BACKGROUND NOTE

13 December 2012

The Commonwealth efficiency dividend: an overview

Dr Nicholas Horne
Politics and Public Administration Section

Contents

Introduction ............................................................................................................................................. 1
Definition, basis and origins ..................................................................................................................... 2
Scope and application .............................................................................................................................. 3
Scope ................................................................................................................................................... 3
Application .......................................................................................................................................... 5
Rate ..................................................................................................................................................... 7
Exemptions ......................................................................................................................................... 8
Ongoing efficiency dividend ................................................................................................................ 8
Additional single-year imposts ........................................................................................................... 10
Supporting arguments and criticisms .................................................................................................... 11
Supporting arguments ....................................................................................................................... 11
Criticisms .......................................................................................................................................... 11
Gauging public sector efficiency ......................................................................................................... 13
Alternatives .......................................................................................................................................... 14
Scrubiny ............................................................................................................................................... 15
2000s ............................................................................................................................................... 15
1990s ............................................................................................................................................... 17
Conclusion .......................................................................................................................................... 19
Introduction

The efficiency dividend, an annual funding reduction for Commonwealth government agencies, has been in place for 25 years. While it is by no means the only mechanism by which the government seeks efficiencies in its operations, the efficiency dividend is ‘the most readily acknowledged across-the-board budget mechanism for promoting improvements in agencies’ efficiency’. ¹ The dividend has attracted attention in recent years in relation to increases (particularly the application of additional imposts over and above the ongoing annual reduction) and its impact on agencies.

As the long life of the efficiency dividend indicates, a focus on efficiency in Commonwealth public service operations is nothing new. Indeed, the importance of efficiency was highlighted as early as 1901 during parliamentary debates on the legislation establishing the public service, and subsequently by the first Public Service Commissioner in 1904.²

The efficiency dividend is not unique to the Commonwealth: most of the state and territory governments apply, or have applied, efficiency dividends to their operations.³ Efficiency dividend mechanisms are also used overseas.⁴

Definition, basis and origins

The efficiency dividend has been defined as an ‘annual reduction in funding for the overall running costs of an agency’. The justification for the dividend is that ongoing increases in productivity make it possible to reduce funding to Commonwealth agencies and realise savings without compromising outputs:

... as the public service continually becomes more productive, there is room for cutting public sector inputs by the rate of increase in productivity (or something less) without changing the level of output. This can allow the derived efficiency gains to be redirected to higher priority areas, as determined by government.

The efficiency dividend also recognises that the public sector does not face the same incentives as the private sector to pass on gains from increased productivity in the form of lower prices. The aims of the efficiency dividend are to:

- give managers the incentive to continually seek new or more efficient means of carrying out continuing government business
- allow government to redirect a portion of efficiency gains to higher priority activities
- clearly demonstrate Public Service efficiencies resulting from improvements in management and administrative practices.

The efficiency dividend commenced in the 1987–88 financial year. In September 1986 then Prime Minister Hawke announced public service efficiency reforms that included an efficiency dividend of 1.00 per cent per annum for three years commencing in 1987–88:

... departments and agencies will be required to achieve real reductions in the running costs of on-going activities—something like the payment of an efficiency dividend of which the Australian taxpayer will be the ultimate recipient. They will be required to reduce the real level of resources directed to administer existing activities by an average one per cent each year over the next three years, starting in 1987–88 ... all government agencies should be able to make continuing efficiency gains by improving their administrative procedures, making better use of improvements in technology and in the use of human resources.
In May 1987, prior to the 1987–88 Budget and the commencement of the efficiency dividend, the government announced that the annual dividend rate would be 1.25 per cent over the 1987–90 period rather than 1.00 per cent. The 1987–88 Budget confirmed the adjusted rate.

The Joint Committee of Public Accounts and Audit (JCPAA) has noted that when it was introduced the efficiency dividend ‘was not a completely new idea’ and had ‘followed years of arbitrary annual percentage cuts that the Government imposed on departments’.

The 1986–87 Budget had foreshadowed the introduction of the dividend and had imposed preliminary cross-portfolio savings in salary and administration expenditures ‘reflecting an initial step in receiving the benefits of efficiency improvements brought about through ... public service reforms put in place by the Government since 1983’. A 2011 government review of agency efficiency observed that ‘the basic concept and application’ of the efficiency dividend ‘have changed little since its introduction’.

Scope and application

Scope

The efficiency dividend operates as an annual funding reduction for Commonwealth Government agencies in real terms. Agencies that receive government appropriations come within the ambit of the efficiency dividend, so it is applied not only to Australian Public Service (APS) agencies such as the main Departments of State but also to non-APS agencies within the General Government Sector such as the Australian Federal Police and the parliamentary departments.

Virtually all Commonwealth agencies are subject to either of two overarching financial framework statutes: the Financial Management and Accountability Act 1997 (FMA Act) or the Commonwealth Authorities and Companies Act 1997 (CAC Act). In 2011, the efficiency dividend was fully applied to 66 per cent of agencies subject to one of these two Acts; 30 per cent (all under the CAC Act) were

---

25%2F0120%22. See also DoFD, Submission to the Joint Committee of Public Accounts and Audit, Inquiry into the effects of the ongoing efficiency dividend on smaller public sector agencies, op. cit., pp. 1–2.
15. The General Government Sector ‘comprises all government departments, offices and some other bodies’ and ‘provides public services that are mainly non-market in nature and for the collective consumption of the community, or involve the transfer or redistribution of income’. Australian Government, Budget measures: budget paper no. 1: 2012–13, Commonwealth of Australia, Canberra, 2012, p. 9–13, viewed 12 December 2012,
not subject to the dividend as they did ‘not receive direct government appropriations’. A number of agencies also have specific exemptions from the efficiency dividend (see further below).

Australian Accounting Standard 1050 Administered Items requires that government agencies distinguish between revenues and expenses that they administer for the Government and those over which they have some control. In the main, administered expenses are the costs of providing programs on behalf of the Government and are ‘normally related to activities governed by eligibility rules and conditions established by the government or Parliament such as grants, subsidies and benefit payments’. Departmental expenses are agencies’ operating costs such as ‘employee expenses; supplier expenses; other operational expenses’. Agencies generally have little control over administered appropriations but have a greater measure of control over appropriations provided to cover their departmental expenses. In 2010–11 administered expenses accounted for some 85 per cent of total Commonwealth budget outlays while departmental appropriations ‘account[ed] for about 12 per cent of total budget outlays’.

The efficiency dividend is primarily applied to departmental appropriations including ‘funding for depreciation/amortisation, Departmental and Administered Capital Budgets and Collection Development Acquisition Budgets’. The dividend is also applied to ‘appropriations for other expenses of a departmental outputs type nature’ and ‘funding for all new policy initiatives following the year in which the new measures are introduced into those appropriations’. Unless otherwise determined, the dividend is not applied to administered appropriations; in 2011 six programs with administered funding were subject to the efficiency dividend, and in March 2011 the government indicated that, from the 2011–12 Budget, the scope of the dividend’s application would include administered appropriations involving ‘payments for outsourced programs that could have been managed within the Australian Government’. In 2010–11, after taking exempted agencies into account, the efficiency dividend was applied to approximately 6.50 per cent of total Commonwealth budget outlays.

---

16. DoFD, *Report of the review of the measures of agency efficiency*, op. cit., p. 66. Some other CAC Act bodies however were subject to the efficiency dividend.


19. Ibid., p. 7.


24. Ibid.
The Commonwealth efficiency dividend: an overview

The efficiency dividend is also not applied to certain monies received by agencies under section 31 of the FMA Act. Under section 31 of this Act agencies may increase their departmental appropriations by retaining certain receipts prescribed in the FMA Regulations (for example insurance recoveries, proceeds from minor departmental asset sales, and cost offsets related to agency activity such as user charges).

Application

Prior to the 2011–12 Budget the efficiency dividend was directly applied to agencies’ budgets. From the 2011–12 Budget the efficiency dividend has been applied at the portfolio level in order to give ministers flexibility to vary the impost of the dividend among agencies in their portfolios: 25

It enables ministers, if they have agencies where they believe there is more scope for efficiencies, to direct that those take a greater proportion of the [efficiency dividend] than another agency in their portfolio. 26

The efficiency dividend is applied before agencies’ appropriations are subjected to indexation. 27

Indexation is the mechanism by which ‘agencies’ appropriations are generally adjusted each year by wage cost indices’: 28

The indices comprise a component to reflect wage increases (in accordance with movements in the safety net adjustment) and a component to reflect changes in the prices of goods and services (as shown by the consumer price index). 29

The Department of Finance and Deregulation (DoFD) has observed that ‘[w]hile the application of the efficiency dividend on agencies reduces the level of resources at their disposal, agencies receive additional resources through the indexation process’. 30 It has been noted elsewhere, however, that if indexation is lower than wage and price increases (resulting in a funding shortfall), the efficiency

27. DoFD, Submission to the Joint Committee of Public Accounts and Audit, Inquiry into the effects of the ongoing efficiency dividend on smaller public sector agencies, op. cit., p. 3.
29. Ibid.
30. DoFD, Submission to the Joint Committee of Public Accounts and Audit, Inquiry into the effects of the ongoing efficiency dividend on smaller public sector agencies, op. cit., p. 4.
The Commonwealth efficiency dividend: an overview

dividend can intensify funding pressures on agencies. Another mechanism through which agencies are able to seek further resourcing is the new policy proposal (NPP) process, which is an ‘opportunity for an agency to obtain additional funding for new work or new programs the Government seeks to implement’. Under the devolved financial management framework established by the FMA and CAC Acts, individual agencies are responsible for how they implement the annual funding reduction imposed by the efficiency dividend. There is no reporting framework for agencies regarding implementation, although the government has indicated that reporting will be required in respect of the additional single-year impost in 2012–13 (see further below).

In 2011 the Australian Public Service Commission (APSC) reported a range of strategies employed by agencies in implementing the efficiency dividend including ‘reducing travel, increasing use of video conferencing, closer monitoring of vacancies to determine if they need to be filled, delaying filling of vacancies, conducting accommodation reviews and reducing non-ongoing employment’. Previously in 2008 the APSC reported broadly similar implementation strategies including travel reductions and increased video conferencing, ‘tighter control over recruitment actions’ and staffing reductions, ‘reprioritising activities’, reductions in contractor/consultancy use, and ‘re-engineering approaches and using more efficient systems’.

The implementation and impact of the efficiency dividend in respect of individual agencies has periodically been raised at Senate estimates hearings. The effect of the dividend on agencies also receives periodic media attention, for example in relation to the 2012–13 additional impost.

31. JCPAA, Report 413: The efficiency dividend and small agencies: size does matter, op. cit., p. 5. The JCPAA estimated for example that, for 2008–09, an indexation shortfall of 2.00 per cent combined with a 3.25 per cent efficiency dividend for that year meant an overall funding reduction for agencies of 5.25 per cent: ibid.


36. See for example ‘Senate Legal and Constitutional Affairs Legislation Committee: estimates’, Senate, Debates, 14 February 2012, viewed 12 December 2012, http://parlinfo.aph.gov.au/parlInfo/search/display/display.w3p;query=Id%3A%22committees%2Festimate%2F845c79f4-24f2-471d-b0a4-310947ada3f0%2F0001%22

Rate

Over the years the annual base rate at which the efficiency dividend has been applied has varied between 1.00 per cent and 1.50 per cent; for most of its existence the dividend has been applied at a rate of either 1.00 per cent or 1.25 per cent. Since 2008 the Government has introduced two additional single-year imposts (in 2008–09 and 2012–13) which have been applied over and above the annual base rate. The 2008–09 additional impost brought the overall rate of the efficiency dividend to 3.25 per cent for that year; for 2012–13 the additional impost has brought the overall rate to 4.00 per cent.

The scope of the additional single-year imposts has differed slightly from that of the ongoing dividend, with further specified exemptions being granted. Table 1 below gives the annual rate of the efficiency dividend since its introduction not including the precursor savings specified in the 1986–87 Budget.

Table 1: Efficiency dividend annual rates 1987–

<table>
<thead>
<tr>
<th>Period</th>
<th>Annual rate (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1987–1994</td>
<td>1.25%</td>
</tr>
<tr>
<td>1994–2005</td>
<td>1.00%</td>
</tr>
<tr>
<td>2005–2008</td>
<td>1.25%</td>
</tr>
<tr>
<td>2008–2009 (base rate of 1.25% + additional single-year 2.00% impost)</td>
<td>3.25%</td>
</tr>
<tr>
<td>2009–2011</td>
<td>1.25%</td>
</tr>
<tr>
<td>2011–2012</td>
<td>1.50%</td>
</tr>
<tr>
<td>2012–2013 (base rate of 1.50% + additional single-year 2.50% impost)</td>
<td>4.00%</td>
</tr>
<tr>
<td>2013–2015 (projected)</td>
<td>1.25%</td>
</tr>
</tbody>
</table>

Sources: compiled from various sources.38

---

38. Compiled from: DoFD, Submission to the Joint Committee of Public Accounts and Audit, Inquiry into the effects of the ongoing efficiency dividend on smaller public sector agencies, op. cit., p. 2; L Tanner, Labor delivers on savings, media release, 22 November 2007, viewed 26 September 2012, 
http://parlinfo.aph.gov.au/parlInfo/search/display/display.w3p;query=Id%3A%22media%2Fpressrel%2FDM0P6%22; Australian Government, Budget measures: budget paper no. 2: 2008–09, Commonwealth of Australia, Canberra,
The monies that the efficiency dividend returns to the Commonwealth Budget are not insubstantial. In December 2008 it was estimated that, over 2008–09, the combination of the ongoing 1.25 per cent dividend and the additional 2.00 per cent impost would return some $662 million to the Budget (approximately $719 million in 2012 prices);\(^{39}\) the 2008–09 Budget estimated that the additional 2.00 per cent impost alone would yield savings of almost $1.76 billion over the 2007–12 period (around $1.9 billion in 2012 prices).\(^{40}\) For 2012–13, the government has estimated that the additional 2.50 per cent impost will return $500 million to the Budget in 2012–13 and just under $1.5 billion over the 2012–15 period.\(^{41}\)

There is very little information on aggregate actual savings realised as a result of the dividend over time. In March 1994 the House of Representatives Standing Committee on Banking, Finance and Public Administration estimated that aggregate savings since the introduction of the efficiency dividend in 1987–88 were $508 million ($824 million in 2012 prices).\(^{42}\)

**Exemptions**

**Ongoing efficiency dividend**

Nine agencies have full or partial exemptions from the ongoing efficiency dividend. Three agencies have full exemptions:

- the Australian Broadcasting Corporation and the Special Broadcasting Service Corporation due to election commitments from both major parties to ‘maintain the real level of funding’ for each broadcaster, and

- Safe Work Australia due to co-funding by both the Commonwealth and state/territory governments.\(^{43}\)

Six agencies have partial exemptions:

- the Commonwealth Scientific and Industrial Research Organisation (CSIRO) and the Australian Institute of Marine Science (AIMS)—application of the efficiency dividend for the CSIRO and the

---

AIMS has generally been restricted to departmental appropriations for administrative expenses (around 30 per cent of funding for the CSIRO and 12 per cent of funding for the AIMS in 2011 and in previous years)\(^4^4\)

- the Australia Council for the Arts—the efficiency dividend is applied to the entirety of Australia Council appropriations except for appropriations for Major Performing Arts organisations funding (around 55 per cent of appropriations in 2011)\(^4^5\)

- the Australian Customs and Border Protection Service—the efficiency dividend is not applied to appropriations for contracted maritime surveillance operations\(^4^6\)

- the Australian Nuclear Science and Technology Organisation (ANSTO)—the efficiency dividend is applied to departmental appropriations for administrative expenses (around 15 per cent of ANSTO’s total appropriation),\(^4^7\) and

- the Department of Defence—the efficiency dividend is applied to approximately 11 per cent of Department of Defence appropriations relating to ‘civilian and non-operational areas’ of the Department.\(^4^8\)

The application and scope of exemptions from the ongoing efficiency dividend can vary over time. The CSIRO, for example, was subject to the dividend across the entirety of its funding for the 2008–09 financial year; ANSTO had a full exemption from the efficiency dividend prior to the 2008–09 Budget.\(^4^9\) Prior to 2005–06 the Department of Defence was fully exempt from the efficiency dividend.\(^5^0\)


\(^4^7\) Ibid., pp. 66–69.

\(^4^8\) Ibid., pp. 66–67, 69.

\(^4^9\) CSIRO, Submission to the Joint Committee of Public Accounts and Audit (Department of Innovation, Industry, Science and Research submission Attachment A), Inquiry into the effects of the ongoing efficiency dividend on smaller public sector agencies, op. cit., p. 2; Australian Nuclear Science and Technology Organisation, Submission to the Joint Committee of Public Accounts and Audit (Department of Innovation, Industry, Science and Research submission
Additional single-year imposts

Agencies exempted from the ongoing efficiency dividend have also been exempted from the additional imposts in 2008–09 and 2012–13, although it is not clear whether this encompasses all agencies with full and partial exemptions from the ongoing dividend or only those with full exemptions.\(^{51}\) Further specific exemptions from the additional single-year imposts have also been granted as follows:

- **2008–09 impost**—Australian Trade Commission; Australian Fair Pay Commission Secretariat; Workplace Authority; Australian Prudential Regulation Authority; Australian Sports Commission\(^{52}\)

- **2012–13 impost**—Family Court of Australia; Federal Court of Australia; High Court of Australia; Federal Magistrates Court; Administrative Appeals Tribunal; Social Security Appeals Tribunal; National Native Title Tribunal; Migration Review Tribunal—Refugee Review Tribunal; Australian National Maritime Museum; National Gallery of Australia; National Museum of Australia; National Library of Australia; Australia Council for the Arts; Australian Film Television and Radio School; Australian Sports Commission; National Film and Sound Archive; National Archives of Australia; Old Parliament House (Museum of Australian Democracy); Screen Australia; Australian Institute of Aboriginal and Torres Strait Islander Studies; Australian War Memorial; Torres Strait Regional Authority; Aboriginal Hostels Limited; Indigenous Business Australia; Indigenous Land Corporation; Australian Communications and Media Authority.\(^{53}\)

---

52. DoFD, Submission to the Joint Committee of Public Accounts and Audit, *Inquiry into the effects of the ongoing efficiency dividend on smaller public sector agencies*, op. cit., p. 4.
Supporting arguments and criticisms

Salient supporting arguments and criticisms that have been advanced in relation to the efficiency dividend are summarised below.

Supporting arguments

As noted above, the basis for the efficiency dividend is that it allows government to realise savings through reductions in agency funding due to ongoing increases in productivity. It is also argued that the dividend:

- is effective for the purpose of returning efficiency savings to the Budget because it is ‘simple, predictable and reasonably equitable owing to its near-universal application’
- assists in budgetary and agency planning due to its predictability
- is ‘administratively efficient, being applied through a simple adjustment to agency estimates’
- ‘provides budgetary pressure, which is an incentive for agencies to operate more efficiently’
- does not impinge on the resource management responsibilities of agency chief executive officers, and
- is preferable to a ‘more interventionist approach by [DoFD] to assess whether agencies [are] operating efficiently and to seek savings where this [is] not the case’.\(^54\)

Criticisms

One of the main criticisms of the efficiency dividend is that it is a blunt instrument—it is applied on the same basis for most agencies without taking into account differing resourcing arrangements, which can lead to varying impacts on agencies:

> Agencies that are more reliant on receipts and the other sorts of appropriations [other than departmental appropriations] tend to be less affected by the dividend. This includes regulators and commercial research agencies that are funded from industry levies. The agencies that are more affected by the dividend include the courts, cultural agencies, oversight agencies and departments of state. For these agencies, [departmental] appropriations can comprise almost 100 per cent of their funding.\(^55\)

In this vein it has been argued that the efficiency dividend can have a disproportionate impact on small agencies due to their budgetary and functional constraints. In 2008 the JCPAA expressed the

---


\(^{55}\) JCPAA, Report 413: The efficiency dividend and small agencies: size does matter, op. cit., p. xi.
view that ‘[s]maller agencies face particular challenges in relation to the efficiency dividend’, and that the dividend is inappropriate for cultural institutions with high asset levels and asset-dependent appropriation funding.\textsuperscript{56} In 2008 also the Australian National Audit Office expressed the view that ‘the increasing demands on agencies, particularly small agencies, since the efficiency dividend was introduced more than 20 years ago suggest it is time to rethink this policy’.\textsuperscript{57}

In 2011 the government review of agency efficiency acknowledged that ‘[f]or some agencies the dividend’s bluntness as an instrument can lead to sub-optimal consequences’,\textsuperscript{58} and that:

... those smaller agencies that have a high ratio of non-discretionary costs and/or that have not historically attracted new funding are likely to be disproportionately affected by the [e]fficiency [d]ividend.\textsuperscript{59}

The 2011 review also stated, however, that it did ‘not share the [JCPAA’s] view that there is at present a definable group of smaller agencies that are universally disproportionately affected by the [e]fficiency [d]ividend’ and that ‘rather than size, an agency’s ability to find efficiencies is perhaps more clearly linked to where that agency is situated on an efficiency spectrum’.\textsuperscript{60}

Other salient criticisms of the efficiency dividend include:

• the blanket nature of the dividend and its implementation by agencies enable governments to avoid making funding decisions at ministerial level regarding specific programs and activities

• agencies that experience difficulty realising efficiency gains can resort to expenditure reductions in other areas (for example staffing) in order to meet the annual funding reduction, which can impact negatively on workloads and outputs

• the rate of the dividend is ‘too high’ and ‘is not underpinned by a formal assessment of the potential for efficiencies to be found’

• ‘[t]here is no clear connection between the dividend and any actual efficiency measures’, and

• the dividend can lead to ‘gaming’ behaviour by agencies in order to compensate for the funding reduction, for example by ‘putting forward new policy proposals in order to gain new funding that is then to some extent used to offset the cumulative impact of the dividend’.\textsuperscript{61}

\textsuperscript{56} JCPAA, Report 413: The efficiency dividend and small agencies: size does matter, op. cit., pp. 6, 56.
\textsuperscript{57} ANAO, Submission to the Joint Committee of Public Accounts and Audit, Inquiry into the effects of the ongoing efficiency dividend on smaller public sector agencies, op. cit., p. 7.
\textsuperscript{58} DoFD, Report of the review of the measures of agency efficiency, op. cit., p. 51.
\textsuperscript{59} Ibid., p. 26.
\textsuperscript{60} Ibid., p. 26.
Gauging public sector efficiency

The criticism that the efficiency dividend is not clearly connected to concrete efficiencies raises the problematic issue of gauging public sector efficiency. As far back as 1994 it was noted that there was no reliable way of calculating APS productivity gains. More recently, in 2009, the OECD noted that ‘[p]roductivity gains in the public sector are very difficult if not impossible to measure’. In 2011 the government review of agency efficiency noted that ‘[t]here is no accepted or reliable way of measuring the relative efficiency of the public sector’, and that:

The absence of reliable data and of an accepted way of measuring productivity in the [APS] poses a serious obstacle to developing a robust estimate of efficiency gains over time; it therefore also hampers the development of policies that allow government to share the benefits of efficiency gains.

The review also noted that ‘[s]ome of the main obstacles to measuring public sector efficiency are the difficulty of accounting for changes in quality and lack of a market price for many public sector outputs’. The review recommended that common functions across agencies be benchmarked in order to better gauge public sector efficiency.


62. HRSCBFPA, Stand and deliver: inquiry into the efficiency dividend arrangements, op. cit., p. 12.
65. Ibid., pp. 17–18. The review also observed however that the Australian Government appears to be ‘reasonably efficient’ on international comparisons: p. 18.
66. Ibid., p. viii.
67. Ibid., pp. viii, 47, 50.
Alternatives

Over the years a number of alternatives or variations to the efficiency dividend have been advocated including the following.

- replacing the efficiency dividend with productivity improvements realised through enterprise bargaining
- replacing the efficiency dividend with ‘regular audits of agency and/or portfolio efficiency as a basis for developing efficiency measures, separately to the annual budget process’, or with regular independent ‘agency reviews which assess the actual potential for savings in each department and use these as a basis for individual agency efficiency targets’, and
- exempting a specified portion of agency appropriations from the efficiency dividend according to agency type or appropriation size (recommended by the JCPAA in 2008—see further below).

The 2011 government review of agency efficiency, while recommending that the efficiency dividend be retained in the short term, noted:

The [e]fficiency [d]ividend encourages efficiency indirectly through necessity—reduced estimates for, in theory, the same quality and level of output—but in a way that does not allow actual efficiencies to be identified and quantified. It is also doubtful that the dividend is the optimum way of promoting substantial efficiencies.

The review concluded that ‘[a]n efficiency agenda that aims to engender substantial change should form part of a long-term fiscal strategy’ and recommended the development of alternative approaches to promoting efficiency over the medium- to long-term (the review posited one conceptual model for this involving the removal of the efficiency dividend, the capping of agency funding, and benchmarking agency expenses against efficient prices for services). The review also recommended the pursuit of a medium-term strategic efficiency agenda involving the ‘[b]enchmarking of common functions’, ‘[r]ationalisation of the number of agencies’, and developing a ‘road-map for standardising common processes and making greater use of shared services’.

70. Ibid., pp. 52, 35–44.
71. Ibid., pp. 45–50.
Scrutiny

Over the last two decades the efficiency dividend has been examined on a number of occasions by both government and the Parliament either as a standalone subject or as part of broader inquiries; the dividend has also been raised at Senate estimates. Significant reviews of the efficiency dividend, including those referred to in this paper, are noted below.

2000s

Government review of the measures of agency efficiency (2011)

In 2010–11 the government conducted an internal review of mechanisms to advance agency efficiency in the APS; the review was recommended by a previous government-commissioned review of Commonwealth public administration.72 In its 2011 report the agency efficiency review considered the efficiency dividend at length and concluded that it ‘was not convinced by any of the information it gathered that the [e]fficiency [d]ividend was manifestly unsustainable in the long term’.

Empirical evidence strongly suggests that the dividend, which has been applied for over 20 years, is relevant in the overall context of the budget framework. Retaining it is obviously a viable option for providing a budgetary incentive for agencies to seek efficiency and to give government a share of efficiency gains. The [e]fficiency [d]ividend is simple, effective and predictable.74

However, the review also noted some flaws in the efficiency dividend, stating that it ‘promotes efficiency only indirectly, by creating a budget pressure for agencies, and probably creates an incentive for budgetary gaming’, and that ‘[f]or some agencies the dividend’s bluntness as an instrument can lead to sub-optimal consequences, which have so far been managed on a case-by-case basis’.75 The review recommended that the efficiency dividend be kept in place for the short term but with ‘more flexibility to re-allocate its impacts at agency level’ via application at the portfolio level.76 The government adopted this recommendation.

The review made a number of other recommendations including developing alternative approaches to promoting efficiency for the medium- to long-term and implementation of a strategy to ‘manage costs across government’ including meeting the impost of the efficiency dividend.78

---

72. AGRAGA, Ahead of the game: blueprint for the reform of Australian Government administration, op. cit., p. 68.
74. Ibid.
75. Ibid., pp. 51–52.
76. Ibid., p. 44.
77. P Wong (Minister for Finance and Deregulation), Driving efficiencies in government, op. cit., p. 1.
Joint Committee of Public Accounts and Audit (2008)

In 2008 the JCPAA conducted an inquiry into the effects of the efficiency dividend on small agencies (defined by the Committee as agencies with annual departmental appropriations of $150 million or less). The JCPAA considered a number of different types of small agencies (non-executive agencies, cultural agencies, courts and scientific agencies) and concluded that ‘size is an important factor for agencies when delivering efficiencies’.79 The Committee further noted that agency function is also a significant factor:

... agencies ... [with] precisely defined technical functions ... have less scope to reprioritise activities because any decrease in a long-standing activity will quickly be identified as a drop in a core function by their stakeholders ... Further, agencies with tightly defined functions are less likely to be able to put convincing cases for new policy funds during the Budget.80

The JCPAA concluded that ‘there is value in retaining a ‘top-down’ efficiency incentive for agencies’, but also came to the view that ‘[s]maller agencies face particular challenges in relation to the efficiency dividend’:81

... smaller agencies are often established to fulfil a specific function or purpose. This limits their capacity to reprioritise or trim discretionary activities. Also, such agencies are occasionally required to absorb new functions. The cost of one additional activity may appear small, but it could represent a large proportion of a small agency’s total budget.

A smaller agency is often disadvantaged by poorer economies of scale and limited bargaining power. This affects an agency’s ability to achieve savings in the procurement of goods and services or the negotiation of rental agreements.82

The Committee concluded that ‘there is a definable group of agencies that are being placed in financial difficulty by the combined effect of the efficiency dividend, the indexation measures and the NPP process. This group is defined by their smaller size and their technical, well defined roles’.83 In particular, the JCPAA concluded that the efficiency dividend is inappropriate for cultural agencies ‘holding significant numbers of assets and whose appropriation funding centres on depreciation of those assets’.84 The Committee also noted that ‘[l]arge agencies do better than small agencies in receiving NPP funding, as well as having better economies of scale with which to manage the efficiency incentives’.85

The JCPAA made a number of recommendations including the development of a ‘new funding model for cultural agencies’ and the establishment of a ‘parliamentary commission ... to recommend

80. Ibid.
81. Ibid., pp. 98, 6.
82. Ibid., p. 6.
83. Ibid., pp. 102–103.
84. Ibid., p. 56.
85. Ibid., p. 125.
funding levels for the parliamentary departments in each Budget’. 86 Perhaps the most prominent of the Committee’s recommendations was the exemption of the first $50 million of agency appropriations from the efficiency dividend, either for all agencies excepting the departments of state, or for all agencies with annual departmental expenses of less than $150 million excepting the departments of state. 87 The government did not accept this recommendation in its response. 88

1990s

House of Representatives Standing Committee on Banking, Finance and Public Administration (1994 and 1995)

In 1993–94 the House of Representatives Standing Committee on Banking, Finance and Public Administration (HRSCBFPA) conducted an inquiry into the efficiency dividend. In its 1994 report the Committee canvassed a range of issues relating to the dividend and recommended that it should continue over the medium term while being reviewed. 89 The Committee also concluded that it did ‘not see a long term future for the efficiency dividend in its present form’:

The variable capacity of organisations to meet the efficiency dividend obligations will ensure that some agencies will begin to lose their capacity to maintain the quality of the services that they are meant to provide. It is imperative that alternative approaches be developed to ensure that managers have an incentive to continue search [sic] for efficiencies and to ensure that the government is able to access a portion of those gains for other Budget priorities. 90

The Committee noted workplace bargaining as one possible future alternative to the efficiency dividend and made a number of further recommendations including lowering the annual rate of the efficiency dividend and investigating the development of ‘a process for measuring productivity which takes account of the quality of output in the [APS]’. 91 In its response the government accepted the recommendations to lower the efficiency dividend rate and review the dividend, and also indicated that it would be ‘reexamining [sic] the issues associated with measuring productivity and quality of service’ in the APS. 92

In 1995 the HRSCBFPA revisited the efficiency dividend as part of its broader inquiry into the devolution of running costs flexibilities for agencies. At this juncture the Committee took the view that workplace bargaining constituted ‘an efficient and sophisticated alternative to the efficiency dividend’.

---

86. Ibid., p. xvi.
87. Ibid., p. xvii.
89. HRSCBFPA, Stand and deliver: inquiry into the efficiency dividend arrangements, op. cit., p. 41.
90. Ibid., p. 46.
91. Ibid., pp. 25–28, xv.
dividend’ and recommended that the government investigate this alternative. The Committee also noted the difficulty of measuring efficiency gains and reiterated its recommendation from its 1994 report regarding the investigation of a process for measuring productivity gains. In its response the government agreed to investigate a process for measuring productivity gains and indicated that the recommendation to investigate workplace bargaining as an alternative to the efficiency dividend would be the subject of further consideration.

Management Advisory Board Task Force on Management Improvement (1992)

In 1991–92 the Management Advisory Board’s Task Force on Management Improvement conducted an evaluation of ten years of APS management reform. In its 1992 report the Task Force considered the impact of the efficiency dividend and noted that the difficulty of making efficiency gains can vary among agencies. The Task Force concluded that ‘[t]here is a strong body of opinion that the future of the efficiency dividend lies in resource agreements and workplace bargaining, not in fixed arbitrary annual reductions in running costs’, and that ‘[s]uch an approach could address many of the objections to the existing arrangement’.

House of Representatives Standing Committee on Finance and Public Administration (1990)

In 1989–90 the House of Representatives Standing Committee on Finance and Public Administration conducted an inquiry into financial management aspects of public sector reform. In its 1990 report the Committee considered the efficiency dividend and noted that ‘most departments and agencies have found the discipline of achieving the efficiency dividend difficult’. The Committee concluded that:

---

93. HRSCBFPA, Keeping the customer satisfied: inquiry into the devolution of running costs flexibilities, op. cit., p. 55.
94. Ibid., p. 54.
96. The Management Advisory Board was established under section 22 of the Public Service Act 1922 (Cth) to ‘advise the Commonwealth Government on significant issues relating to the management of the Australian Public Service’ and ‘to be a forum for consideration of major management activities affecting the Australian Public Service as a whole’. Since 1999 the equivalent body, established by section 64 of the Public Service Act 1999 (Cth), has been the Management Advisory Committee.
98. Ibid.
... it is difficult to establish a case that the great majority of departments/agencies are disadvantaged in being required to achieve the ‘efficiency dividend’ given the scope for utilising new managerial flexibilities and technology.100

However, the Committee also recommended that the Finance Department should ‘take careful account of the merits of exceptional cases’ in the application of the efficiency dividend and ‘take steps to improve its marketing’ of the dividend within the public service.101 In its response the government accepted this recommendation.102

**Conclusion**

The efficiency dividend has been a feature of the Commonwealth budgetary landscape for 25 years and appears set to remain in place. The straightforward and predictable nature of the dividend, combined with its effectiveness in returning monies to the Budget, make it an attractive mechanism for governments keen to drive public sector efficiencies and realise the associated benefits. However, consideration of the efficiency dividend by authoritative sources—including the Commonwealth Parliament, the Australian National Audit Office and the Government’s own review of agency efficiency—suggest that the dividend is not without its flaws, and that the mechanisms for driving efficiency warrant further exploration.

100. Ibid.