

The Auditor-General  
Audit Report No.16 2002-03  
Business Support Process Audit

# **The Administration of Grants (Post-Approval) in Small to Medium Organisations**

Australian National Audit Office

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of Australia 2002

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Canberra ACT  
4 November 2002

Dear Mr President  
Dear Mr Speaker

The Australian National Audit Office has undertaken a business support process audit across agencies 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 this report of this audit, and the accompanying brochure. The report is titled *The Administration of Grants (Post-Approval) in Small to Medium Organisations*.

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 'I. McPhee', written in a cursive style.

Ian McPhee  
Acting Auditor-General

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

## AUDITING FOR AUSTRALIA

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

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## Abbreviations/Glossary

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|                      |  |
|----------------------|--|
| BSP audit            | Business Support Process audit.  |
| ANAO                 | Australian National Audit Office.  |
| APS                  | Australian Public Service.   |
| Acquittal            | Evidence provided by recipients to demonstrate grant funds have been expended in accordance with the terms and conditions of the funding agreement. <sup>1</sup>   |
| CEO                  | Chief Executive Officer.   |
| Conflict of interest | A conflict of interest arises where a person makes a decision or exercises a power in a way that may be, or may be perceived to be, influenced by either material personal interests (financial or non-financial) or material personal associations.   |
| FMIS                 | Financial Management Information System.   |
| Fraud control plan   | A plan devised to protect the revenue, expenditure and property of an organisation from any attempt, either by members of the public, contractors, sub-contractors, organisations, intermediaries or its own employees to gain by deceit financial or other benefits. This policy is designed to protect public money and property, protect the integrity, security and reputation of our public institutions and maintain a high level of services to the community consistent with the good government of the Commonwealth.  |
| Funding agreement    | <p>A legally enforceable agreement setting out the terms and conditions governing funding. These terms and conditions are determined by the funding organisation. The form of the agreement will depend on the intent of the grant and the degree of control required. The forms of enforceable funding agreements include:</p> <ul style="list-style-type: none"><li>• Deed;</li><li>• Contract; and</li><li>• Exchange of letters.</li></ul> <p>In the case of grants to State governments or in networked grant programs, Memorandum of Understanding (MOU), or a combination of MOUs and legally enforceable agreements, may be necessary.<sup>2</sup></p> |

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<sup>1</sup> *Administration of Grants—Better Practice Guide*. ANAO, Canberra, May 2002, p. 1.

<sup>2</sup> *ibid.*, p. 6.

|                            |  |
|----------------------------|--|
| Grant                      | <p>A grant is a sum of money given to organisations or individuals for a specified purpose directed at achieving goals and objectives consistent with government policy.</p> <p>The term is generally used to include any funding arrangement where the recipient is selected on merit against a set of criteria. However, this does not include funding of activities relating primarily to the provision of goods and services directly to a government organisation. Guidance on these arrangements is provided by the Commonwealth Procurement Guidelines.<sup>3</sup></p> |
| GMS                        | Grant Management System.   |
| Grantee                    | Receiver of grant funds.   |
| Grant program              | Set of individual grant projects aimed at achieving particular strategic objectives of the funding organisation.   |
| Grant project              | Activity funded by the Commonwealth and aimed at contributing to the overall objectives of an individual grant program.  |
| GST                        | Goods and Services Tax. GST may apply to grant payments and needs to be determined on a case-by-case basis.  |
| Internal control framework | Policies and procedures adopted by management to assist in achieving the entity's objectives. It comprises the interrelated components of risk assessment, control environment, control activities, information and communication processes, and monitoring and review processes. <sup>4</sup>   |
| Milestone report           | Report provided by recipients detailing performance information on the achievement of program aims and objectives throughout the life, and at the termination, of the project.   |
| Monitoring                 | Process by which the funding organisation establishes whether individual grants are expended in accordance with the terms and conditions of the funding agreement.   |

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<sup>3</sup> Minister for Finance and Administration, *Commonwealth Procurement Guidelines and Best Practice Guidance*. Canberra, 12 February 2002.

<sup>4</sup> *Better Practice Guide to Effective Control, Control Structures in the Commonwealth Public Sector: Controlling Performance and Outcomes*, ANAO, Canberra, 1997.



|                     |   |
|---------------------|---|
| Performance measure | Performance measures are evidence about performance that is collected and used systematically. In some cases, quantified performance measures may not be available and less direct performance indicators have to be used. Performance measurement is best supported by relevant, accurate, timely, accessible, interpretable and coherent performance information. |
| Risk management     | The culture, processes and structures that are directed towards effective management of potential opportunities and adverse effects. <sup>5</sup> In other words, it is the systematic application of management policies, procedures and practices to the tasks of identifying, analysing, assessing, treating and monitoring risk.                                |

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<sup>5</sup> Standards Australia *Guidelines for managing risk in the Australian and New Zealand Public Sector* (HB143:1999), Standards Association of Australia, Sydney 1999.



# **Summary and Recommendations**



# Summary

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## Background

1. A grant is described as ‘...a sum of money given to organisations or individuals for a specified purpose directed at achieving goals and objectives consistent with government policy. The term is generally used to include any funding arrangement where the recipient is selected on merit against a set of criteria’.<sup>6</sup>
2. For the purposes of this audit, a grant is defined as a payment of money on conditions specified by the funding organisation. It includes arrangements whereby funds are provided as a means to support particular activities such as research and development, art and sport. However, the term ‘grant’ does not include funding of activities primarily relating to the provision of goods and services directly to a government organisation.<sup>7</sup>
3. The administration of grants is a significant feature of public sector administration. Grants require a sound risk management approach as grant money is commonly provided to individuals and community organisations not directly accountable to the Government. In small to medium organisations, grants can represent a significant proportion of their total expenditure.
4. For the year ended 30 June 2001, direct Commonwealth expenditure on grants amounted to approximately \$3 billion.<sup>8</sup>

## Audit objectives and coverage

5. The objectives of the audit were to:
  - assess whether small to medium organisations have implemented appropriate risk management strategies for grant programs;
  - assess whether grants have been administered in accordance with the appropriate legislation, Commonwealth guidance, and other applicable internal controls; and
  - recommend improvements in the controls and practices relating to the administration of grants, as necessary.

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<sup>6</sup> op. cit., *Administration of Grants—Better Practice Guide*.

<sup>7</sup> Guidance on these arrangements is provided by the Minister for Finance and Administration. *Commonwealth Procurement Guidelines and Best Practice Guidance*, Canberra, 12 February 2002.

<sup>8</sup> This amount has been sourced from the Commonwealth Government Consolidated Financial Statements for the year ended 30 June 2001. As at the date of this report, figures for the year ended 30 June 2002 were unavailable.

6. The audit focused on the administration of grants from the time that the grant is approved. The selection process for awarding grants was not included within the audit scope.
7. The audit was conducted in six Commonwealth organisations, namely:
  - Australia Council;
  - Australian Greenhouse Office;
  - Australian Sports Commission;
  - Australian Centre for International Agricultural Research;
  - Land and Water Australia; and
  - Rural Industries Research and Development Corporation.

## Audit conclusion

8. The ANAO concluded that the organisations audited had implemented appropriate risk management strategies for grant programs. However, the ANAO also concluded that some audited organisations had not conducted an assessment of the risks associated with the day-to-day administration of individual grants.
9. The organisations were generally administering grants in accordance with applicable legislation, government policy and internal controls. Nevertheless, there were generally opportunities for these organisations to enhance their performance in this significant area of operations by adopting the sound and better practices highlighted in this report.

## Audit findings

### Risk assessment

10. All audited organisations had completed organisational-level risk assessments. However, one organisation had not reviewed and updated its assessment on a regular and timely basis. In addition, some audited organisations had not reviewed and updated their fraud risk assessments and fraud control plans.
11. Further, some of the organisations had not assessed the risks associated with the process of administering grants. The other audited organisations' risk assessments could be improved by considering possible causes and scenarios of risks so that effective controls can be put in place.

## Control environment<sup>9</sup>

12. All but one of the organisations audited had comprehensive funding agreements, developed in consultation with legal advisers, which met terms and conditions considered to be better practice. All organisations had developed standardised funding agreement general terms and conditions in the form of templates. Special funding agreements were developed where necessary.

13. Organisations would benefit from enhancing formal training provided to new and less experienced staff involved in the administration of grants so that policies and procedures are understood, and staff are fully aware of their individual responsibilities.

14. The ANAO found that the audited organisations had provided guidance on conflict of interest issues to employees at the start of their employment. However, greater consideration could be given to developing and implementing a policy to capture individual board and staff members' changes in circumstances, which may give rise to potential conflicts of interest.

15. Given limitations in their Grants Management System (GMS), some organisations had developed alternative methods for recording and reporting of information. This resulted in inefficiencies, such as the duplication of data entry.

## Control activities

16. The ANAO found that audited organisations could improve their mechanisms to administer grants by:

- progressively monitoring project actual expenditure against budgets, at the category/expenditure level;
- linking interim financial acquittals to milestone payments;
- establishing timely, consistent and transparent methods of follow-up of recipient provided information within organisations;
- considering the documentation needs of all stakeholders; and
- performing, reviewing and appropriately documenting reconciliations.

## Information and communication

17. The ANAO found that some of the organisations' operational and financial reporting was inadequate because there was no analysis of information in the

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<sup>9</sup> The control environment relating to grants administration was examined under four main elements: process; people; structure; and technology.

reports. Improved analysis would assist users to obtain a better understanding of financial and performance data, which in turn, would inform decision-making.

## **Monitoring and review**

18. Whilst all audited organisations were undertaking some form of monitoring and review activities of the administration of grants, only some organisations had developed mechanisms to report the results of these activities regularly.

19. The organisations would benefit if they had formal arrangements in place that allowed for managers at all levels to assess whether the administration of grants, for which they are responsible, is being conducted efficiently and effectively.

## **Sound and better practices**

20. In conducting the audit, the ANAO observed examples of sound and better practices for the day-to-day administration of grants to compliment those detailed in the Better Practice Guide<sup>10</sup>. A summary of the sound and better practices is provided in Table 1.

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<sup>10</sup> *op. cit.*, *Administration of Grants—Better Practice Guide*.



**Table 1****Sound and better practices observed in the administration of grants.**

| <b>Control framework component</b>   | <b>Sound and better practices</b>   |
|--------------------------------------|---|
| <b>Risk assessment</b>               | <ul style="list-style-type: none"> <li>• A risk register was developed which summarised risks identified through the risk assessment process as well as recommended and required action to mitigate individual risks at both an organisational and process level.</li> </ul>  |
| <b>Control environment</b>           | <ul style="list-style-type: none"> <li>• Policies, procedures and templates were distributed to staff via the Intranet/network server and other electronic means such as e-mail, which provided a single reference source so that consistent and up to date information could be accessed.</li> <li>• A 'Master Document Status List' was maintained to record all current documents utilised.</li> <li>• Induction, formal and one-off training programs had been used effectively.</li> <li>• Job description documentation was in place to identify tasks and responsibilities.</li> <li>• Program areas were provided with ready access to the financial experience and knowledge of staff within the finance branch to assist with the review of financial acquittals.</li> <li>• GMSs were interfaced with the Financial Management Information System (FMIS).</li> <li>• An integrated system was utilised comprising of a record keeping system; a GMS; a workflow system; and an FMIS.</li> <li>• Some activities of the administration of grants were automated.</li> <li>• Most organisations' GMSs had different levels of access for staff.</li> </ul> |
| <b>Control activities</b>            | <ul style="list-style-type: none"> <li>• Standard templates were used for the assessment of milestone reports and acquittals; guidelines and templates were provided to recipients to assist in the preparation of required information; and funding was withheld until such time as required milestones were met.</li> <li>• Interim acquittals were attached to milestones and hence grant payments. This ensured recipients were meeting the terms and conditions of their funding agreement prior to further payments being released.</li> </ul>  |
| <b>Information and communication</b> | <ul style="list-style-type: none"> <li>• Communication plans/strategies had been implemented, and were comprehensive.</li> <li>• Section heads were provided with access to real-time financial data.</li> </ul>  |
| <b>Monitoring and review</b>         | <ul style="list-style-type: none"> <li>• Quality assurance reviews were undertaken and provided some assurance to management in relation to the administration of grants.</li> </ul>  |

# Recommendations

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The recommendations set out below are based on the findings made in the organisations reviewed but *may* have relevance to other Commonwealth organisations.

## Risk assessment

**Recommendation  
No. 1  
Para 2.17**

The ANAO *recommends* that organisations regularly undertake a process-level risk assessment of the grants administration function to define the full range of risks, related controls and treatment plans.

## Control environment

**Recommendation  
No. 2  
Para. 3.20**

The ANAO *recommends* that organisations:

- maintain policy and procedural documents in a manner that allows them to be easily identified, accessed and updated;
- consider including items identified as better practice in the ANAO Better Practice Guide<sup>11</sup> in their policies and procedures for the administration of grants; and
- as appropriate, review the status of funding agreements to ensure clearly defined terms and conditions have been established and are enforceable in the event of non-compliance by the recipient.

**Recommendation  
No. 3  
Para. 3.29**

The ANAO *recommends* that organisations conduct both initial and refresher training programs to ensure that all staff appointed to the administration of grants are fully aware of, and understand, relevant policies, procedures and individual responsibilities.

**Recommendation  
No. 4  
Para. 3.50**

The ANAO *recommends* that organisations:

- as appropriate, conduct a cost-benefit analysis of improving the functionality of their Grants Management Systems to make administration of grants more efficient; and
- ensure that appropriate general and application IT controls are in place to provide adequate security for their systems and recorded data.

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<sup>11</sup> *ibid.*

## Control activities

### Recommendation No. 5 Para. 4.20

The ANAO *recommends* that organisations:

- link the provision of financial acquittals to project milestones to ensure adequate and timely information is available to allow for projects to be monitored progressively; and
- assess the adequacy of existing systems and procedures for satisfying recordkeeping requirements.

## Information and communication

### Recommendation No. 6 Para. 5.16

The ANAO *recommends* that organisations provide users with appropriate analysis of the financial and performance results of grant programs and individual grant projects to help them better understand and make use of financial and performance reports.

## Monitoring and review

### Recommendation No. 7 Para. 6.18

The ANAO *recommends* that organisations enhance mechanisms to assist in monitoring and reviewing the administration of grants through the use of appropriate performance indicators.

## Responses to the recommendations by organisations included in the audit

21. A similar grouping of recommendations was made in a detailed report to each of the organisations covered by the audit. The recommendations varied according to the adequacy of the individual control framework operating within the organisation. Organisations agreed with the recommendations and a number indicated that remedial action had been undertaken before the audit was completed.



# **Audit Findings and Conclusions**



# 1. Introduction

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## Background

1.1 A grant is described as ‘...a sum of money given to organisations or individuals for a specified purpose directed at achieving goals and objectives consistent with government policy. The term is generally used to include any funding arrangement where the recipient is selected on merit against a set of criteria’.<sup>12</sup>

1.2 For the purposes of this audit, a grant is defined as a payment of money on conditions specified by the funding organisation. It includes arrangements whereby funds are provided as a means to support particular activities such as research and development, art and sport. However, the term ‘grant’ does not include funding of activities primarily relating to the provision of goods and services directly to a government organisation.<sup>13</sup>

1.3 ‘The power to give a grant may be unfettered (such as the Commonwealth’s power to grant financial assistance to the States under section 96 of the Commonwealth Constitution) or it may be governed by specific legislation or government policy applying to the program’.<sup>14</sup>

1.4 The administration of grants is a significant feature of public sector administration. Grants require a sound risk management approach as grant money is commonly provided to individuals and community organisations not directly accountable to the Government. In small to medium organisations, grants can represent a significant proportion of their total expenditure.

1.5 For the year ended 30 June 2001, direct Commonwealth expenditure on grants amounted to approximately \$3 billion.<sup>15</sup>

## Audit objectives, coverage and scope

1.6 The objectives of the audit were to:

- assess whether small to medium organisations have implemented appropriate risk management strategies for grant programs;

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<sup>12</sup> op. cit., *Administration of Grants—Better Practice Guide*, p. 1.

<sup>13</sup> ibid.

<sup>14</sup> ibid.

<sup>15</sup> This amount has been sourced from the Commonwealth Government Consolidated Financial Statements for the year ended 30 June 2001. As at the date of this report, figures for the year ended 30 June 2002 were unavailable.

- assess whether grants have been administered in accordance with the appropriate legislation, Commonwealth guidance, and other applicable internal controls; and
- recommend improvements in the controls and practices relating to the administration of grants, as necessary.

1.7 The audit focused on the administration of grants from the time that the grant is approved. The selection process for awarding grants was not included within the audit scope.

1.8 The audit was undertaken in six Commonwealth organisations. Overall, the six organisations spent \$286.3 million on grant funding, or on average, 68.4 per cent of their total expenditure in 2001–2002. Table 2 lists the organisations audited, and shows their expenditure on grant funding, both in dollar terms and as a percentage of total expenditure. For most of these organisations, the administration of grants is their core business.

1.9 Some of the organisations audited are subject to the *Financial Management and Accountability Act 1997* (FMA Act) while others are subject to the *Commonwealth Authorities and Companies Act 1997* (CAC Act).

**Table 2**

**Audited organisations grant funding expenditure**

| Organisation  | Grant funding expenditure<br>2001–2002 |                        |
|---|--|------------------------|
|   | \$m                                    | % of total expenditure |
| Australia Council   | 118.0                                  | 89.8                   |
| Australian Centre for International Agricultural Research | 34.8                                   | 72.6                   |
| Australian Greenhouse Office                              | 38.9                                   | 48.0                   |
| Australian Sports Commission                              | 59.2                                   | 46.6                   |
| Land and Water Australia                                  | 16.7                                   | 70.0                   |
| Rural Industries Research and Development Corporation     | 18.7                                   | 83.1                   |

Source: Organisations' audited financial statements for year ended 30 June 2002.



## Audit evaluation criteria

**1.10** This audit is one in a series of Business Support Process (BSP) audits looking at business and financial processes in the Commonwealth. The criteria for these audits have been based on the internal control framework detailed in the ANAO's Better Practice Guide<sup>16</sup> and consist of:

- risk assessment;
- control environment;
- control activities;
- information and communication; and
- monitoring and review.

**1.11** The internal control framework can be described as follows:

The control environment is the foundation for the effectiveness of all the other components. It reflects management's commitment and attitude to establishing an effective control structure. It is sometimes referred to as the 'tone at the top' and is dependent on firm leadership and clarity of direction from the governing body.

Risk assessment and control activities include identification, analysis and assessment of risks to achieving objectives and the design of control policies and procedures to manage those risks, focussing on those that have potential for more significant exposures and are critical to the business.

Regular and relevant information needs to be collected and communicated to enable performance to be monitored and reviewed. The effectiveness of the control structure also requires on-going monitoring and review.<sup>17</sup>

### Detailed criteria

**1.12** The above audit criteria have been adapted and expanded to take account of the diverse risks and operations of the administration of grants. Development of the criteria also considered better practice in the administration of grants.

**1.13** Table 3 shows the audit evaluation criteria mapped against the components of the internal control framework, against which each organisation's administration of grants was assessed.

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<sup>16</sup> op. cit., *Better Practice Guide to Effective Control, Control Structures in the Commonwealth Public Sector: Controlling Performance and Outcomes*.

<sup>17</sup> ibid.

**Table 3****Audit evaluation criteria**

| <b>Risk Assessment</b>   |   |
|--|---|
| Each organisation would be expected to have completed a risk assessment that included consideration of the administration of grants. The assessment would be expected to have covered the risk of grant programs not achieving expected outcomes, inappropriate accounting for grant monies and the effectiveness of existing controls. Each organisation's fraud control plan would also be expected to have considered the risk of misappropriation of grant funding.  |   |
| <b>Control Environment</b>   |   |
| <b>Process</b>   | Each organisation would be expected to have in place, effective and efficient policies and procedures that reflect the organisation's governance responsibilities.  |
| <b>People</b>  | Senior management is expected to take a pro-active approach to risk and control, ensuring key personnel are aware of governance responsibilities, through training and communication.                             |
| <b>Structure</b>   | Organisations would be expected to have structured the administration of grants in a way that efficiently meets the business needs of the organisation, allowing for clear responsibilities and accountabilities. |
| <b>Technology</b>  | Organisations would be expected to have implemented information systems as a strategic resource and have appropriate general IT controls in place.  |
| <b>Control Activities</b>  |   |
| Each organisation would be expected to have specific controls to ensure validity, completeness, and accuracy of grant funding transactions, including the appropriate general and application IT controls. These controls would cover all elements of the process including planning, acquittals, compliance with grant conditions, monitoring and internal and external reporting.  |   |
| <b>Information and Communication</b>   |   |
| Each organisation would be expected to have in place systems to capture and report grants administration information. It would also be expected that close links have been developed between the general ledger and the GMS to enable good decision making in relation to grant monies. Each organisation would also be expected to have regular two-way information flows between the staff working on the function, and management.  |   |
| <b>Monitoring and Review</b>   |   |
| Each organisation would be expected to have regular monitoring and review processes in place to ensure that policies and procedures are adhered to and properly applied, and to identify changes and weaknesses in the operating environment. This might be achieved by reporting against performance measures through internal checking and auditing processes. The results of this process then need to be input into the next round of strategic planning and risk assessment performed by each organisation. |   |

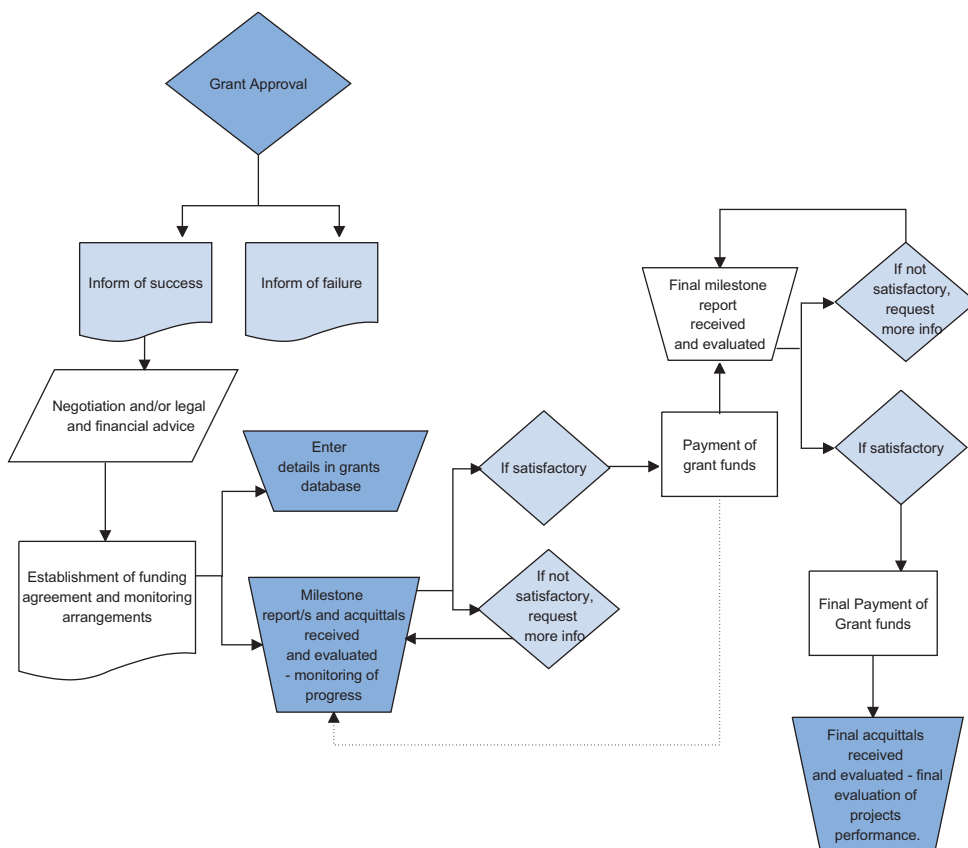
## The administration of grants

1.14 The administration of grants, from the time that the grant is approved, is the set of activities comprising of the following:

- establishment of funding agreements;
- establishment of monitoring arrangements;
- monitoring of progress including review and evaluation of milestone reports and acquittals;
- acquittal of funds;
- payment of funds; and
- evaluation of the grant project.

1.15 These activities are graphically represented at Figure 1 below.

**Figure 1**  
The administration of grants flowchart



Source: Developed by the ANAO.

## Previous audit coverage

**1.16** In 1996–97, the ANAO conducted a performance audit of the administration of grants in the Australian Public Service.<sup>18</sup> The main objectives of the audit were to examine the efficiency and administrative effectiveness of grant programs and identify any weaknesses and evidence of better practice in both program administration and organisation guidelines. The audit concluded that scope for improvement in the administration of grants existed. Key areas of improvement included planning, monitoring, and reviews of grant programs.

**1.17** As part of the 1996–97 performance audit, the ANAO undertook a revision of the 1994 *Best Practice Guide for the Administration of Grants*, which resulted in a new version being published. This, in turn, was revised and a new better practice guide was published in May 2002 to provide practical guidance to those involved in the planning, project selection, management and review of grant programs.

**1.18** In addition, the Joint Committee of Public Accounts and Audit (JCPAA), in its review of the *Administration of the Federation Fund Program* audit report, encouraged Commonwealth agencies to examine and adopt the ANAO's Better Practice Guide on Grants whenever they have grant management responsibilities.<sup>19</sup>

## Audit methodology

**1.19** The audit methodology involved interviews with selected officers, the examination of files and records supporting the administration of grants, and general observation and inspection.

**1.20** The ANAO provided each organisation reviewed with a report of the audit, which included a number of detailed and specific recommendations relevant to the particular organisation.

**1.21** The audit was undertaken in accordance with ANAO Auditing Standards at an approximate cost of \$308 000.

## Structure of the remainder of the audit report

**1.22** Chapters 2-6 discuss the findings and recommendations of the audit against each component of the internal control framework.

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<sup>18</sup> ANAO Audit Report No.32 1996–97, *Administration of Grants in the Australian Public Service*.

<sup>19</sup> *Report 390, Review of Auditor-General's Reports 2001–2002, First, Second and Third Quarters*, JCPAA, Canberra, August 2002, p. 43.

**1.23** The ANAO's observations are presented in two categories:

- *Audit findings* which detail control weaknesses contributing to a breakdown in both efficiency and effectiveness of the internal control framework; and
- *Sound and better practices* relating to business practices, which, if adopted, would strengthen the internal control framework and lead to improved effectiveness and efficiency of the administration of grants.

## 2. Risk Assessment

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### Introduction

2.1 Risk assessment is the starting point for evaluating the administration of grants control framework, because it provides the basis for designing appropriate and cost-effective controls. A sound risk assessment also ensures that responsibility for managing risks is appropriately allocated to managers who need to understand the risks of grants administration and can be held accountable for their management through the operation of the control framework.

### Organisational and process-level risk assessments

2.2 Risk assessments should be conducted at both the *organisational* and *process* levels to assess whether organisations have properly applied the results of the risk assessment to the design of the control framework and related activity. Risk management activities generally commence with an organisational-level risk assessment that involves formally identifying risks within the context of the breadth of organisational activity. These risks would then be evaluated and sourced to activities or functions.

2.3 While the organisational-level risk assessment provides management with the necessary knowledge and understanding to manage risks, further development of risk assessment activity related specifically to the administration of grants is required to fully understand the control requirements.

2.4 Process-level risk assessments are the basis for subsequent design of all aspects of the control environment, specific control activities, information and communication processes, and monitoring and review procedures. Process-level risk assessments can lead to enhanced control structures, the detection of control weaknesses, prevention of control breakdown and increased operational efficiency.

### Audit findings and comments

2.5 The following table summarises the relevant principle and audit evaluation criteria, which were used to assess an organisation's risk assessments.

**Table 4**  
**Risk assessment**

|                                  |   |
|----------------------------------|---|
| <b>Principle</b>                 | Implementation of an effective risk assessment framework is a central element of grants administration.   |
| <b>Audit evaluation criteria</b> | Each organisation would be expected to have completed a risk assessment that included consideration of the administration of grants. The assessment would be expected to have covered the risk of grant programs not achieving expected outcomes, inappropriate accounting for grant monies and the effectiveness of existing controls. Each organisation's fraud control plan would also be expected to have considered the risk of misappropriation of grant funding. |

### Administration of grants risk assessment

**2.6** Although the administration of grants within the Commonwealth is generally considered as a medium risk process, organisations are exposed to a number of risks warranting consideration, including:

- the effect of partial or insufficient grant funding on the viability of projects;
- grant programs not contributing to the achievement of the strategic objectives of the funding organisation;
- incremental and undocumented changes in interpretation of grant program objectives or guidelines over time;
- actual or perceived conflicts of interest;
- unapproved variations to projects during the grant period; and
- shared accountabilities.<sup>20</sup>

**2.7** Additionally, organisations are exposed to a number of risks in relation to individual grant recipients, including:

- the possibility of 'double-dipping';
- fraud or misrepresentation;
- use of grant funds for purposes contrary to the terms and conditions of the funding arrangement;
- changes in the status/competence of the grant recipients which could adversely affect their ability to carry out or complete relevant project work<sup>21</sup>; and
- underperformance, or non-performance, of grant recipients.

<sup>20</sup> op. cit., *Administration of Grants—Better Practice Guide*, p. 11–12.

<sup>21</sup> *ibid.*

**2.8** Organisations must establish controls to mitigate these potential risks in order to limit their exposure to fraud, financial loss and underperformance, or non-performance, of grant recipients. Clear policies and procedures must be developed for, and regularly disseminated to, staff involved in the administration of grants. In addition, organisations must develop systems to monitor grant recipients to detect accidental misuse or fraud of grant funding and underperformance or non-performance of grant recipients.<sup>22</sup> For example, regular reporting by the recipient is designed to obtain assurance that the project is performing in accordance with the terms and conditions of the grant.

**2.9** Organisations that adopt formal process-level risk assessments have an opportunity to maximise the social and economic benefits of grant programs, whilst reducing the probability and/or consequences of associated risks. This can also assist in streamlining planning, implementation, monitoring and review processes to the extent practicable and necessary.<sup>23</sup>

**2.10** All organisations audited had a pro-active approach to risk assessment activities and had implemented organisational-level risk assessments in which risks pertaining to the administration of grants have been included and assessed. However, some organisations had not undertaken formal process-level risk assessments relating to the administration of grants and/or had not identified all underlying causes of risks so that effective controls can be put in place.

**2.11** Some organisations had developed a risk register which summarised risks identified through the risk assessment, as well as recommended and required action to mitigate individual risks at both an organisational and process level. This assisted in the allocation of responsibility for the establishment and timely monitoring of controls.

**2.12** The ANAO noted that risks and controls identified in one organisation's risk assessment were not reviewed and updated regularly. This organisation planned to conduct a review of the risk assessments.

## **Fraud control plans**

**2.13** Fraud control plans had been implemented in all organisations, with one organisation's fraud control policy incorporated in the organisational-level risk assessment.

**2.14** Some organisations had not reviewed and updated fraud control plans and fraud risk assessments for some time. However, most organisations were in the process of arranging for this to occur.

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<sup>22</sup> *ibid.*

<sup>23</sup> *ibid.*



## Conclusion

**2.15** All audited organisations had completed organisational-level risk assessments. However, one organisation had not reviewed and updated its assessment on a regular and timely basis. In addition, some audited organisations had not reviewed and updated their fraud risk assessments and fraud control plans.

**2.16** Further, some of the organisations had not assessed the risks associated with the process of administering grants. The other audited organisations' risk assessments could be improved by considering possible causes and scenarios of risks so that effective controls can be put in place.

## Recommendation No.1

**2.17** The ANAO recommends that organisations regularly undertake a process-level risk assessment of the grants administration function to define the full range of risks, related controls and treatment plans.

### *Implementing the recommendation*

**2.18** Risk assessments should have regard to the significance and materiality of the grants administration function to the organisation as a whole.

## Sound and better practices noted

**2.19** Some organisations had a risk register, which summarised risks identified through the risk assessment process as well as recommended and required action to mitigate individual risks at both an organisational and process level. This helps to ensure that the responsibility for the establishment and timely monitoring of controls is appropriately allocated.

## 3. Control Environment

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### Introduction

**3.1** A critical element of an effective control environment is management's attitude and commitment to the implementation and maintenance of an effective internal control structure. The level of management support 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 control framework for the administration of grants.

**3.2** Organisations should establish a control environment that clearly sets out the responsibilities relating to the administration of grants and promotes sound management principles, including continuous improvement and cost-effective processing.

**3.3** Comprehensive and up-to-date policies and procedures, on-going training programs to promote staff awareness of their requirements, and keeping information systems up to date with changes in the organisation and its business, are *fundamental* to achieving such an environment.

**3.4** The control environment relating to the administration of grants was examined under the following four main elements:

- *process*—the organisation's policies and procedures should be complete and effectively communicated in order to reflect the organisation's governance responsibilities;
- *people*—the need for high quality and experienced staff to be employed, with their responsibilities and accountability clearly defined, as well as promoting these through effective training and communications programs;
- *structure*—the structure of the function should relate to the organisation's needs, and allow for clear responsibilities, accountabilities and transparency of process; and
- *technology*—the technology used within the function should be established to support all the elements of the established control environment.

**3.5** The audit findings for each of the above elements are detailed below.

## Audit findings and comments

### Control environment (process)

3.6 The following table summarises the relevant principle and audit evaluation criteria, which were used to assess an organisation's control environment (process).

**Table 5**

#### Process

|                                  |  |
|----------------------------------|--|
| <b>Principle</b>                 | Effective policies and procedures provide all relevant personnel with access to a documented framework for the administration of grants.                           |
| <b>Audit evaluation criteria</b> | Each organisation would be expected to have in place, effective and efficient policies and procedures that reflect the organisation's governance responsibilities. |

#### *Policies and Procedures*

3.7 The existence of up-to-date policies and procedures is a key element for developing guidance for the administration of grants and preventing possible control breakdown, should, for example, the organisation experience high staff turnover. These mechanisms include the use of Chief Executive Instructions (CEIs), policies and procedures, as well as guidelines and detailed process descriptions.

3.8 All organisations had formal documented CEIs, policies and procedures, which, in most cases, had been endorsed by senior management. Generally, these policies and procedures were comprehensive, clear and concise, and provided sufficient guidance for staff to perform daily tasks in a controlled and consistent manner. Furthermore, most organisations' procedural documentation contained flowcharts, which helped the users' understanding of processes.

3.9 However, some organisations' policies and procedures required improvement and/or updating. In particular:

- procedures relating to acquittals, monitoring and review and evaluation were not adequately considered;
- local procedures specific to grant programs had not been formally documented;
- ambiguities in responsibility levels and time frames existed; and
- some policies and procedures were contained in separate manuals and were not cross-referenced to other guidance material.

**3.10** These improvements would assist, for example, staff (particularly new members) in understanding and finding all guidance material relevant to grants administration.

**3.11** Most organisations were increasingly utilising Intranet functionality or other technology to communicate policies and procedures, which provided a single reference source where consistent information could be accessed. In addition, some organisations utilised a 'Master Document Status List' to record all documents used by an organisation and allowed staff to identify current documents easily. This is considered to be better practice.

### *Funding Agreements*

**3.12** A fundamental requirement of effective grants administration is the ability of the funding organisation to protect its interests in ensuring public money is used for the intended purpose. An essential component of grants administration is a well-drafted funding agreement that provides for:

- a clear understanding between the parties on required outcomes, prior to commencement of funding;
- accountability for, and protection of, Commonwealth funds;
- legal protection of the recipients and the funding organisation;
- agreed terms and conditions of the funding assistance, including performance information and access requirements and clearly defined roles and responsibilities of all parties; and
- dispute resolution.<sup>24</sup>

**3.13** Furthermore, the terms and conditions of funding agreements should be expressed with sufficient precision so that it can be determined whether the recipient is complying with those terms and conditions, how disputes are to be resolved and include circumstances for:

- release of funds;
- banking arrangements;
- terms and conditions of payments;
- amendments to terms and conditions;
- access to information in order to monitor compliance;
- remedial action where non-compliance occurs (including withholding or reclamation of the grants if necessary);

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<sup>24</sup> *op. cit.*, *Administration of Grants—Better Practice Guide*, p. 6.

- repayment of unspent funds and interest; and
- the recipient to notify any significant changes in the assisted project.<sup>25</sup>

3.14 Comprehensive funding agreements satisfying these requirements had been established, in consultation with legal advisers, by all but one organisation. This organisation is looking to formally address how its funding agreement can be strengthened. All organisations had developed standardised funding agreement general terms and conditions in the form of templates, which applied to most funding arrangements. Special funding agreements were developed, where necessary. Intellectual property, patents and copyright clauses had been incorporated into funding agreements where applicable.

3.15 There are legal risks associated with how grant terms and conditions are formalised in organisations. In particular, the lack of a formal agreement or inadequate terms and conditions may make it difficult for the Commonwealth to enforce specific requirements should a problem or dispute occur with the recipient.

3.16 Whilst there is no form of funding agreement that suits all circumstances, forms of enforceable funding agreements include deeds under seal, contracts and exchange of letters. One way of removing any doubt in relation to whether the resource agreement is legally enforceable is by embodying the agreement in the form of a deed under seal. However, where resource agreements are not contracts, sanctions for failure to acquit the grant in accordance with the terms and conditions of the agreement are limited.

3.17 With respect to funding agreements, the ANAO considered the ability to protect the Commonwealth's interest could be improved by the use of an appropriate form of funding agreement that enables the enforcement of the relevant grant conditions.

3.18 Some organisations view their role as more of a provider of assistance to recipients rather than as a body that ensures compliance against funding agreements. Notwithstanding this, organisations should consider removing any doubt as to whether agreements are legally enforceable and strengthen funding agreements in relation to terms and conditions as outlined above.

## **Conclusion—control environment (process)**

3.19 All but one of the organisations audited had comprehensive funding agreements, developed in consultation with legal advisers, which met terms

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<sup>25</sup> *ibid.*

and conditions considered to be better practice. All organisations have developed standardised funding agreement general terms and conditions, in the form of templates. Special funding agreements were developed where necessary.

## Recommendation No.2

3.20 The ANAO recommends that organisations:

- maintain policy and procedural documents in a manner that allows them to be easily identified, accessed and updated;
- consider including items identified as better practice in the ANAO Better Practice Guide<sup>26</sup> in their policies and procedures for the administration of grants; and
- as appropriate, review the status of funding agreements to ensure clearly defined terms and conditions have been established and are enforceable in the event of non-compliance by the recipient.

### Sound and better practices noted

3.21 The following sound and better practices were identified in some organisations:

- policies, procedures and templates were distributed to staff via the Intranet/network server and other electronic means such as e-mail, which provided a single reference source so that consistent and up-to-date information could be accessed; and
- a 'Master Document Status List' was maintained to record all current documents utilised.

### Control environment (people)

3.22 The following table summarises the relevant principle and audit evaluation criteria, which were used to assess an organisation's control environment (people).

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<sup>26</sup> *Administration of Grants—Better Practice Guide*, ANAO, Canberra, May 2002.

**Table 6****People**

|                                  |  |
|----------------------------------|--|
| <b>Principle</b>                 | Organisations employ high quality and experienced staff and through training and regular communication ensure all relevant personnel are aware of their responsibilities, policies and procedures. |
| <b>Audit evaluation criteria</b> | Senior management is expected to take a pro-active approach to risk and control, ensuring key personnel are aware of governance responsibilities, through training and communication.              |

*Training*

**3.23** Organisations had engaged appropriately qualified and experienced staff to administer grants. At all levels, a number of staff involved in grants administration, had appropriate tertiary and other post-graduate qualifications.

**3.24** Most organisations had job descriptions for each position involved in the administration of grants to ensure staff were aware of their responsibilities. These job descriptions were also used for developing selection criteria when hiring new staff.

**3.25** All organisations had implemented formal and informal training programs that varied in substance and areas covered. Formal training was generally in the form of induction training, provided upon commencement of employment. Generally, this provided new staff with an introduction to the organisation and some common processes.

**3.26** All organisations ascertained individual training needs through a performance assessment/management process, and the majority of organisations trained staff in the administration of grants through on-the-job training and by having experienced staff members provide guidance. The ANAO considered this was adequate given the size of the organisations. However, some organisations would benefit from enhancing formal training, including both initial and refresher training programs, in the administration of grants to assist staff members understanding of specific internal processes and ensure they are fully aware of their individual responsibilities and tasks.

**3.27** Organisations had made use of one-off programs to communicate new and emerging issues. This was demonstrated by the amount of training performed on GST issues relating to grant funding.

**Conclusion—control environment (people)**

**3.28** Organisations would benefit from enhancing formal training provided to new and less experienced staff involved in the administration of grants so that policies and procedures are understood, and staff are fully aware of their individual responsibilities.

## Recommendation No.3

3.29 The ANAO recommends that organisations conduct both initial and refresher training programs to ensure that all staff appointed to the administration of grants are fully aware of, and understand, relevant policies, procedures and individual responsibilities.

### Sound and better practices noted

3.30 The audit noted the following in some organisations:

- induction, formal and one-off training programs had been used effectively; and
- job description documentation was in place to identify tasks and responsibilities.

### Control environment (structure)

3.31 The following table summarises the relevant principle and audit evaluation criteria, which were used to assess an organisation's control environment (structure).

**Table 7**

#### Structure

|                                  |   |
|----------------------------------|---|
| <b>Principle</b>                 | Organisations structure the administration of grants to specify responsibilities and accountabilities and allow for transparency of processes.  |
| <b>Audit evaluation criteria</b> | Organisations would be expected to have structured the administration of grants in a way that efficiently meets the business needs of the organisation, allowing for clear responsibilities and accountabilities. |

### *Responsibilities*

3.32 Program areas were responsible for the day-to-day activities associated with the administration of grants, whilst the finance branch was responsible for processing payments of grant funds. In some organisations, the finance branch was also responsible for reviewing, or providing support in the review of, financial acquittals. The ANAO considers that providing program areas with access to the financial experience and knowledge of staff within the finance branch to assist with the review of acquittals is better practice.



### *Delegations and authorisations*

3.33 The Chief Executive Officer (CEO) or Executive/Managing Director of most organisations had allocated responsibility for the efficient, effective and ethical management of the administration of grants to managers of individual program areas. In most cases, responsibility was allocated through CEIs and policy and procedural documents, including delegation schedules.

3.34 All organisations had formally documented delegations/authorisations. Generally, the delegations/authorisations provided authority to a range of officers commensurate with levels of responsibility. These delegations had been distributed to staff and were accessible via the Intranet and other electronic means such as e-mail.

### *Conflicts of interest*

3.35 All organisations provided guidance on conflict of interest issues to employees upon commencement of employment. However, most organisations did not formally consider any potential conflict of interest issues when allocating responsibility for particular recipients to individual staff members. The consideration of this issue is more relevant to organisations that do not have mechanisms in place to address conflicts of interest in an appropriate way (such as through the appointment of committees to review and approve grant applications). While no conflict of interest issues arose during this audit, all organisations should develop and implement a policy to capture individual board and staff members' changes in circumstances, which may give rise to potential conflicts of interest.

## **Conclusion—control environment (structure)**

3.36 The ANAO found that the audited organisations had provided guidance on conflict of interest issues to employees at the start of their employment. However, greater consideration could be given to developing and implementing a policy to capture individual board and staff members' changes in circumstances, which may give rise to potential conflicts of interest.

## **Sound and better practices noted**

3.37 Providing program areas with ready access to the financial experience and knowledge of staff within the finance branch to assist with the review of financial acquittals is considered to be better practice.

## Control environment (technology)

3.38 The following table summarises the relevant principle and audit evaluation criteria, which were used to assess an organisation's control environment (technology).

**Table 8**  
**Technology**

|                                  |  |
|----------------------------------|--|
| <b>Principle</b>                 | Organisations use technology to support the administration of grants in a way that contributes to the organisation's strategic objectives as well as ensuring cost-effective and efficient processing. |
| <b>Audit evaluation criteria</b> | Organisations would be expected to have implemented information systems as a strategic resource and have appropriate general IT controls in place.   |

### *Grants Management System (GMS)*

3.39 A GMS is a management information system designed to capture and record information pertaining to individual grant projects. Depending on the operational requirements of individual organisations, the ANAO considers that an effective GMS should have the capability to:

- accommodate systems-generated monitoring of key milestones by all teams;
- monitor actual grant payments against budgets;
- interface with other organisational systems<sup>27</sup>; and
- facilitate exchange of information/documentation (financial and non-financial) between and within the organisation and grant recipients.

3.40 All organisations utilised a GMS. However, the degree of functionality of systems between the organisations varied. One organisation's integrated system comprised of a recordkeeping system; a GMS; a workflow system; and an FMIS, while some organisations' GMSs were interfaced with an FMIS only. In other organisations, the GMS was a stand-alone system. The ANAO considers significant cost-benefits will result from the integration and/or interfacing of systems, including reduced data entry and a greater assurance that information between systems is consistent.

3.41 Some organisations' GMSs had the ability to record additional details of projects including performance and monitoring information, whilst in other organisations, information system capabilities were limited to recording of grant

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<sup>27</sup> For example, an FMIS.

details. These organisations used alternative systems and/or spreadsheets, to maintain performance assessment and monitoring data, and to meet various reporting requirements. In turn, this had led to some duplication of data entry.

**3.42** Other deficiencies noted in some organisations' GMS included:

- information that was inconsistent with information held in the FMIS and documentation filed on individual grant files including funding agreements. This highlights the need for organisations to ensure data recorded in systems is current and up to date;
- not all relevant information, such as dates of grant approval, funding agreement execution, payment and milestones; and project commencement, was recorded; and
- payment transactions were recorded exclusive of GST, which led to subsidiary ledgers being inconsistent with the general ledger. This in turn, resulted in inefficiencies, including the duplication of data entry. In addition, as payments were required to be matched to tax invoices, a manual adjustment was needed to ensure the GST was correctly accounted for and paid, despite the GMS being interfaced with the FMIS.

**3.43** Furthermore, some organisations were not fully utilising their current GMS. For example, some organisations were not utilising the GMSs' capability to record all details of projects including progress and communication with recipients. The ANAO considers that utilising all functions of the GMS, where appropriate, may lead to efficiencies and a more complete picture of the progress of individual projects.

**3.44** The ANAO noted innovations in some organisations' GMSs, including the automation of some grants administration processes. For example, some funding agreements, acknowledgment letters, and e-mail reminders about due/overdue milestone reports/acquittals were generated automatically.

### *General and application Information Technology (IT) controls*

**3.45** General and application IT controls are important for ensuring the validity, completeness and accuracy of data held within IT systems. As more processes become automated, IT controls become increasingly important and management should implement and regularly monitor these controls to help ensure their ongoing validity.

**3.46** General IT controls include, for example, unique identification log-ons and password controls that assist in ensuring the security of the computer system and environment. Application IT controls are controls that are used at the application level, that is, controlling individual items of software.

3.47 Most organisations have implemented computerised systems with the majority of organisations fully implementing general and application IT controls. The controls, which still needed to be implemented in one organisation, included the requirement for:

- individual and unique passwords to be allocated to individual staff members rather than program teams;
- passwords to be changed on a frequent basis;
- log-on identification to be restricted to one machine at any one time;
- user accounts to be disabled after a set number of failed attempts to logon; and
- the IT section to be advised when a staff member leaves so their user accounts can be closed.

3.48 Without controls such as these, there is a higher risk that the security and integrity of data is exposed to unauthorised changes. Furthermore, regular monitoring of IT controls will identify control weaknesses such as these and allow for corrective action to be taken by management.

### **Conclusion—control environment (technology)**

3.49 Given limitations in their GMS, some organisations had developed alternative methods for recording and reporting of information. This resulted in inefficiencies, such as the duplication of data entry.

## **Recommendation No.4**

3.50 The ANAO recommends that organisations:

- as appropriate, conduct a cost-benefit analysis of improving the functionality of their Grants Management Systems to make the administration of grants more efficient; and
- ensure that appropriate general and application IT controls are in place to provide adequate security for their systems and recorded data.

### **Sound and better practices noted**

3.51 The following sound and better practices were noted in some organisations:

- GMSs were interfaced with the FMIS;
- some activities of the administration of grants were automated; and

- most organisations GMSs had different levels of access for staff.

**3.52** In addition, in one audited organisation, the integrated system comprised a record keeping system; a GMS; a workflow system; and an FMIS.

## 4. Control Activities

### Introduction

4.1 Control activities are the specific practices, processes and methodologies that help an organisation ensure that:

- risks are reduced whilst opportunities for improvement are identified;
- irregularities are prevented or detected and addressed;
- assets are safeguarded; and
- financial records and relevant data are complete and accurately reflect the activities of an organisation.

4.2 An effective governance framework includes controls that minimise the impact of risks and contributes to the efficient and effective delivery of quality outputs and outcomes. Control activities promote compliance with the policies and procedures through the integrity, accuracy and completeness of administrative processes. Conversely, the failure of controls can create wide-ranging risks, including exposure to fraud. For this reason, emphasis should be more on preventative rather than detective controls.

### Audit findings and comments

4.3 The following table summarises the relevant principle and audit evaluation criteria, which were used to assess an organisation's control activities.

**Table 9**

#### Control activities

|                                  |   |
|----------------------------------|---|
| <b>Principle</b>                 | The establishment of specific control mechanisms within the administration of grants.   |
| <b>Audit evaluation criteria</b> | Each organisation would be expected to have specific controls to ensure validity, completeness, and accuracy of grant funding transactions, including the appropriate general and application IT controls. These controls would cover all elements of the process including planning, acquittals, compliance with grant conditions, monitoring and internal and external reporting. |

### Mechanisms to ensure grants are administered efficiently

4.4 The extent and frequency of ensuring that grants are being administered efficiently will vary according to the size of the grant, the associated risks or the sensitivity of the funding assistance, and will enable the assessment of whether:

- funds are being used for the purposes intended;

- individual projects are being undertaken as agreed;
- tasks critical to the success of projects are being accomplished;
- the final outcomes of the individual projects will be achieved; and
- the overall objectives of the grant program are being achieved.

4.5 All organisations had in place mechanisms to ensure individual grant projects were administered efficiently. These mechanisms were communicated to recipients through funding agreements, and included regular, formal and informal communication with recipients and review of milestone/final project reports and financial acquittals. However, a number of improvements to these mechanisms are discussed below.

### *Milestone reports and financial acquittals*

4.6 Funding for grants comes from public money made available to the organisation to be administered on behalf of the Government. Acquittal is one of the processes by which the recipient demonstrates that it has administered grant funds in a responsible and legal manner. If grants are not being acquitted properly, the level of accountability is reduced and the risks of misuse or loss of Commonwealth funds are increased.

4.7 The provision of guidelines and templates for milestone reports and financial acquittals ensures consistency in the format of information received from recipients and also allows for a more efficient review of the progress of grant projects. Most organisations had issued guidelines and/or templates to assist recipients with the provision of required information. Organisations that had not specified the requirements of milestone reports and financial acquittals in adequate detail received a variety of milestone reports and acquittals with varying quality from recipients.

4.8 Some organisations utilised a standard checklist/form in the assessment of milestone reports and financial acquittals. The ANAO considers that this ensured the consistency of reviews across program areas and provided for outcomes of these reviews to be documented on file with further action to be taken noted. However, in some instances, these forms had not been properly utilised or completed.

### *Comparisons of project actual expenditure versus budgets*

4.9 Reviewing performance against budget targets regularly assists in alerting management to any potential problems with a particular project including its ongoing viability. Furthermore, reviewing progress payments against budgetary targets assists in mitigating risks associated with a project that might prematurely

commit itself, overspend, or conversely, is unable to spend the full grant in the prescribed period. In such a case, the funding organisation can help to minimise the impact of this by authorising a transfer of funds between budget items. However, this can only be done if comparisons of project actuals versus budgets are performed progressively, and recipients provide financial information at the category/expenditure level.

**4.10** Some organisations had not progressively conducted comparisons of project actual expenditure against budgets at the category/expenditure level. Rather, these comparisons were performed at a holistic level and did not consider whether funds transferred between category/expenditure levels were approved transfers. Most organisations would benefit from enhancing the design of financial acquittal templates to assist with this.

### *Timeliness and follow-up of recipient provided information*

**4.11** Reliable, timely and adequate evidence is required to demonstrate that funds have been expended in accordance with the terms and conditions of the funding agreement. Administrative procedures to acquit grants on a regular basis are an important management control. The stringency of acquittal procedures should be balanced against the level of risk and take into account the cost of compliance. Risk management strategies will help achieve this balance.<sup>28</sup>

**4.12** The ANAO found that the provision of interim financial acquittals for multiple year projects was not tied to a portion of grant funds within most organisations reviewed. Furthermore, information was not always provided in a timely manner by recipients according to milestone report and financial acquittal due dates. Most organisations did not have consistent and transparent methods and time lines for the receipt, and follow-up, of overdue information to ensure grant payments were only made when key requirements were met.

**4.13** The ANAO considers that the provision of satisfactory milestone reports and interim acquittals should be a requirement of funding agreements and notes that it is often good practice to retain a small but significant portion of the grant funds until the recipient's final milestone report has been acquitted.<sup>29</sup> This enables regular review of the financial performance of projects and also provides an incentive to recipients to provide this information in a timely manner. Furthermore, organisations should consider not releasing further funding until such time as all milestone reports and acquittals have been provided for prior periods.

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<sup>28</sup> op. cit., *Administration of Grants—Better Practice Guide*. p. 11.

<sup>29</sup> ibid.



## Documentation

**4.14** The ANAO observed a lack of documentation on file in all audited organisations, relating to formal records of phone conversations and email correspondence. As well, most organisations did not maintain evidence of management review of grant files. In addition, some organisations did not maintain evidence of the review of recipient provided milestone reports, and some variations of milestone due dates and payments were not always formally documented.

**4.15** In the absence of proper documentation, it is not possible to determine whether timely action has been taken where required. The ANAO considers that this deficiency highlights the need for organisations to conduct a systematic risk-based assessment of recordkeeping requirements based on business, accountability/regulatory and stakeholder needs, and implement systems and procedures to create and capture records as required.<sup>30</sup>

## Reconciliations of systems utilised

**4.16** Reconciliations are an essential internal control over system integrity and facilitate assurance to management that system-generated information is complete and valid. Reconciliations should be performed on a timely and regular basis and should be reviewed by a responsible officer to ensure they are properly prepared. The risks associated with not carrying out this process include the early release of grant payments and erroneous decisions to fund recipients in future periods.

**4.17** The ANAO found data recorded in most organisations' GMS were inconsistent with data recorded in the FMIS and that some organisations had not performed reconciliations of payment and/or recipient information held in various systems.

**4.18** In addition, the ANAO noted that of the organisations that conducted regular reconciliations of payment transactions, reconciliation reports were not: always maintained properly; not signed off and dated by the preparer as complete; and not reviewed by someone independent of the reconciliation. Furthermore, some reconciliation reports generated were difficult to follow and interpret which made management review difficult.

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<sup>30</sup> The ANAO's report on recordkeeping provides information on what a sound recordkeeping system may include—*Recordkeeping*, Audit Report No.45, 2001–02.

## Conclusion

**4.19** The ANAO found that audited organisations could improve their mechanisms to administer grants by:

- progressively monitoring project actual expenditure against budgets, at the category/expenditure level;
- linking interim financial acquittals to milestone payments;
- establishing timely, consistent and transparent methods of follow-up of recipient provided information within organisations;
- considering the documentation needs of all stakeholders; and
- performing, reviewing and appropriately documenting reconciliations.

## Recommendation No.5

**4.20** The ANAO recommends that organisations:

- link the provision of financial acquittals to project milestones to ensure adequate and timely information is available to allow for projects to be monitored progressively; and
- assess the adequacy of existing systems and procedures for satisfying recordkeeping requirements.

## Sound and better practices noted

**4.21** In some organisations, the ANAO noted the following sound and better practices:

- standard templates were being used for the assessment of milestone reports and acquittals;
- guidelines and templates were being provided to recipients to assist in the preparation of required information; and
- funding was withheld until such time as required milestones were met.

**4.22** In one organisation, interim acquittals were attached to milestones and hence grant payments. This ensured recipients were meeting the terms and conditions of their funding agreement prior to further payments being released.

# 5. Information and Communication

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## Introduction

**5.1** An organisation's information and communication arrangements are fundamental to ensuring the achievement of organisational objectives. Effective arrangements provide a solid foundation for informed decision making and performance reporting. Information and communication arrangements will differ depending on the size, structure and geographical distribution of the organisation. The arrangements will also involve manual and computerised systems.

**5.2** Effective information and communication helps organisations establish whether resources are being directed towards the achievement of desired outputs and outcomes in the most efficient, effective and ethical way. With specific reference to the administration of grants, organisations need to ensure effective lines of communication both internally and externally.

**5.3** External communication requirements include promoting programs to prospective applicants, communicating results/outcomes of individual projects and programs to interested stakeholders including community interest groups, and Commonwealth reporting purposes such as annual reports.

**5.4** Internal communication requirements include ensuring managers and processing staff have up-to-date and complete information about individual projects and programs as a whole. An organisation must also ensure that managers have the right information to make decisions, for example, the financial progress and performance of an individual project, to ensure timely corrective action can be taken where necessary.

**5.5** Performance reporting assists organisations understand whether the administration of grants is meeting the needs of the organisation. It contributes to continuous improvement and enables staff to undertake and monitor their own operational activities, which can also be used as a tool in building staff confidence and morale.

## Audit findings and comments

**5.6** The following table summarises the relevant principle and audit evaluation criteria, which were used to assess an organisation's information and communication.

**Table 10****Information and communication**

|                                  |  |
|----------------------------------|--|
| <b>Principle</b>                 | Information systems are in place to provide relevant information for financial and management reporting purposes to the right people at the right time.  |
| <b>Audit evaluation criteria</b> | Each organisation would be expected to have in place systems to capture and report grants administration information. It would also be expected that close links have been developed between the general ledger and the GMS to enable good decision making in relation to grant monies. Each organisation would also be expected to have regular two-way information flows between the staff, working on the function, and management. |

**Financial and operational reporting**

**5.7** All organisations had formal reporting frameworks in place and prepared regular reports to the boards of management, which summarised the achievements, financial status and emerging risks (if any) of each of their programs. In addition, most organisations prepared some form of financial and operational reports on a regular basis for the use of senior management and program area managers. The reports provided information on the performance of grant programs and individual projects. In most cases, the processes used to generate them were effective including generation directly via the organisation's FMIS or GMS.

**5.8** Exception reports were also used in some organisations to determine: projects with outstanding milestone reports and acquittals; projects with milestone reports/acquittals received from the recipient but yet to be reviewed; grant payments due and payable; and recipients who have not met all terms and conditions of funding agreements.

**5.9** However, in organisations where the finance section reviews acquittals, and program areas are responsible for communicating with recipients, it may be beneficial for reports to be generated and disseminated to prompt follow-up of grantee provided information. In addition, generating reports from the GMS to aid communication within and between program areas would be more beneficial if greater analysis was conducted.

**5.10** One innovation noted during the audit was an icon appearing on individual desktop computers with pop-up boxes alerting users when updated financial reports were available online. The pop-up boxes also reminded individuals when they were due to review particular information, which enabled section heads to have access to real-time financial data. In addition, there were advantages in not having to distribute these reports in hard copy.

## **Information and communication with external stakeholders**

**5.11** Most organisations had, or are about to implement, communication strategies and/or plans. These plans and strategies are comprehensive and incorporate how each organisation provides information both internally and to external stakeholders such as grant recipients and community interest groups. Hence, communication strategies and plans are an important tool for organisations administering grants.

**5.12** A number of organisations had developed publications relating to individual grant programs. These publications contained information such as program guidelines and assisted potential applicants in preparing applications for funding. One organisation's initiative was to produce a handbook, which provided a consolidated overview of all programs funded by the organisation and clear and concise guidance and information on eligibility and appraisal criteria to potential grant applicants.

**5.13** Most organisations had developed, or were in the process of developing, their Internet web sites to contain publications and other information useful to grant recipients when applying for grants and meeting their funding obligations as well as to other interested parties.

**5.14** Some organisations had also conducted public forums; seminars; and workshops on grant programs.

## **Conclusion**

**5.15** The ANAO found that some of the organisations' operational and financial reporting was inadequate because there was no analysis of information in the reports. Improved analysis would assist users to obtain a better understanding of financial and performance data, which in turn, would inform decision-making.

## **Recommendation No.6**

**5.16** The ANAO recommends that organisations provide users with appropriate analysis of the financial and performance results of grant programs and individual grant projects to help them better understand and make use of financial and performance reports.

## Sound and better practices noted

5.17 The audit noted the following sound and better practices:

- comprehensive communication plans/strategies had been implemented in some organisations; and
- section heads, in one organisation, were provided with access to real-time financial data.

# 6. Monitoring and Review

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## Introduction

**6.1** Monitoring and review is the final component of an effective control framework. It is a key element of an organisation's continuous improvement process that helps ensure the organisation implements effective processes and tools to monitor and review relevant data. An effective monitoring and review environment includes performance measurement, and the use of both periodic reviews, such as those undertaken by internal audit and external consultants, as well as in-built review mechanisms including on-going monitoring.

## Performance measurement

**6.2** Performance measurement is widely recognised as a key tool by which organisations can monitor and review performance. One of the main advantages of performance measurement is that it enables organisations to express the results of a business process in quantitative, not qualitative, terms.

**6.3** Performance measures are evidence about performance that is collected and used systematically to report on the progress of an activity. They provide management with sufficient knowledge to make informed decisions on the performance of the function.

**6.4** By providing reliable, quantifiable data to evaluate business processes, performance measurement allows organisations to provide feedback about current performance and to set relevant, identifiable goals (targets) for future improvement. Moreover, it has long been acknowledged that, in general, 'what gets measured, gets done'. That is, the practice of measuring a task or activity focuses direct attention on it, and as a result, people will naturally strive to improve the result. It is therefore integral to any continuous improvement environment. Performance measurement is also integral to the internal control environment as it helps an organisation identify process problems as they occur, often well before the problems adversely affect outputs and outcomes.

**6.5** In some cases, quantified performance measures may not be available and less direct performance indicators may have to be used. These should be suitably described so that they can be put in perspective. Performance measurement is best supported by relevant, accurate, timely, accessible, interpretable and coherent performance information. This is necessary for the confidence of all parties and adds to their credibility and assurance.

## Methods to undertake monitoring and review

6.6 In addition to monitoring performance measures, the effectiveness of the control structure itself also needs to be monitored and reviewed. Control monitoring and review can be undertaken in various ways, including:

- on-going monitoring which is an inherent part of the process, such as control self-assessment, and by encouraging staff to identify breakdowns, redundancies, duplications and gaps in control procedures; and
- separate periodic reviews and evaluations, such as internal audit or process reviews. These reviews look at the effectiveness of control structures from another perspective and often provide the opportunity for on-going monitoring procedures to be revisited.

6.7 The scope and frequency of monitoring and review activities will depend primarily on an assessment of risks and the effectiveness of on-going monitoring. The greater the on-going monitoring, the less need there will be for separate evaluations. It is also important to note that the effectiveness and appropriateness of the control framework can change as the environment changes.

6.8 Monitoring and review provides assurance and feedback on whether program objectives are being achieved efficiently and effectively. They also provide an on-going check on the effectiveness of the internal control framework. Activity in this area significantly impacts continuous improvement. Periodic monitoring and review is often aligned with the sharing of ideas, both across the organisation and externally. This is associated with the benefits of sourcing independent and objective views. In-built monitoring and review mechanisms, such as control self-assessment, encourage ownership of controls and an enhanced internal control framework.

6.9 Control self-assessment is a reporting process where managers are actively responsible for developing, assessing, maintaining and monitoring the controls within their own areas of responsibility. This usually involves the completion of self-assessment checklists to confirm that control processes and procedures are clearly understood, implemented and are operating effectively. The checklist data can be collated along with other financial and operational performance data into reports.

## Audit findings and comments

6.10 The following table summarises the relevant principle and audit evaluation criteria, which were used to assess an organisation's monitoring and review.



**Table 11****Monitoring and review**

|                                  |  |
|----------------------------------|--|
| <b>Principle</b>                 | Monitoring and review takes place on an appropriate periodic basis that enables the organisation to check the internal control framework and help to ensure the organisation's strategic objectives are being achieved.  |
| <b>Audit evaluation criteria</b> | Each organisation would be expected to have regular monitoring and review processes in place to ensure that policies and procedures are adhered to and properly applied, and to identify changes and weaknesses in the operating environment. This might be achieved by reporting against performance measures through internal checking and auditing processes. The results of this process then need to be input into the next round of strategic planning and risk assessment performed by each organisation. |

**Performance measurement and reporting**

6.11 The ANAO found organisations were regularly reviewing performance indicators for the administration of grants. Specifically, some organisations had identified both quantitative and qualitative measures for individual grant projects and programs as a whole. However, reporting and analysis of performance against these indicators varied.

6.12 Most organisations had established program objectives, strategies, targets and performance indicators, which were reviewed and updated on an ongoing basis. These reviews, generally conducted by independent consultants, considered whether the program was conducted efficiently and effectively. Areas for improvement were also noted and, where required, action was implemented. Some organisations performed detailed cost-benefit analysis across program and sub-program areas to determine whether funding should be continued.

**Monitoring and review of the control structure**

6.13 While the governing body of an organisation is responsible for the control framework, individual senior and line managers can facilitate operational improvement through taking responsibility for the framework within their areas of control.

6.14 Some organisations had not adopted formal control self-assessment processes, relating to the administration of grants, as a mechanism to build-in regular monitoring and review. However, some organisations had regularly undertaken quality assurance reviews on various components of the administration of grants. Notwithstanding this, all organisations would benefit from improving the monitoring and review of the administration of grants to ensure both organisational and control objectives were being achieved efficiently and effectively.

6.15 All organisations had used the internal audit function as a means of monitoring grants administration, or had reviews scheduled to be performed in their current strategic internal audit plan.

## Conclusion

6.16 Whilst all audited organisations were undertaking some form of monitoring and review activities of the administration of grants, only some organisations had developed mechanisms to report the results of these activities regularly.

6.17 The organisations would benefit if they had formal arrangements in place that allowed for managers at all levels to assess whether the administration of grants, for which they are responsible, is being conducted efficiently and effectively.

## Recommendation No.7

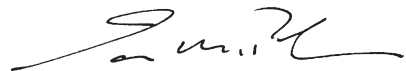
6.18 The ANAO recommends that organisations enhance mechanisms to assist in monitoring and reviewing the administration of grants through the use of appropriate performance indicators.

## Sound and better practices noted

6.19 The ANAO noted that in some organisations, quality assurance reviews were undertaken and provided some assurance to management in relation to the administration of grants.

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Canberra ACT  
4 November 2002



Ian McPhee  
Acting Auditor-General

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