

EXPLANATORY STATEMENT

Issued by the authority of the Minister for Finance and Deregulation

Financial Management and Accountability Act 1997 and Commonwealth Authorities and Companies Act 1997

Finance Minister's Orders (Financial Statements for reporting periods ending on or after 1 July 2011)

Financial Management and Accountability Act 1997 (FMA Act)

Subsection 63(1) of the *FMA Act* provides that Orders may be made on any matter on which the *FMA Act* requires or permits Orders to be made and on any matter on which regulations under the *FMA Act* may be made. Section 49 of the *FMA Act* provides that the Chief Executive of an Australian Government Agency must prepare financial statements in accordance with Finance Minister's Orders. These requirements are currently specified in Schedule 1 to the *Finance Minister's Orders (Financial Statements for reporting periods ending on or after 1 July 2011)* (FMOs).

Commonwealth Authorities and Companies Act 1997 (CAC Act)

Subsection 48(1) of the *CAC Act* provides that Orders may be made on any matter on which the *CAC Act* requires or permits Orders to be made. Section 9 of the *CAC Act* requires the directors of a Commonwealth authority to prepare an annual report in accordance with Schedule 1 to the *CAC Act*. Part 1 of Schedule 1 to the *CAC Act* provides that the annual report must include financial statements prepared by the directors in accordance with the Finance Minister's Orders. These requirements are currently specified in Schedule 1 to the *Finance Minister's Orders (Financial Statements for reporting periods ending on or after 1 July 2011)*.

Other legislative provisions

The Finance Minister's Orders are also made under the relevant provisions as set out below:

- subsection 47(1) of the *High Court of Australia Act 1979* in relation to how financial statements must be prepared by the High Court of Australia;
- subsection 193H(1) of the *Aboriginal and Torres Strait Islander Act 2005* in relation to how the accounts and financial statements must be prepared for the Land Account;
- subsection 50B(4) of the *Defence Service Homes Act 1918* in relation to how financial statements must be prepared by the Defence Service Homes Corporation; and
- subsection 43(3) of the *Natural Heritage Trust of Australia Act 1997* in relation to how financial statements must be prepared for the Natural Heritage Trust of Australia Account.

The Finance Minister's Orders set out the financial statement reporting requirements for Australian Government entities for reporting periods ending on or after 1 July 2011.

Specifics in relation to the Orders are as follows:

Finance Minister's Orders (Financial Statements for reporting periods ending on or after 1 July 2011)

Clause 1 of the Orders deals with naming of the Orders.

Clause 2 of the Orders deals with commencement of the Orders.

Clause 3 inserts Schedule 1, which sets out requirements for the preparation of annual financial statements for reporting periods ending on or after 1 July 2011, and specifies the legislation to which it applies.

Clause 4 of the Orders prescribes record-keeping requirements for the purposes of section 48 of the FMA Act.

Single Legislative Instrument

For 2011-12, the separate *Financial Management and Accountability Orders (Financial Statements)* and *Commonwealth Authorities and Companies Orders (Financial Statements)* prepared in previous years have been combined into a single legislative instrument. This has no impact for preparers of financial statements.

Retrospectivity

The retrospective commencement date of this legislative instrument does not adversely affect the rights of persons or otherwise impose liabilities, other than onto the Commonwealth, and as such, does not contravene subsection 12 (2) of the *Legislative Instruments Act 2003*.

Consultation

In accordance with section 17 of the *Legislative Instruments Act 2003*, all Commonwealth entities required to apply the Orders have been consulted and provided with the opportunity to submit comments on the draft version. This was achieved through the circulation of an exposure draft, publishing the draft documents on the Department of Finance and Deregulation's website and hosting information sessions for informal feedback which attracted high levels of attendance from a wide range of Commonwealth entities.

Where specific issues had a significant impact for particular entities, the Department of Finance and Deregulation also collaborated separately with affected entities. The Australian National Audit Office has also been consulted throughout the drafting process and has provided detailed comments on the Orders.

All feedback has been considered and amendments made where appropriate.

Attachments

Details of the main changes to reporting requirements for the reporting periods ending on or after 1 July 2011, as compared to the requirements that were previously in force, are provided in Attachment A. As a broad statement, the changes from the previous requirements are considered relatively minor.

The Statement of Compatibility with Human Rights as required by the *Human Rights (Parliamentary Scrutiny) Act 2011* is provided in Attachment B.

Attachment A to the Explanatory Statement

This attachment summarises the main changes in relation to the FMOs requiring the preparation of financial statements for reporting periods ending on or after 1 July 2011 for Australian Government entities.

New Policy

1. *Division 2 Content, Philosophy and Structure:* Added sections on content and philosophy of the FMOs, which set out the principles adhered to when preparing the FMOs. This additional policy will assist auditors and preparers in their interpretation of policies set out in the FMOs.

Amendments to existing policies

1. *Division 9 Financial Reporting Structure and Form:* All entities must explicitly disclose whether they operate on a for-profit or not-for-profit basis. Previously, only for-profit entities were required to disclose their basis of operation. This disclosure will increase transparency and public understanding of the operations of entities and results from a change in Australian Accounting Standards.
2. *Division 23 Director/Executive Remuneration:* Entities must prepare banded package disclosures based on 'reportable remuneration', which comprises actual benefits paid to senior executives as per the payment summary and payslips (where available). The requirements include separate disclosure of salary (including fringe benefits), allowances, superannuation, and performance bonuses in \$30,000 bands. These disclosures must also be prepared for other highly paid staff who do not meet the definition of a senior executive, yet received reportable remuneration in excess of \$150,000 for the financial reporting period.

The scope of this disclosure has also been extended to overseas employees and for-profit entities, (excluding other highly paid staff on overseas operational deployments consistent with previous years). These more comprehensive disclosures will enhance transparency and accountability for senior executives and other highly paid staff for whom remuneration is paid from public money.

3. *Division 85 to 91 Administered Reporting:* Entities with administered activities must now prepare more detailed disclosures including a full schedule of comprehensive income, a schedule of assets and liabilities, a cash flow and cash flow reconciliation. These disclosures were revised to provide more comprehensive information about the administered activities of agencies.
4. *Division 104 Disclosure of Appropriations:* Entities must now disclose determinations which support adjustments to annual appropriations showing date of effect and amounts. Entities must also disclose total unspent annual appropriations for administered by annual Appropriation Act, in addition to existing departmental disclosures. In addition, entities are now required to separately disclose Departmental and/or Administered Capital Budgets, showing amounts appropriated, formal adjustments and appropriation applied during the financial reporting period.
5. *Division 120 Special Accounts:* Entities with special accounts must split amounts debited into administered, departmental and special public money, rather than the previous nominal designation applied to all transactions and balances relating to the special account. Entities are also required to separately disclose amounts transferred back to the Official Public Account (where they are no longer required).
6. *Division 123 Competitive Neutrality and Cost Recovery:* These disclosures have been separated from Outcome disclosures and relocated to a new note. Income subject to Cost Recovery Policy is now required to be disclosed by activity.

Removal of policies

1. *PRIMA Forms*: Based on a conceptual review of information provided and some duplication of information in other notes, the Schedule of Asset Additions has been removed.

Statement of Compatibility with Human Rights

Prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011

Finance Minister's Orders (Financial Statements for reporting periods ending on or after 1 July 2011)

This Legislative Instrument is compatible with human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny Act) 2011*.

Overview of the Legislative Instrument

The purpose of the FMOs is to achieve consistency in the preparation of general purpose financial statements by Commonwealth entities and to enhance accountability and transparency with respect to financial reporting by Government.

Division 23 of the FMOs increases the extent to which Commonwealth reporting entities are required to disclose remuneration paid to senior executives, directors and other highly paid staff. PRIMA Forms of Financial Statements (which are mandatory under the FMOs) also require disclosure of related party transactions for directors of CAC authorities, including loans to directors. These disclosures are the Commonwealth's equivalent of private sector disclosures required by Australian Accounting Standards.

Human rights implications

This Legislative Instrument engages article 17 of the International Covenant on Civil and Political Rights, namely that it limits the human rights to privacy and reputation through the requirement to disclose information about the remuneration of senior executives, directors and other highly paid staff, as well as related party disclosures.

Legitimate objective

The disclosure of remuneration paid to senior executives, directors and other highly paid staff of Commonwealth entities is in the public interest, and forms part of a general move towards greater transparency over government finances and operations, as does the disclosure of related party transactions.

Further, the proposed level of disclosure is one of the Department of Finance and Deregulation (Finance)'s responses to a broader focus on public sector transparency and accountability, including the report 'Review of Operation Sunlight: Overhauling Budgetary Transparency'. Prepared by the then Senator Andrew Murray, this report investigated and restated the importance of transparency and accountability in the public sector financial management framework.

Reasonable, necessary and proportionate

The potential impact on the privacy and reputation rights of individuals has been considered in the development of the FMOs, and Finance has undertaken extensive consultation with Commonwealth entities on the proposed disclosures.

The disclosure requirements in Division 23 of the FMOs entail a limitation of privacy that is similar to that required by Division 23 of the FMOs in previous years, with the 2011-12 requirements only entailing slightly more disaggregated disclosures which

separately identify each element of remuneration received. However, information is still aggregated to a level that makes it unlikely that most individuals could be separately identified. In addition, remuneration information for secretaries of Departments of State (who are the individuals most likely to be separately identifiable in the remuneration disclosures) is otherwise publicly available, and thus the disclosure of their remuneration would not limit privacy any further.

Disclosures about related parties are consistent with previous financial reporting periods (and are broadly based on equivalent disclosures for for-profit entities under Australian Accounting Standards).

The limitation on privacy and reputation imposed by the FMOs is not targeted at all employees of an agency; it is only directed at senior executives, directors and other highly paid staff. The disclosures made under Division 23 of the FMOs capture all substantive senior executives as well as other highly paid staff, which is a broader range of individuals than is captured by private sector disclosures; however, the disclosures relating to each individual are much less extensive and personal than those made in the private sector, in which individuals are explicitly named and details of their individual performance and related remuneration are published without aggregation.

Conclusion

The FMOs are compatible with human rights as it is in the public interest to create a public sector financial reporting framework that provides greater transparency and accountability in relation to the remuneration of individuals who are paid from public funds. To the extent that the FMOs limit the privacy of such individuals, those limitations are reasonable and proportionate.

Penelope Ying Yen Wong, Minister for Finance and Deregulation