Attorney-General’s Luncheon

Corporate Governance – More than a Passing Fad

12 June 2002

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CORPORATE GOVERNANCE – MORE THAN A PASSING FAD

Governance and associated subjects have become, both explicitly and implicitly, important issues for business, government, politics, and last but not least for the general public. ¹

I. OPENING REMARKS

Thank you for your invitation to speak at the Alfred Deakin Club luncheon on a topic which is central to our success as a responsive, and results oriented, public service. For some years now, I have been seeking to foster a healthy and positive corporate governance culture in the Australian Public Service (APS) through presentations such as this, and by making corporate governance a prominent theme in the Australian National Audit Office’s (ANAO’s) audit coverage. As my colleague Ian McPhee observed recently:

The profile given to corporate governance in the public sector has been one of the most positive stimuli for change and better performance in the last decade. It may not have received top billing among the specific reform agenda items but it has always been seen as a front row contributor to a highly performing Australian Public Service (APS) that has universal application to all Commonwealth bodies. ²

Over the past decade, policy makers, regulators, and market participants around the world have increasingly come to emphasise the need to develop good corporate governance practices. There is no doubt that good corporate governance is inexorably linked to good performance and achieving required results in a reasonable timeframe. However, in order to ensure good performance in a changing world, the OECD has noted that organisations must innovate and adapt their corporate governance practices so that they can meet new demands and grasp new opportunities.³

Importantly, with of the recent spate of corporate failures in Australia and overseas the term ‘corporate governance’ is also receiving significant coverage in the media. It is now well and truly in the wider public arena generating a heightened public awareness of the concept and what it entails. Notwithstanding this awareness, corporate governance is one of those fundamental, but in some ways fuzzy, concepts that, on one hand, many organisations claim to understand and implement, yet on the other, do not come to grips with in practice. As I stressed in my foreword to the ANAO’s Better Practice Guide on Corporate Governance:

The challenge ... is not simply to ensure that all the elements of corporate governance are effectively in place but that its purposes are fully understood and integrated as a coherent and comprehensive
organisational strategy focussed on being accountable for its conduct and results.  

A note of caution should, however, be sounded. Even when all these elements come together, there is still no guarantee that there will not be failures or breakdowns in governance structures and operations. As one commentator said recently ‘Governance is about how people work together and the recent crop of failures are about human frailty, and that no system will ever fix’.  

Along similar lines, David Morgan, Chief Executive Officer (CEO) of Westpac, recently noted that:

...at the end of the day, you can’t legislate goodness, and important as accounting standards are, and as independent auditors are, corporate governance is really a state of mind and it is around the integrity of the company and its leadership...

Many would agree that ‘tone at the top’ is an essential element of sound corporate governance and its integrity and credibility. The investment community is increasingly recognising this both in their decisions and direct involvement in demanding, and creating, improvements in the governance framework of many corporates.

Going back in history, Sir Isaac Newton (who reportedly lost £20,000 in the infamous 1720 South Sea Bubble saga) claimed:

I can calculate the motions of heavenly bodies but not the madness of people

Nor will focusing on one element in isolation (for example the current issue of auditor independence) be a ‘cure all’, as it is unrealistic to expect any single governance measure to be a failsafe panacea. The challenge is not to focus primarily on process or even just on selected elements of the governance framework, but rather to have a holistic integrated approach that takes account of both strategic and operational issues and other imperatives for the organisation. That is, it is not enough to simply put the various elements of good corporate governance in place. The imperative is to ensure that those elements are effectively integrated; well understood; applied effectively; and, importantly, an appropriate balance is maintained between the conformance and performance requirements of the organisation.

Finally, but no less importantly, one size does not fit all as organisations do have different needs at different times. However, there are intrinsic issues and approaches where we are able to point to better practice that can help all of us to establish sound frameworks that can address the particular needs of the time. Perhaps, more importantly, the measures can be preventative or facilitative, depending on whether we need to avoid, counter, or take advantage of the circumstances confronting us.

Turing to my brief for today, I thought the best way to cover the ground in the time available is to lightly cover the important elements of good corporate governance, and then drawing on recent audit reports and two high profile private sector examples, highlight some lessons for the future. Firstly, corporate governance – what is it?
II. **CORPORATE GOVERNANCE – AN OVERVIEW**

Corporate governance in the public sector has to be understood in the context of the overall governance framework. Governance is:

> the structural manifestation of state adaptation of its external social, political and economic environment with particular reference to the evolving processes and mechanisms of control, co-ordination, accountability and the location of power within complex networks.\(^8\)

Or,

> [Government] Governance is defined as safeguarding the interrelationship between management, control and supervision by government organisations and by organisations set up by government authorities, aimed at realising policy objectives efficiently and effectively, as well as communicating openly thereon and providing an account thereof for the benefit of the stakeholders.\(^9\)

In simple terms, corporate governance is the system by which companies or organisations are directed and controlled.\(^10\) It is about how an organisation is managed, its corporate and other structures, its culture, its policies and strategies, and the ways in which it deals with its various stakeholders. It is concerned with structures and processes for decision-making and with the controls and behaviour that support effective accountability for performance outcomes/results.

The ANAO’s discussion paper *Principles for Core Public Sector Corporate Governance: Applying Principles and Practice of Corporate Governance in Budget Funded Agencies* \(^{11}\) aimed at fostering good corporate governance in the public sector, included a checklist designed to assist CEOs to assess the strengths and weaknesses of their agencies’ current governance framework. The following key operating principles underpin a sound corporate governance framework in the public sector:

- **openness** is about providing stakeholders with confidence regarding the decision-making processes and actions of public sector agencies in the management of their activities. Being open, through meaningful consultation with stakeholders and communication of complete, accurate and transparent information leads to effective and timely action and lends itself to necessary scrutiny;

- **integrity** is based on honesty, objectivity as well as high standards of propriety and probity in the stewardship of public funds and the management of an agency’s affairs. It is dependent on the effectiveness of the control framework and on the personal standards and professionalism of the individuals within the agency. Integrity is reflected in the agency’s decision-making procedures and in the quality of its performance reporting;
accountability is the process whereby public sector agencies and the individuals within them are responsible for their decisions and actions and submit themselves to appropriate external scrutiny. Accountability can only be achieved when all parties have a clear understanding of their responsibilities and roles are clearly defined through a robust organisational structure; and

leadership involves clearly setting out the values and standards of the agency. It includes defining the culture of the organisation and the behaviour of everyone in it.\textsuperscript{12}

Against these over-arching principles, the important components of corporate governance in the APS include the following eight elements.

A Contemporary Legislative Framework

Any discussion of good governance in the federal public sector needs to be undertaken against the backdrop of at least the following legislative framework:

- the Financial Management and Accountability (FMA) Act;
- the Commonwealth Authorities and Companies (CAC) Act;
- the Public Service Act; and
- the Workplace Relations Act.

Central to this legislative framework is the clear responsibility of Chief Executive Officers/heads of public sector agencies under the FMA Act for promoting the efficient, effective and ethical use of resources. Chief Executives now carry more responsibility than in the past, both due to the legislative changes and also because of the devolution of authority to agencies from the coordinating agencies for a wide range of personnel, workplace relations and financial management functions. Basically, they need a clear view of their role and mission, commitment, stamina, strategic direction, and good ongoing support.

For organisations subject to the CAC Act, and which normally involve boards, it has been suggested that, in terms of governance dimensions, there is a heavy focus on conformance:

\begin{quote}
Through its (the Act’s) primary emphasis on directors’ duties, public auditing, and public reporting obligations, rather than on substantive performance, sustainability, or any of the other dimensions of corporate governance.\textsuperscript{13}
\end{quote}


It was as if the board had become reckless in its indifference to the realities. To propound and adopt a plan that simply did not make sense compels a conclusion that neither management nor
Prime elements in a corporate governance framework and, indeed, key responsibilities of directors (or CEOs), are setting the direction of the organisation and monitoring performance. One of the real challenges facing agencies is how to devote the necessary time and energy to longer term strategic initiatives and new approaches, while managing on a day-to-day basis. There are no easy answers to this conundrum but, suffice to say, that agencies need to invest today for progress tomorrow.

The governing body has to consciously put in place sound strategies to deliver better targeted and more efficient outcomes and to ensure the agency has the capability to deliver, that is, organisational alignment should follow strategy. In the APS in particular, the major areas where these imperatives are at a premium is in relation to our people and our information, or knowledge.

**A Sound Risk Management Framework**

*Effective risk management means being able to anticipate, prepare for and mitigate adverse outcomes, without eradicating, or unnecessarily hindering, beneficial risk-taking. Letting risks get out of hand, or being rendered powerless by not taking any risk, can destroy organizations.*

Corporate governance is concerned with achieving results while taking account of risk, thus making formal risk management an essential element of sound corporate governance and management practice. It is becoming even more important in the move to a more networked or joined-up government.

Risk management is primarily the responsibility of the CEO and/or board. Effective governance arrangements require the identification of business risks, as well as potential opportunities, and ensure the establishment, by management, of appropriate processes and practices to manage all risks associated with the organisation’s operations. The goal for all agencies should be to embed a culture of risk management in their organisations so that the consideration of risks, and risk mitigation strategies, becomes second nature. This is particularly important as the nature and significance of risks change in the public sector as the role of the public sector itself changes. The lack of suitable risk management practices generally features in examples of poor administration that are highlighted in our audit reports from time to time. Many managers are still coming to grips with the notions of insurable and non-insurable risk.

The devolution of authority and accountability to agency heads and the recent changes to financial and industrial legislation, together with contracting out and contestability, has significantly increased the risk profile of agencies. With the wide range of business risks being confronted, I am not alone in suggesting we need a more holistic approach to the identification and management of risk in the business environment. James Deloach, a partner in Arthur Andersen, highlights the criticality of managing business risk using an enterprise-wide approach which:
aligns strategy, processes, people, technology and knowledge with the purpose of evaluating and managing the uncertainties the enterprise faces as it creates value\textsuperscript{17}

This approach minimises the influence of the management `stove pipes’; leading to a more holistic, integrated, proactive and process oriented approach being taken to manage all key risks and opportunities. This theme has been picked up in CPA Australia’s publication ‘Enterprise-Wide Risk Management’.\textsuperscript{18} You might be interested in the management self-assessment tool included as Appendix 1 in that publication.

CPA Australia recently surveyed thirty-one public sector agencies from the three tiers of government (CPA Australia Risk Management Survey 2001). Commenting on the survey results, Adam Awty, the public sector policy adviser for CPA Australia, observed that:

\textit{It [risk management] is now becoming entrenched within the public sector and is resulting in better performance. CPA Australia’s survey results show that the public sector has moved to address risk management and is now more accountable, better managed and a better service provider than it was in the mid-1990s... The challenge for the future is to develop mature methodologies such as risk-performance indicators and benchmarking. Public-sector agencies also need more sophisticated skills to monitor, communicate and link risks directly with corporate objectives.\textsuperscript{19}}

While there are many positives in the survey, one disturbing response was that less than half the organisations covered considered their corporate culture considerably, or significantly, encourages individuals to encourage their peers to take responsibility for identifying risks.

\textbf{An Effective Control Environment}

Complementary to a sound risk management approach is a robust system of administrative control. Again, the notion of a control environment needs to start from the top of an agency and, to be effective, it requires clear leadership and commitment. This imperative is reinforced by the interrelationship of risk management strategies with the various elements of the control culture. The adoption of a sound and robust control environment at the top of an agency will strongly influence the design and operation of control processes and procedures to mitigate risks and achieve the agency’s objectives. The clear intent and message to staff should be that such processes and procedures are designed to facilitate, rather than to inhibit, performance. This approach should be promoted as good management. In short, the control environment is a reflection of management’s attitude and commitment to ensuring well controlled business operations that can demonstrate accountability for performance.

Importantly, in carrying out this responsibility, management should review the adequacy of internal controls on a regular basis to ensure that all key controls are
operating effectively and are appropriate for achieving corporate goals and objectives. The entity’s executive board, audit committee and internal audit are fundamental to this exercise. Management’s attitude towards risk and enforcement of control procedures strongly influences the control environment.

In the ANAO’s experience, it is difficult to overstress the importance of integrating the agency’s approach to control with its overall risk management approach in order to determine and prioritise the agency functions and activities that need to be controlled. Both require similar disciplines and an emphasis on a systematic approach involving identification, analysis, assessment and monitoring of risks. Control activities to mitigate risk need to be designed and implemented and relevant information regularly collected and communicated throughout the organisation. Management also needs to establish ongoing monitoring of performance to ensure that objectives are being achieved and that control activities are operating effectively.20

The key to developing an effective control framework lies in achieving the right balance so that the control environment is not unnecessarily restrictive nor unduly encourages risk averse behaviour and, indeed, aims to promote sound risk management. As one commentator observes:

All organisations face a central problem of autonomy and control. ...Too much autonomy and too little control can undermine coordination and prevent the delivery of a consistent service and product. Too much control at the center can undermine motivation among those who are furthest from the source of power....The challenge is to balance the control necessary for a united strategy with sufficient autonomy to foster initiative and responsiveness 21

The control structure must provide a linkage between the agency’s strategic objectives and the functions and tasks undertaken to achieve those objectives. A good governance model will include a control and reporting regime which is geared to the achievement of the organisation’s objectives and which adds value by focusing control efforts on the ‘big picture’ and not simply on particular processes.

Finally, it must be kept in mind that control is basically a process, a means to an end, and not an end in itself. It impacts on the whole agency; it is the responsibility of everyone in the agency; and is effected by staff at all levels.

Clearly Defined Responsibilities

The principles of corporate governance require those involved to identify and articulate their responsibilities and their relationships; and consider who is responsible for what, to whom, and by when. Or put another way, good corporate governance requires a clear identification and articulation of: the definitions of responsibility; a real understanding of relationships between the organisation’s stakeholders and those entrusted to manage its resources and deliver its outcomes; and support from management, particularly from the top of an organisation. In a complex operating environment, such as is evident in the APS, these requirements become that much more important for both accountability and performance (and results) to a range of stakeholders
Hence, a clear understanding and appreciation of the roles and responsibilities of the relevant participants in the governance framework (importantly, those of the responsible Minister(s), Board and CEO) are key components of sound accountability. The flip side is that the absence of these features weakens accountability and threatens the achievement of organisational objectives.

**An Independent and Effective Audit Committee**

Ian McIntosh, formerly Chief Accountant at the Australian Securities and Investments Commission (ASIC) and now dealing with country financial management in the World Bank, in nominating his five top tips for directors, singles out audit committees as being of particular importance, as follows:

*The audit committee is a vital part of your company’s governance structure. It is crucial that you have confidence in their integrity and commitment, and that they have confidence in yours. An independent and fearless audit committee will report accurately back to you on the true state of the company.*

Audit committees provide a complementary vehicle for implementing relevant control systems incorporating sound risk management plans. This view is shared by the private sector, where effective audit committees and risk management plans are an indication of best practice and markedly improve company performance, including decision-making. The internal auditing function of an organisation plays an important role in this respect by examining and reporting on control structures and risk exposures and the agency’s risk management efforts to the agency governance team. It is interesting to note that Federal Government legislation requires all Commonwealth organisations to have an audit committee. Yet it is only recently that a recommendation was made for corporations to have such a committee as a condition of Australian Stock Exchange Listing.

An effective audit committee can improve communication and coordination between management and internal and well as external audit, and strengthen internal control frameworks and structures to assist CEOs and boards meet their statutory and fiduciary duties. The committee’s strength is its demonstrated independence and power to seek explanations and information, as well as its understanding of the various accountability relationships and their impact, particularly on financial performance. Both internal and external audit have an important part to play in assisting the committee to be effective in this goal. In turn, the committee plays a significant role in ensuring the effectiveness of the various audit processes and operations, including the implementation of audit recommendations.

A recent Canadian publication states that, for audit committees, there are three key outcomes that need to be achieved and, additionally, the committee mandate should explicitly recognise them. These outcomes are as follows:

- The audit committee needs to assure itself that the auditors are independent. It must have access to all information about the audit firm’s relationship with the corporation that is necessary in order to come to a reasonable conclusion.
The audit committee needs to assure itself that the external auditors are satisfied that the accounting estimates and judgements made by management, and management’s selection of accounting principles, reflect an appropriate application of Generally Accepted Accounting Principles (GAAP).

The audit committee must develop a relationship with the external auditors that allows for full, frank and timely discussion of all material issues, with or without management as appropriate in the circumstances.  

The independence theme has been given a lot of air play lately with most authoritative reports recommending that, in the private sector, either the audit committee comprise only independent directors or at least include a majority of independent directors. The fundamental position is that an audit committee should be in a position to discuss matters with the auditors without the constraint of having senior management on the committee. Better practice would also indicate that the Board Chair or CEO should not chair the committee. Indeed, better practice would suggest there should be an independent chair.

In keeping with this theme, I have been gently advocating that public sector agencies appoint independent members to their audit committees, including giving consideration to the selection of an independent person to chair those committees. At the ANAO, we have appointed Will Laurie (a former Price Waterhouse partner) to chair our audit committee and, as another example, Defence has Paul McGrath (the former CEO of AMSA) to chair its audit committee with Will Laurie as an independent member.

**Agency Values and Codes of Ethics**

Good corporate governance is based on a clear code of ethical behaviour and integrity that is binding on management and staff and clearly communicated to stakeholders.

The values, standards and practices which underpin corporate governance in public sector agencies flow from peak public service values, obligations and standards, which in turn are derived from legislation, policy and accepted public service conventions. We have a clearly articulated set of Values set out in Section 10(1) of the Public Service Act 1999 which define the Australian Public Service and differentiate it from other organisations. All APS employees are required to uphold the APS Values and to comply with any directions by the Public Service Commissioner in relation to them. The Values, which outline the requirements of a highly performing, best practice organization, can be reduced to five key elements, namely:

- an impartial, apolitical and ethical public service;
- a public service that is responsive to the Government;
- a public service that delivers services fairly and courteously to the Australian public;
- a fair workplace; and
- a focus on achieving results and being accountable for performance.
Impartiality has been the most commonly identified core value in OECD countries.

Adherence to such values can have a marked impact on the culture and performance of any APS organisation. This should not just be seen in the narrow context of the prevention and detection of fraud, important as that is, but also extends to all behaviours and dealings within, and outside, the organisation. The OECD Public Management Committee has observed that fair and reliable public services inspire public trust and create a favourable environment for businesses. In particular, the Committee notes that:

*Public service ethics are a prerequisite to, and underpin, public trust, and are a keystone of good governance.*

**Performance Measurement and Review**

The Government has emphasised performance information as an integral part of its public management reforms with the main objective being to improve accountability and results. The move to an accrual-based outcomes/outputs framework was designed to ensure a focus on:

*Resource management with an emphasis on measuring performance, in terms of what is being produced, what is being achieved and what is the cost of individual goods and services…*

A fundamental starting point, once the key elements of the governance framework have been settled, is in good scorekeeping systems (balanced scorecards or executive snapshots) which firstly translate the organisation’s strategies into key operational indicators and then systematically report on the health of the business, both in terms of operational responsibilities and future positioning initiatives. This provides the feedback loop on the effectiveness of organisational strategies and the basis for communicating with staff and other stakeholders on how the agency is travelling. Without such reporting, there is a very significant risk of unfortunate surprises and belated, often expensive, recovery action.

Sound performance information can reduce the workload for individuals within an agency by making management information at all levels in the planning hierarchy readily available and applicable to their activities. Appropriate performance information enables individuals to determine how their activities contribute to agency outputs and, hopefully, its outcomes. For this reason, among others, it is essential that agency staff be made aware that performance information is a valuable management tool and that Portfolio Budget Statement (PBS) performance, accountability related, information and general management performance information are part of the same integrated framework.

I will take this opportunity to draw your attention to the just released Better Practice Guide on performance information which was developed in response to the Senate Finance and Public Administration Legislation Committee’s request to develop a guide relation to the development of performance information for the PBS. This builds on the earlier 1996 guide. The following diagram focuses on the key role performance information plays in the governance framework.
III. PRIVATE SECTOR GOVERNANCE FAILURES

Having set out what I see as the main drivers of corporate governance I will now focus on two very large corporate collapses – Enron and HIH, the largest companies to fail in the United States and Australia respectively. Both companies are now the subject of public enquiries and have become a ‘lightning rod’ with accusations of corrupt dealings and shonky accounting. Even though we await with a great deal of interest the outcome of these enquiries, some early observations have been made on the failures in the governance mechanisms.

The Enron collapse

The Enron Corporation collapse has provoked much recrimination and has added another word to our lexicon – Enronitis, and while the investigations continue, it is becoming clear that failures in corporate governance contributed to its downfall.

...every governance mechanism failed as Enron used money to influence the judgement of its auditors, audit committee, regulators and politicians... The suborning of governance was the modus operandi.

In the Enron case the issues appear to come down to: accounting and accounting standards; auditor independence; audit committees; and culture/ethics. Briefly the concerns are as follows:

a) Accounting/Accounting Standards

While too complex to go into detail here, the main points seems to be the use of complex accounting transactions, including off-balance sheet transactions, and the
adequacy of accounting standards. However the flavour of the concerns is captured in the following observation by the accounting firm Ernst & Young:

_A transaction that is over structured runs the risk of being perceived to be deliberately complex in order to mask the economic and commercial realities. Likewise if the transaction cannot be fully explained to the independent auditor then it will be near impossible for the auditor to satisfy her/himself as to the accuracy and appropriateness of the accounting treatment and disclosure of the transaction._

Currently, in Australia, increased attention is being given to the issue of potential fraud due to the introduction of a new auditing standard that explicitly requires auditors to consider, document and communicate with management on the issue of fraud. For example, there would need to be assurance of the existence of fraud control plans and that detected fraud is brought to attention. However, there is still no expectation that all fraud would be detected by an audit. The standard (AUS 210) states that:

_The primary responsibility for the prevention and detection for fraud and error rest both with those charged with the governance and the management of an entity._

**b) Auditor Independence**

A critical component of the ethical conduct of auditors is that they remain sufficiently independent in fact and in perception, to provide an unbiased and hence creditable audit opinion. Accounting firms have become more diversified and multi-disciplinary with a vast expansion of new non-audit services being offered to clients. These additional services range from outsourcing of many corporate business functions through to strategic business and financial planning.

The potential effect of non-audit services on auditor independence has long been an area of concern. This has been compounded of late due to the significant increase in the amounts of these additional services being performed. An interesting statistic that demonstrates the magnitude of this growth is that revenues from management and advisory services of the five largest public accounting firms is estimated to constitute half of total revenues for these firms compared to only 13 per cent of total revenues in 1981.

In the Enron case this issue is well described as follows:

_The auditor was Arthur Andersen whose $US50 million per annum web of business relations on external audit, internal audit and consultancy made Enron a highly valued customer. Andersen's Houston partners convinced themselves that the off-balance sheet vehicles were aggressive accounting though, as an Enron whistleblower noted, none would stand scrutiny in the bright light of day._
In February 2001, the United States SEC released a final ruling on the requirements for auditor independence which sets forth restrictions on financial, employment and business relationships between an accountant and an audit client and restrictions on an accountant providing certain non-audit services to an audit client. The ruling provides four principles by which to measure an auditor’s independence. These state that an accountant is not independent when the accountant:

- has mutual or conflicting interest with the audit client;
- audits his or her own firm’s work;
- functions as management or an employee of the audit client; or
- acts as an advocate for the audit client.

Additionally, the Comptroller General and head of the General Accounting Office (GAO) recently announced (25 January 2002) significant changes to the auditor independence requirements under Government Accounting Standards. The new standards deal with a range of auditor independence issues with the most significant changes relating to the rules associated with non-audit, or consulting services.

Australian auditors have also been under scrutiny. An important part of this scrutiny has been the Federal Government inquiry into the state of audit independence in Australia. The result is the Ramsay Report, released on 4 October 2001. In welcoming the Report, the Minister for Financial Services and Regulation observed that:

> We must ensure the independence of auditors is preserved and that stakeholders are secure with the knowledge that the auditor is objective and independent.

Professor Ramsay indicates a range of relationships with the client which would result in an auditor not being independent. These cover employment, financial and business relationships. Interestingly, he recommended that the regulation of non-audit services provided by audit firms to their clients be dealt with in professional ethical rules, suitably updated to reflect proposals being made by the International Federation of Accountants (IFAC). Perhaps more controversially, he also recommended the establishment of an Auditor Independence Supervisory Board to be funded by the professional accounting bodies. The other recommendations that I want to refer to here are those relating to amendments to the Corporations Act indicating a general statement of principle requiring an auditor to be independent and for the auditor to make an annual declaration, addressed to the board of directors, that the auditor has maintained its independence in accordance with the Corporations Law and the rules of the professional Accounting bodies.

This issue is causing accounting firms to examine their structures with some accounting firms announcing they would separate their consulting business or, indeed, have already done so. In Australia, the accounting bodies are currently reviewing the audit independence issue but noting the following observation:
Australia’s professional accounting bodies, such as CPA Australia, are content with this country’s self-regulatory regime, although it and the Institute of Chartered Accountants have distributed a discussion paper on the existing standards of audit independence. This is in contrast to the American Institute of CPA’s, which this month [February 2002] took the extraordinary decision to support moves to ban accounting firms from providing audit clients with internal audits or system integration. 42

Another possible threat to independence is where there has been a long association of senior audit personnel with the client. The IFAC now requires the rotation of audit signing partners when they have been in place for more than seven years, similar to the requirement that already exists in the United States. The Ramsay Report contained a similar recommendation. Some commentators have called for the rotation of audit firms after a period of time. However, this seems to have only limited support to date in the Australian context. 43

While the debate will continue amongst the profession worldwide, the issue of audit independence will come under further scrutiny in Australia with the JCPAA’s recent decision to launch an inquiry into this topic. The JCPAA will examine whether government should intervene to regulate the auditing profession. The issue of auditor independence is also likely to be considered as part of the royal commission into the collapse of HIH. The Statement of Auditing Standards AUS 1 requires an auditor not only to be independent, but also to appear to be independent. For the purpose of this Statement:

(a) actual independence is the achievement of actual freedom from bias, personal interest, prior commitment to an interest, or susceptibility to undue influence or pressure; and

(b) perceived independence is the belief of financial report users that actual independence has been achieved.44

While the Statement of Auditing Practice provides guidance to auditors when considering independence, the recently released Professional Statement F1, entitled ‘Professional Independence’ addresses the principles of independence. The ANAO supports the Ramsay Report45 recommendation that the auditor should make an annual declaration, addressed to the board of directors, that the auditor has maintained his/her independence in accordance with the Corporations Act 2001 and the rules of the professional accounting bodies. I should note that, pursuant to that Act, the Auditor-General is a registered company auditor. You may also be interested in a recent comment by Senator Andrew Murray that audit independence requires appointment by a third party, for example an elected corporate governance board additional to the main board.46

I should mention that the mandate of the Auditor-General is legislated by Parliament with funding provided by means of parliamentary appropriations. In my case, I am an independent Officer of the Parliament. I note the call by Professor Craig, I guess
'tongue in cheek’, to put public company audits in the hands of an independent government appointed public servant working for a statutory audit authority.  

c) The Audit Committee

Another important governance lesson from the Enron collapse is the essential role of the audit committee should play and the requirement that all members be completely independent. While there has been only limited coverage of this aspect, the following observation gives food for thought:

The [Enron] audit committee was a six-strong assembly drawn from all over the world… who never asked difficult questions…one had a consultancy contract, two benefited from Enron donations to their universities and collectively owned Enron shares worth $US 7.5 million at the peak.  

The Institute of Chartered Accounts in Australia and CPA Australia have just released a professional statement on ‘Professional Independence’. This statement provides a framework for identifying, evaluating and responding to threats to audit independence. The framework establishes principles that members of the profession should use to identify threats to audit independence, evaluate the significance of those threats, and, if the threats are other than clearly insignificant, identify and apply safeguards to eliminate the threats or reduce them to an acceptable level. The statement includes the following observation:

Audit Committees can have an important corporate governance role when they are independent of direct management and can assist the Board of Directors in satisfying themselves that a firm is independent in carrying out its audit role.

d) Culture and Risk

Early indications are that all was not well regarding the culture and ethics at Enron, the following is one commentator’s view of the situation:

[senior managers] created an organisation with an internal culture of recklessness. Bonuses and stock options incentivised them to deliver results – not raise problems. The resulting balance between individual incentive and corporate risk might be acceptable in a professional services firm which lived by charging out hours; in a trading house such as Enron, operating in areas where nobody understood the business model, the result was likely to be an unhealthy appetite for risk and a reluctance to accept bad news.

The HIH collapse

The dust surrounding the HIH collapse has not settled sufficiently to make any definitive judgements with Justice Neville Owen’s Royal Commission still taking evidence. Indeed, the scope has been widened to make it clear the Royal Commissioner can enquire into whether decisions or actions of any person
contributed to the failure of HIH or on any undesirable corporate governance practices. However a scanning of the media reports shows the recurring themes of: auditor independence, audit competence, creative accounting treatments, lack of due diligence, and the independence and effectiveness of audit committees.

The independence issues have been underscored by the fact that directors of HIH were also Andersen partners. Two members were ex-members of the accounting firm that, at the same time, undertook the external audit. As Henry Bosch observed:

*I think that’s far too cosy. Just having the machinery is not enough. You’ve got to use the machinery properly. An audit committee has a responsibility to ensure the independence of the auditors, and to have ex-partners sitting on the audit committee...seems to me to be a very unusual practice and not one to be recommended in practice*.54

And on the due diligence, risk management, and business planning front we have this telling observation:

*FAI was HIH’s Trojan horse. It was willingly, indeed enthusiastically, hauled into the middle of HIH’s Troy ...by the directors and senior management of HIH who thought it a great prize, only to discover soon after to their horror, that it contained the seeds of their own destruction.*55

I should note that an effective board is being increasingly recognised as one of the principal factors behind a firm’s success. With increasing public scrutiny, a board that can demonstrate in its annual reports that it has undergone a recognised process of evaluation can see its reputation for corporate governance significantly enhanced.56

IV. ANAO’S COVERAGE OF GOVERNANCE ISSUES

Turning closer to home, audit reports over recent years have highlighted the value of sound corporate governance as a stimulus to performance and compliance. However, there are some significant areas and common themes where weaknesses have arisen in public administration. Agencies need to take account of these when framing their corporate governance arrangements as significant damage to reputation, performance and accountability can be done through poor administration. For example, it is incumbent on all agencies to have in place mechanisms to continually monitor performance and conformance.

You would not be surprised that a quick ‘canter’ through recent audit reports has highlighted ‘the usual suspects’, to borrow the title from a Kevin Spacey movie. That is, there is not a great deal that is not known, or at least widely discussed, but the enduring problems are acceptance, commitment and implementation. I spoke earlier of the importance of ‘tone at the top’. However, this has to translate into changing the mindset throughout the organisation to secure real understanding, and ownership, of a robust corporate governance culture. The main governance themes and associated audit observations are canvassed below.
**Corporate/Strategic Planning**

I have already made the point that setting the direction of an organisation and monitoring performance are prime elements in any corporate governance framework. These issues have drawn considerable audit comment over the years highlighting the fact that there is significant scope to improve strategic planning and performance measurement so that agencies can demonstrate just how well they are performing against key performance indicators.

As an example, the ANAO’s strategic planning framework comprises a corporate plan, a business plan, operational plans and the Portfolio Budget Statement (PBS) as shown in the following diagram:

**Diagram 1 – ANAO Strategic Planning Framework**

This framework was recently recognized by the Department of Immigration and Multicultural and Indigenous Affairs in its *Access and Equity Annual Report 2001*\(^58\) as providing corporate governance mechanisms and processes that give effect to the principles underpinning the *Charter of Public Service in a Culturally Diverse Society*.\(^59\)

The following extracts from audit reports give a flavor of the main points to consider when developing a strategic planning framework. The extracts are illustrative only. They are not meant to single out any particular agency for comment but to identify recurring themes.

- *past* Corporate Plans have not clearly informed stakeholders of the corporate objectives, priorities, strategies, policies, expected results (including targets), contained actual measures of corporate performance (including quantitative targets), nor generally set higher levels of performance for the Corporation. The new Corporate Plan 2001–04 represents a significant improvement on the previous Corporate Plan. The changes, when fully implemented, have the potential to produce real improvement in the governance and performance.\(^60\)
The broad congruence between management operations and the planning framework of the new Corporate Plan should facilitate greater transparency in the internal administration of the ..., and in turn allow for the Corporation to be able to provide Parliament with a full account of its performance.  

there is a strong management requirement to ensure that appropriate performance standards are built into the planning system.  

the effectiveness of the ... performance information framework in addressing its statutory objectives is affected by limitations in the linkages between performance measures and statutory objectives... is currently unable to demonstrate that it is fully meeting all of its statutory objectives.  

in the Corporate Plan, there are limitations in the links between the statutory objectives and corporate objectives, and the extent to which the ensuing strategies can be seen to be giving effect to the statutory objectives.  

the corporate plan does not clearly communicate the necessary link between ... performance and the provision of quality client service. From a customer service perspective, the corporate objectives do not set a strategic focus for managers and employees that links the overall performance of the business directly to meeting the needs and expectations of the clients.  

there is evidence of different work cultures associated with different functions, suggesting the need to strengthen the strategic linkages between ...organisational units to ensure ... operates as a single coherent and consistent organisation.  

linkages between the ... corporate objectives and its statutory responsibilities are not sufficiently clear for effective management.  ... needs to ensure that as part of its corporate planning framework, the corporate objectives are carried through into operational action and are supported by an effective performance information framework.  

Effective corporate governance is supported by alignment of planning at different organisational and program levels to ensure that strategies and operations give effect to the outcomes and outputs required.  

Performance Information/Measurement

Another important common theme running through ANAO audits is that performance measurement and reporting are intrinsic to the whole process of public management, including planning, implementing, monitoring, evaluation and public accountability. Performance results included in agency annual reports provide an important record of an agency’s progress towards meeting its objectives. Publication of those results makes it possible for stakeholders to exert pressure for improvement, where this is required.

Well presented and informative reports can help Parliament and the public assess how effectively public money is being spent and what is being achieved with it. Such reports are therefore essential for stakeholder assurance. Again, I point to our just released Better Practice Guide – Performance Information in Portfolio Budget Statements - as an authoritative guide. The Joint Committee of Public Accounts and Audit (JCPAA) is also currently undertaking a related review entitled Review of the Accrual Budget Documentation.

Most agencies have developed some form of balanced scorecard to assess their own performance in terms of both the financial and non-financial indicators for key result
areas. Most executive reporting systems, however, still have scope for considerable improvement when it comes to producing integrated management information. Given the level of change resulting from the various public sector reforms and organisational restructuring, this is hardly surprising. At the same time, the criticality of quality information for decision-making means that systems integration and focussed management information for people at all levels must be on the priority list for most agencies.

Without credible performance information, there is no baseline to assess performance and measure/assess improvements in effectiveness. In my view, a practical approach to the difficult task of credibly assessing performance has been provided by the notion, and use, of intermediate outcomes. The latter have certainly assisted in articulating better the relationship over time between agency outputs and ministerially required outcomes.

The ANAO and Finance have provided a checklist for agencies to consider when developing and implementing their performance information framework which has been updated by Finance to accord with the Accrual-based Outcomes and Outputs Framework. In essence, performance indicators should be:

- measurable (or, at least, assessable);
- able to support decision-making;
- balanced, that is, appropriately cover all outcomes and outputs;
- reported with sufficient explanation and comparison (including targets, benchmarks and trends over time) to enable actual performance to be assessed;
- reliable, that is, stable over time to allow for comparisons;
- valid; and
- cost-effective to collect, store and manage.

The following extracts from audit reports emphasise these criteria and stress the importance of the alignment of objectives and measures.

- there are significant gaps and the data could be used more strategically. ..work is required to collect and integrate valid and reliable performance information, including financial information, that is aligned with the new Corporate Plan.
- there is still scope ... to better integrate its internal performance measuring, targeting and reporting framework with its financial management system.
- the Board’s capacity to monitor and evaluate the performance of the Corporation has been inhibited by a lack of such a consistent [strategic planning, operational management, and financial and performance reporting] framework.
- There is also scope to improve performance reporting to the Board, and to comply more fully with requirements for reporting on performance of outcomes against objectives in its annual report. ..should adopt a more structured and strategic approach to evaluating its key programs and activities.
- Strengthening of performance management arrangements would help ensure that management, staff and clients are focused on the requirement to deliver prompt and responsive services.
in most cases, export development and promotion activities could not be identified from statements of agency outcomes and outputs. ... for some agencies, performance indicators at the Portfolio Budget Statement level necessarily reflected the core business of those agencies rather than lower priority export activities. In other agencies, the ANAO found that the performance indicators were more a restatement of the export activity.  

Many performance indicators were not aligned with relevant objectives, and were not always measurable.  

There is generally scope for statutory bodies to improve the usefulness of their annual reports by reporting against a selected range of key performance indicators, and outlining performance in terms of achievement of statutory objectives, principal outputs and contribution to outcomes both intermediate and/or final. This will allow the Parliament and other key stakeholders to make more informed judgements on performance.  

the Department does not yet have a comprehensive and transparent performance information framework for its settlement services. ... the plans provide little performance information aligned to assess the contribution of each level of administration to the achievement of subprogram objectives.  

Administrative reporting that is undertaken tends to be narrowly focussed, not addressing a full range of relevant measures, and with little progress reporting against targets, plans and standards. ... A more structured approach to performance information and progress reporting, incorporating a balanced range of measures and timely reporting against plans, targets and standards would enable all program areas ... to receive necessary feedback on their performance for review purposes. Such action would contribute greatly to efficient and effective achievement of outputs and planned outcomes, as well as provide improved external accountability. 

There is very little information available on outcomes, which is a consistent theme in this report.  

... should review its monitoring arrangements to ensure that they are effective, and consider a risk managed approach to help address some of the workload pressures and to provide greater assurance on achievement of objectives.  

The internal reports ... for review of grant results were largely output focussed, did not include information against targets or standards, or address servicing of priority groups and provided little information on outcomes in relation to the grants program.  

... has an extensive system of performance information. However, the management information systems providing this performance information are not fully integrated. Arrangements for consolidating performance information across the ... and reporting it in a focused manner to the Board on a periodic basis and in the Annual Report could be developed further to improve its usefulness and contribute to better decision-making. 

it was not clear how the performance indicators identified in the report were to be measured or assessed, nor whether targets, standards or benchmarks had been identified, and if so, what they were. Performance reporting had incomplete coverage of the identified performance indicators and generally tended to be more activity-based than output-based.  

targets and benchmarks were not adequately developed to enable performance to be assessed. ... the Commission was collecting data which did not directly support the measurement of its objectives. The value (cost/benefit) of collecting such data for management purposes and/or accountability arrangements is questionable and should be reviewed. Experience suggests that more focused assessments provide more benefit to decision-makers. 

Risk Management 

The risk management theme runs through many of our audit reports highlighting the need for:
a strategic direction in setting the risk management focus and practices;

transparency in the process; and

effective management information systems.

For a number of years, the ANAO has encouraged the embedding of a culture of risk management in agencies and other Commonwealth organisations, so that consideration of risks, and risk mitigation strategies, literally becomes second nature to managers. As a result, managing organisational risks should be accepted as an essential element of sound corporate governance. With the increasing use of different service delivery arrangements; greater involvement of the private sector in the provision of public services; and with a more contestable/competitive market-oriented environment, risk management can only become more critical to successful governance.

While taking note of parliamentary perceptions and concerns about unwarranted exercise of management discretion and possible loss of public resources, public service decision-makers need to be able to demonstrate that a strategic, as well as systematic, enterprise-wide approach is being taken that should alleviate such concerns. A corporate governance framework that strikes an appropriate balance between conformance and performance would provide such assurance. In that respect, it is also necessary for managers to regard risk as an opportunity, not just something to be eliminated or minimised. Nevertheless, the risks have to be well managed in order to ensure that better performance is likely to generate greater benefits than costs.

To be effective, the risk management process needs to be rigorous and systematic. The Australian Customs Service (ACS) and the Australian Taxation Office (ATO) were early implementers of such an approach. The ATO was among the first APS agencies to introduce formal risk management principles to its strategic planning framework. The ACS Executive gave risk management a high corporate priority, the organisation had refined its risk management processes and developed a good infrastructure to support corporate risk management. Some further audit observations reflect the imperatives:

- Contingency planning should be based on a systematic risk assessment, updated regularly, and more focused on the protection of Australian travellers and residents overseas.

- .. risk management has not yet been applied in a sufficiently comprehensive and integrated manner to the management of ... operations to produce more cost effective outcomes. The use of risk management principles needs to develop from the ... corporate and strategic planning and link directly into its operations. The results of the ... risk management planning also need to be reflected in resource allocation decisions.

- most agencies surveyed have undertaken some identification and analysis of...risks but few agencies have done so as part of an overarching corporate risk management plan.

- as a representative .. and facilitator, could have drawn to the attention of the Team the benefits of a more systematic and structured approach to these issues. Such an approach would ensure the early identification of strategies to counter the risks associated with slippages in timetable and
cost over-runs, and provide greater assurance regarding the achievement of effective implementation of the objectives. 93

- reflects the importance of risk identification and treatment as an integral part of management at all levels of an organisation. 96

The above observations indicate the need for managers to be proactive, rather than reactive, to risk. In the more commercial environment being experienced in the APS, managers also have to better understand notions of insurable and non-insurable risk, with the latter generally constituting around 70 per cent of all risks.

**Board Issues**

Any discussion of corporate governance within the private sector and, indeed, for public authorities and companies, usually begins with a discussion of the role of the Board of Directors, which has a central role to play in corporate governance. This was clearly indicated by Sir Ronald Hampel’s Committee on Corporate Governance, which has been extensively quoted in governance literature, namely that:

‘It is the Board’s responsibility to ensure good governance and to account to shareholders for their record in this regard.’ 97

Differences between the public and private sectors are reflected, for example, quite markedly between (a) those agencies that are governed by the CEO, possibly with the assistance of a board of management in an advisory capacity; and (b) those organisations that have a governing board to which the CEO should preferably be accountable, such as government business enterprises (GBEs) and companies. While the latter have more in common with the private sector, they also have added complexities as a result of the additional party in the accountability chain, that is, their responsible Minister. In both sectors, the board’s relationship with management is critical to healthy governance.

Amongst the top responsibilities of boards, whether advisory or GBE type boards, the following three would be in any ‘top five’ identified:

- setting corporate strategy, as well as mission;
- control, supervision and monitoring of top management; and
- reviewing and approving the use of resources.

A number of audit reports have highlighted areas where a board’s performance could be improved. Some examples are as follows:

- The Board’s capacity to monitor and evaluate the performance of the Corporation, in particular as to how well it is meeting its Charter obligations, could be improved. 98

- There is also scope to improve performance reporting to the Board, and to comply more fully with requirements for reporting on performance of outcomes against objectives in its annual report. ..should adopt a more structured and strategic approach to evaluating its key programs and activities. 99
There is a risk that the Board is unable to demonstrate satisfactorily that it is fulfilling its statutory responsibilities. A number of areas in which the Board could improve its operations and practices in order to be able to demonstrate that it is fulfilling these responsibilities. These areas include improving measurement, monitoring and reporting on the Commission’s performance against its objectives; management of delegations; the Board’s strategic role in determining policy and recording of Board activities and decisions. To assist the Board in addressing these issues, the ANAO, in consultation with legal/corporate expert advisers, has developed a suggested checklist on aspects of the operations of the Board and corporate governance generally.

The ANAO expected that, as part of its control system, the Board would be briefed regularly on KPIs to inform the Board on how well the Commission is performing against its objectives, targets and strategies contained in or derived from its Strategic and Annual Operational Plans. Such information has not been provided on a regular basis. The Board should be provided with key performance information on a regular basis to contribute to greater accountability and assurance of outcomes.

A number of senior executives are new to the public sector. As a consequence, there is scope for a better appreciation of specific features of the Commonwealth’s accountability framework. Their understanding of their responsibilities appears to be focused on their relationship with the Managing Director. They see the Managing Director, and of course the Board itself, as having exclusive responsibility for the public accountability aspects of their work and do not perceive any major role for themselves in this framework outside their line responsibilities to the Managing Director. This would appear to be an insufficient base for the achievement of corporate governance standards suggested by ... publicly funded status. There is scope for senior staff to obtain a fuller understanding of the Board’s statutory obligations which they must support, and to better understand the relationship between the .., as a publicly funded [corporation], and the Commonwealth’s accountability framework.

The Control Environment

I noted earlier that an important element of corporate governance is an organisation’s control structure: the key components of which comprise its overall control environment, its risk assessment and risk management processes, its information and communication arrangements, and its internal control measures, including monitoring and review arrangements. By its nature, control is perceived to be more about conformance (assurance) than performance (results).

The control structure should be tailored to each organisation’s specific situation. However, typically, it will be reflected in measures such as an organisation’s structure, its systems for processing and authorisation, its risk management and fraud control strategies, staff training plans, management review and oversight arrangements, and the role of the executive and key business committees, such as the audit committee.

An effective internal control structure is vital for the confidence of all stakeholders, particularly when the organisation’s risk profile is changing. The various public sector reforms have impacted directly on entities’ internal control structures, including business and accounting processes and financial systems. These ‘house-keeping’ matters can be overlooked, with the considerable emphasis being given to outputs and outcomes as part of the reform agenda. ANAO Audit Reports No.52 of 1999–2000 and No.23 of 2000–2001 have highlighted implementation and internal control issues where organisational improvements were required.
ANAQ Audit Report No. 51, 2001-2002 pointed up the lack of specific standards, business rules and guidance on project management, with some existing policies not well implemented. A more structured, corporate approach to project management (supported by management processes to support implementation) would provide greater assurance that sound practices are being appropriately applied, and would facilitate the monitoring and review of the quality of project management. The report also commented on the lack of guidance, or policy, on the tracking of project progress. As a result, divisions vary in the means and extent to which timeliness data is collected and analysed for management review.

Some other illustrations from recent audit reports are as follows:

- Program management should ensure that appropriate controls are in place to safeguard assets and account for liabilities and that decisions are made in accordance with legislative and executive financial authority and public sector values and Codes of Conduct.

- Many existing fraud control indicators were not able to be assessed or measured because terms such as quality, timely and effective had not been defined specifically for each indicator. As well, targets and standards had not been included, where necessary, as a basis of comparison and assessment.

- ...there was no audit trail for management purposes. This is an important issue for all agencies as systematic monitoring, and documenting the outcomes of that monitoring, will assist with ensuring appropriate accountability for fraud control. In this way, the Department would have been able to consistently ascertain whether fraud control arrangements were working in practice so that early action could be taken to resolve any problems cost effectively.

- ...all organisations covered by the audit were not adequately protecting the confidentiality of sensitive information in accordance with the Commonwealth’s security classification system, related Government policy and standards, and recognised best practice. ...the more common and serious breakdowns related to risk assessments and planning, allocation of responsibility, IT&T networks, security clearances, staff training and awareness, and monitoring and review activities. ...there was a high risk of unauthorised access to sensitive information within most of the organisations examined. This was particularly so in relation to ...contractors and clients.

- Improved information security requires a higher level of interest and attention from senior management of Commonwealth organisations. ...the audit found there was a need for higher level direction and review of security matters, preferably, where practicable, through an executive management committee.

- ...although penalties are an important enforcement strategy featured in the ...Compliance Model, the ...lacks appropriate control structures to oversight the accountability, consistency and effectiveness of its penalty administration. Currently, ...management is unable to provide assurance to the Commissioner that penalties are being applied consistently and in accordance with the legislation.

- A critical component of an effective control environment is management’s attitude and commitment to the implementation and maintenance of an effective internal control framework. The level of positive support by management strongly influences the design and operation of control policies and procedures. Without an effective control environment, managers will be unable to ensure the adequacy of the GST processing control framework.
Organisations should establish a control environment that clearly sets out GST management and processing responsibilities and promotes sound principles of pro-active management, including continuous improvement and cost-effective processing.  

Control activities refer to that group of specific internal controls that, within an effective control environment, combine to mitigate unacceptable risks to assist the achievement of business objectives. They operate as the organisation’s front line of defence in ensuring the existence of basic controls, such as the segregation of duties, authorisation, completeness, accuracy, timeliness and system security. They should also ensure the adequacy of documentation relating to the treatment of transactions.

Clear Definition of Roles and Responsibilities

As previously canvassed, the importance of identifying and articulating who is responsible for what, to whom, and by when, are essential for sound corporate governance. Two observations from ANAO Audit Report No 50 1997-98 provide some indication of the issue:

- clear definition of roles and responsibilities at the start of the implementation process was particularly important given the complexity of the issues involved and the wide range of tasks which had to be completed ... Such action would strengthen the accountability and effectiveness of the governance arrangements for managing the transition. It would also minimise risk exposure and the possibility of duplication and waste, as well as unnecessary frustration on the one hand and insufficient oversight and control on the other, thereby assisting with the effective and efficient implementation of reforms.

- While terms of reference were provided ... they do not clearly spell out the Team’s role and reporting responsibilities or specify the collective responsibility and accountability for decisions and required action, other than a requirement to represent the interests of industry and Government. This lessens the effectiveness of the accountability framework for the operations of the body.

A more recent observation is as follows:

- Two organisations, however, had either not clearly assigned responsibility and accountability for GST or had assigned responsibility to an individual at an inappropriate level within the organisation. Inadequate or inappropriate allocation of responsibility for GST means:
  - formal process level risk assessment may not be initiated;
  - the impact of legislative changes may not be appropriately assessed and acted upon;
  - staff are unclear as to who they should contact for advice on technical GST issues;
  - inappropriate decisions relating to GST technical issues may be implemented;
  - policies and procedures may not be updated on a timely basis; and
  - there is no focus for the continuous improvement of GST processes.

Some organisations had documented responsibilities and task descriptions for both managers and GST processing staff; however, most organisations had not.

V. Concluding Remarks

I want to stress that effective corporate governance is more than just putting in place structures, such as committees and reporting mechanisms, to achieve desired results. Such structures are only a means for developing a more credible corporate
governance framework and are not ends in themselves. That is, there must be more emphasis on the *substance* rather than the *form* of good corporate governance.

The work that the ANAO has previously done with Australian public service agencies has clearly indicated the contribution that good corporate governance can make to an organisation’s performance and to the confidence and assurance of stakeholders.

A key aspect of corporate governance is to ensure that all participants are aware of, and accept, their roles, responsibilities and accountabilities and that they have a sound understanding and appreciation of the latter’s practical importance in meeting the public interest. The framework is very people oriented involving better communication; a more systematic approach to corporate management; a greater emphasis on corporate and ethical conduct; risk management; skills development; relationship with citizens as clients; and quality service delivery.

The Australian Stock Exchange Listing Rules now require listed public companies to disclose their corporate governance practices in their annual reports.

The importance of this disclosure should not be overstated. However, the mere observance of this rule is insufficient. The organisation’s commitment is also required to ensure good corporate governance practices are implemented or, as I have said elsewhere, applied corporate governance that is both strategic and operational.

Many unlisted companies and GBEs have followed suit and are disclosing their corporate governance practices in their annual reports. Perhaps this could be generally adopted by agencies to demonstrate to major stakeholders, including the general public, that there is a proper system by which their organisations are controlled and directed. Such action would enhance the confidence of all concerned in public sector organisations’ ability to demonstrate both requirements for conformance and compliance and their levels of performance, or achievement of intended results. We need to deal positively with a situation where:

> *it has become commonplace to look disapprovingly on the traditional values of public administration, with their emphasis on control and process.*"}

The particular challenge for the corporate governance framework is to confront effectively the inevitable tensions, where the balance to be achieved is likely to change from time to time, particularly given the various pressures that might be applied by a range of stakeholders. That is the nature of the political environment in which we work.

The private and public sectors are different. While corporate governance applies primarily to the business sector with its Boards of Directors, the concepts, approaches and techniques have important application to the public sector. However, the latter is complicated by the complexity of relationships, particularly with Ministers and the Parliament, requirements for accountability, notably openness, and the range of performance information that constitute its results, or bottom line.

While the growing convergence of both sectors has made many elements of governance more common, or less different, that convergence, through outsourcing
and greater collaboration and partnerships, has also contributed to greater complexity of the corporate relationships. Nevertheless, in my view, the clarity and discipline involved in the corporate governance framework help us to focus more clearly on what we have to do, who is responsible, and accountable, for what, and who are our stakeholders. That has to result in better public administration, which should be our common aim, and which makes corporate governance more than a management fad.
NOTES AND REFERENCES


12. Ibid, pp.9 and 10.


15. Awty, Adam, 2002. *A Check on Risky Business*, The Public Sector Informant, Supplement to the Canberra Times, April, p. 11

16. Department of Finance and Administration, 1999, ‘Submission to the JCPAA Inquiry into Corporate Governance and Accountability Arrangements for Commonwealth GBES’.


22 McIntosh, Ian 2001 ‘*Top Five Tips for Directors*’, Company Director, August.

23 This is a requirement for Commonwealth bodies under both the *Financial Management and Accountability Act 1997* (Section 46) and the *Commonwealth Authorities and Companies Act 1997* (Section 32).


26 Ibid, p. 30-31


33 For a coverage of this issue refer to the *Corporate Governance Update*, March 2002Published by Ernst & Young available on [www.ey.com/au](http://www.ey.com/au)

34 Ibid. p.2


38 The new audit standard is available on the GAO’s web site at [http://www.gao.gov/govaud/ybk01.htm](http://www.gao.gov/govaud/ybk01.htm)

The Ramsay Report’s recommendations included:

- mandatory disclosure of non-audit services and the fees paid for those services;
- amending the ASX Listing Rules to require that all listed companies have an audit committee;
- strengthening the role of audit committees;
- requiring that at least one member of the audit committee should have accounting and or finance expertise;
- the establishment of an Auditor Independence Supervisory Board to monitor, amongst other things, the adequacy of disclosure of non-audit services; and
- the mandatory rotation of audit partners.

CPA Australia has published a proposal - Financial Reporting Framework – The Way Forward, April 2002, in which the discussion on auditor independence makes the point that any reforms must go beyond audit considerations.


Ibid. pp.44-46
The terms of reference require the Committee to:
- inquire into the effectiveness of, and options for enhancing the format and content of, the current budget documentation including Portfolio Budget Statements, Annual Reports, and the Portfolio Additional Estimates, for the purposes of Parliamentary scrutiny. More information can be found on: http://www.aph.gov.au/house/committee/jcpaa/accrualbudget.


Ibid. p. 20


Ibid p. 23

Ibid p.23


Ibid, p. 14-15

Ibid, p. 15


Ibid


107 Ibid p. 62


110 Ibid., p. 17


112 Ibid p. 14

113 ANAO Report No. 31, 1999-2000, Administration of Tax Penalties, Canberra, 16 February, p. 11


115 Ibid, p. 35

116 Ibid p. 42


118 Ibid

119 Ibid p. 37

120 Australian Institute of Company Directors, 2001. Company Director Manual, p.283. However, the Australian Stock Exchange (ASX) is under pressure to consider taking a more leading role in enforcing corporate governance standards, particularly given the New York Stock Exchange’s (NYSE) recent release of the Recommendations from its Corporate Accountability and Listing Standards Committee which proposed new standards for corporate governance, including a requirement that boards of NYSE listed companies have a majority of independent directors, and greater disclosure practices. See NYSE Corporate Accountability and Listing Standards Committee, 2002. Report. New York, 6 June, pp.1-30.

121 Ibid. p. 283