b>	<b>127</b>	<b>36</b>
<b>TOTAL</b>			<b>134 268 031</b>	<b>33 567 013</b>	<b>450</b>	<b>113</b>
Notes 1. ACLG Categories are explained in Table 2 of this Appendix. 2. ACT Department of Territories and Municipal Services.						

Source: Local Government National Report 2005–06. DITRD LG Population Change 1997–2006 accessed from [www.infrastructure.gov.au](http://www.infrastructure.gov.au).

**Table 2****Australian Classification of Local Government (ACLG) category descriptions**

	Category	Number of LGAs	Number of LGAs included in ANAO's sample
RAL	Rural Agricultural Large (RAL)	68	2
RAM	Rural Agricultural Medium (RAM)	80	3
RAS	Rural Agricultural Small (RAS)	75	5
RAV	Rural Agricultural Very Large (RAV)	70	2
RSG	Rural Significant Growth (RSG)	9	-
RTL	Rural Remote Large (RTL)	11	-
RTM	Rural Remote Medium (RTM)	28	-
RTS	Rural Remote Small (RTS)	30	-
RTX	Rural Remote Extra Small (RTX)	43	-
UCC	Urban Capital City (UCC)	7	-
UDL	Urban Developed Large (UDL)	23	-
UDS	Urban Developed Small (UDS)	17	3
UDM	Urban Developed Medium (UDM)	28	-
UDV	Urban Developed Very Large (UDV)	20	3
UFL	Urban Fringe Large (UFL)	11	4
UFM	Urban Fringe Medium (UFM)	14	2
UFS	Urban Fringe Small (UFS)	29	-
UFV	Urban Fringe Very Large (UFV)	12	4
URL	Urban Regional Large (URL)	7	3
URM	Urban Regional Medium (URM)	39	7
URS	Urban Regional Small (URS)	68	2
URV	Urban Regional Very Large (URV)	11	-
<b>Total</b>		<b>700</b>	<b>40</b>
Note: Total excludes ACT, which does not have an ACLG Classification.			

Source: ANAO analysis and *Local Government National Report 2005–06*.

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