

VICTORIA

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Auditor-General  
of Victoria

**REPORT ON  
MINISTERIAL PORTFOLIOS  
MAY 1996**

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*Ordered by the Legislative Assembly to be printed*

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May 1996

The President  
The Speaker

Parliament House  
Melbourne, Vic. 3002

Sir

Under the authority of section 15 of the *Audit Act* 1994, I transmit my Report on Ministerial Portfolios. The Report also contains a section on the Parliament of Victoria as well as a section on matters of broad scope interest.

This Report completes the cycle of my auditing activities in relation to the 1994-95 financial year.

Yours faithfully

C.A. BARAGWANATH  
*Auditor-General*



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# Foreword

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In the Foreword to my May 1995 *Report on Ministerial Portfolios*, I referred to the fact that, in future, such Reports issued under the authority of section 15 of the *Audit Act* 1994 will mainly contain matters arising from financial audits conducted by my Office. It has been the practice in the past to produce an omnibus Report covering all Ministerial Portfolios which has traditionally been tabled in the Parliament in May each year. One of the problems encountered by the Parliament, particularly the Public Accounts and Estimates Committee, has been giving due consideration to the number and range of issues included in these Reports. In future, it is therefore proposed that when a major review is undertaken, a separate Report will be prepared and tabled in the Parliament under the authority of section 15 of the Act. The preparation of separate Reports on major reviews should assist the Parliament in the timely deliberation of the relevant issues.

Under the current Government's reform process, outsourcing has become an increasingly important element of the Victorian public sector culture. The risks associated with the management of outsourcing arrangements have been recognised by the Department of Treasury and Finance which recently issued comprehensive guidelines that clearly delineate responsibility and accountability for such arrangements. I have raised with the Department the need for my Office to have full, free and timely access to relevant records of service providers and the need to ensure that such access is provided for in contracts between public sector agencies and service providers.

In recent years, I have been increasingly confronted with claims that information I propose to include in my Reports to the Parliament was regarded as being "commercially confidential", and I am concerned that such claims may escalate as outsourcing of activities to private service providers becomes more prevalent. In responding to such claims in the past I have followed the principle that I expressed in my Report on the 1990-91 Finance Statement:

*"... the issue of commercial confidentiality and sensitivity should not override the fundamental obligation of government to be fully accountable at all times for all financial arrangements involving public moneys".*



I am required by professional auditing standards to respect the confidentiality of information acquired in the course of an audit and not to disclose such information unless there is a legal or professional requirement to do so. The current Audit Act does not provide grounds to exempt allegedly commercially sensitive information from publication. Further, no alternative machinery exists within the parliamentary arena to evaluate the merit of claims that certain material should not be publicly disclosed in reports to the Parliament. It is therefore left to my judgment to decide whether or not claims that material is commercially confidential or sensitive are legitimate and, more importantly, whether or not disclosure of such material is in the public interest.

The Public Accounts Sub-committee in 1992 resolved to provide guidelines setting out the grounds under which public sector agencies could make application to the Committee to have material which agencies regard as commercially confidential or sensitive exempt from publication in an Auditor-General's Report to the Parliament. Unfortunately, these guidelines are yet to be developed and I believe that this is an issue which warrants consideration by the incoming Public Accounts and Estimates Committee.

C.A. BARAGWANATH  
*Auditor-General*



May 1996

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I request that the Report be tabled as soon as possible.

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# Part 1



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# Executive Summary



# Part 1.1

## Major findings

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**1.1.1 Key findings** arising from the audit reviews of ministerial portfolios are highlighted at the beginning of each individual section of this Report. **Major findings** are summarised below.

|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        |                |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------|
| <b>EDUCATION</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       | <b>Page 21</b> |
| <b>Property management at University of Melbourne</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                  |                |
| <ul style="list-style-type: none"><li>• The University of Melbourne owns and manages a property portfolio with a combined land and building valuation of \$1 billion at December 1995, of which the main campus in Parkville accounts for \$767 million. <i>Paras 3.1.30</i></li><li>• Over many years, the University has used a property purchasing strategy which identifies and reacts to acquisition opportunities as they arise. In some cases, when properties are acquired, lengthy delays occur in the determination of an appropriate academic or research related use, resulting in properties being under-utilised or inappropriately utilised for lengthy periods. <i>Paras 3.1.46 to 3.1.47 and Paras 3.1.51 to 3.1.53</i></li><li>• The University should place greater emphasis on rationalising and consolidating its existing stock of property assets and accelerating the sale of marketable properties. <i>Paras 3.1.51 to 3.1.53</i></li><li>• The construction of the University's Information Technology and Electrical Engineering building was part-funded using a leasing arrangement which resulted in the University incurring additional costs of \$5.1 million. <i>Paras 3.1.59 to 3.1.67</i></li></ul> |                |

|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |                |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------|
| <b>HUMAN SERVICES</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                               | <b>Page 63</b> |
| <b>Follow-up review of visiting medical officer arrangements at public hospitals</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                |                |
| <ul style="list-style-type: none"><li>• While a number of public hospitals have made significant steps to improve controls over payments to visiting medical officers (VMOs), further work is needed, particularly in improving the standard of record keeping and adhering to established procedures. <i>Paras 3.2.18 to 3.2.24</i></li><li>• Significant savings can be made by public hospitals moving to revised VMO engagement arrangements, and the Department of Human Services needs to work with hospitals to ensure that uneconomic fee-for-service arrangements do not continue. <i>Paras 3.2.25 to 3.2.30</i></li></ul> |                |



**INFRASTRUCTURE** **Page 87**

**Analysis of Melbourne City Link project**

- The processes adopted for the assessment and selection of the private sector consortium to deliver and operate the Melbourne City Link, which is estimated to cost \$2 billion, were fair and equitable, and resulted in the engagement of Transurban, the consortium which was best suited to deliver the project in accordance with its established scope and objectives.  
*Para 3.3.13 and Paras 3.3.67 to 3.3.117*
- Evidence was not produced to audit in the form of a detailed model, comparing project costings on the basis of private sector financing versus government borrowings.  
*Para 3.3.13 and Para 3.3.91*
- While the users of the City Link via toll payments will in substance be the financiers of the project, Transurban has ultimately accepted substantial risks in relation to the delivery and operation of the project.  
*Para. 3.3.15*
- The obligations of the State in relation to the City Link project are not sufficient to constitute, or support the recognition of, the financing of the project as a debt of the State.  
*Paras 3.3.211 to 3.3.225*
- The Government may implement future traffic enhancement measures over the life of the project which could assist Transurban in enhancing the revenues of the project. However, any revenue generated by these additional traffic management measures will be shared between the State and Transurban.  
*Para 3.3.217*

**Local government reforms**

- Recent reforms to the local government sector have been without parallel in Victoria and are designed to provide a solid foundation for the industry to service the future needs of the community.  
*Paras 3.3.226 to 3.3.286*
- Based on municipal council budgets, savings of \$323 million in operating expenditure will be achieved in the 1995-96 financial year with rate reductions in the order of 18 per cent incorporated into rate notices for the 1995-96 rating period.  
*Paras 3.3.263 to 3.3.266*

**Financial standing of municipal councils on creation**

- Due diligence audits of newly-created municipal councils, conducted at the request of their commissioners, identified a wide range of issues impacting on the financial viability of the former councils, financial exposures inherited by the new councils and inappropriate action by former councils prior to amalgamation.  
*Paras 3.3.287 to 3.3.296*

**Peppercorn rentals for community assets**

- A number of municipal councils had leased certain assets to third parties for nominal rentals even though the assets were utilised by the third parties for commercial purposes, such as gambling venues.  
*Paras 3.3.297 to 3.3.305*



**INFRASTRUCTURE - continued****Page 87****Urban Land Authority property dealings**

- The depressed real estate market in recent years adversely impacted on the value of certain of the Authority's undeveloped land holdings, resulting in a \$10.5 million write-down in the value of these holdings during the 1994-95 financial year, particularly comprising land at Roxburgh Park and Goonawarra Estates.

*Paras 3.3.322 to 3.3.336*

- Due to the disappointing level of sales associated with a joint venture at the Lynbrook Estate, the project incurred a deficit in the 1994-95 financial year of \$284 000 and is projecting to incur a further deficit of \$215 000 in the 1995-96 financial year.

*Paras 3.3.350 to 3.3.354*

- The duplication of services provided by the Authority and other government agencies suggests that scope may exist for some rationalisation, with potential for cost savings and more effective use of available expertise.

*Paras 3.3.355 to 3.3.356***JUSTICE****Page 179****Sheriff's Office - Uncollected fines**

- Despite productivity measures and changes to legislation, the amount of uncollected fines and costs continued to rise.

*Paras 3.4.12 to 3.4.19*

- Over the period 1986-87 to 1994-95, total outstanding fines and costs has grown 9 times from \$41.3 million to \$366.6 million.

*Para 3.4.18*

- At 30 June 1995, outstanding fines and costs totalling \$289.1 million was payable to the State. Of this amount, \$85.1 million has been written-off as bad debts and the collection of \$116.9 million is regarded as doubtful.

*Paras 3.4.21 to 3.4.22*



|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |                 |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------|
| <b>NATURAL RESOURCES AND THE ENVIRONMENT</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          | <b>Page 209</b> |
| <b>Melbourne water industry reform</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                |                 |
| <ul style="list-style-type: none"><li>• While strategies have been developed to reduce the total debt of the Melbourne water industry to approximately \$3 billion by 30 June 1998, the level of debt will continue to have an adverse impact on the industry.<br/><i>Paras 3.5.70 to 3.5.72</i></li><li>• In the absence of appropriate asset management systems to accurately assess maintenance requirements, projected maintenance expenditure for the Melbourne Water Corporation and the retail water companies may be understated.<br/><i>Paras 3.5.93 to 3.5.98</i></li></ul> |                 |

|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                            |                 |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------|
| <b>PREMIER AND CABINET</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 | <b>Page 241</b> |
| <b>Executive salaries</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                  |                 |
| <ul style="list-style-type: none"><li>• Executive officer contracts were generally entered into and administered in accordance with the guidelines issued by the Public Service Commissioner.<br/><i>Paras 3.6.4 to 3.6.10</i></li><li>• Payments of \$70 581 were made to a former senior public servant in excess of contract entitlements.<br/><i>Paras 3.6.11 to 3.6.13</i></li><li>• While certain public servants in the past have received approval to be members of non-Victorian public bodies, it is my opinion that only in extenuating circumstances should such appointments be approved and that government employees should not personally benefit from such arrangements.<br/><i>Para. 3.6.14</i></li><li>• In my view, the provision of a gift valued at \$9 500 to a senior public servant upon departure from the Victorian public service was extravagant.<br/><i>Paras 3.6.15 to 3.6.16</i></li></ul> |                 |

**Gas industry reform in Victoria**

- The aggregate costs incurred by the State on the gas industry reform process to 31 March 1996 were around \$11 million. *Paras 3.8.4 to 3.8.9*
- On the split-up of the Gas and Fuel Corporation of Victoria, net liabilities of \$54.4 million, together with certain other substantial contingent liabilities, were not allocated to the newly established gas entities but were transferred to the SECV. *Paras 3.8.10 to 3.8.27*

**Victorian electricity industry privatisation**

- The processes followed for the sale of the 5 distribution businesses were appropriate to ensure that the best available result was achieved by the State, with fair and equitable treatment accorded to all bidding parties. *Paras 3.8.39 to 3.8.65*
- The estimated cost directly incurred by the State in relation to these sales was in the order of \$40 million, with further indirect costs relating to electricity privatisation of \$5 million. *Para. 3.8.69*
- The net benefit to the State from the sale of the 5 distribution companies is around \$4.1 billion. *Paras 3.8.67 to 3.8.69*
- Based on established projections, the sale of the distribution companies will result in a positive cashflow to the State over future years estimated to be around \$350 million a year. *Paras 3.8.81 to 3.8.83*
- Under the sale arrangements, the State has provided certain indemnities and warranties to the purchasers, and has retained certain financial obligations, which may expose the State to future liability and cost. One of these liabilities relates to an agreement by the State to ultimately bear the financial costs of the companies' sales tax obligations estimated at \$35 million a year. *Paras 3.8.84 to 3.8.98*

**Final audit of United Energy Ltd**

- A qualified audit opinion was issued under the *Audit Act* 1994 by the Auditor-General on the financial statements of United Energy Ltd for the year ended 30 June 1995. *Para. 3.8.106*
- The financial statements of United Energy Ltd do not reflect the reality of its financial activities and position due to the inappropriate inclusion by the company, after its sale, of provisions and related expenditure totalling \$70.9 million. Had this amount not been provided for, the company would have reported an operating profit after tax of \$44.9 million. *Paras 3.8.107 to 3.8.121*



**Final audit of United Energy Ltd - continued**

- United Energy Ltd was able to obtain a confirming audit opinion under the *Corporations Law* only after taking action to remove the Auditor-General as *Corporations Law* auditor at the time when the company was aware that its financial statements were likely to be qualified.

*Paras 3.8.122 to 3.8.126*

**Victorian Funds Management Corporation**

- The failure of the Corporation to attract the majority of public sector investment funds into its pooled trust products has meant that the expected benefits to the State from the Corporation's establishment, of between \$16 million and \$24 million a year, have not been realised.

*Paras 3.8.128 to 3.8.134*

- Since the restructure of the Corporation's Board in November 1995, various initiatives have been commenced to establish appropriate products and structures for the Corporation. The effective implementation of these initiatives will be vital to the ongoing viability of the Corporation and to the achievement of cost-efficiencies to the public sector from centralised funds management.

*Paras 3.8.157 to 3.8.166*

**Utilisation of property**

- While a strategic plan for the management of the State's leased and owned accommodation in the Melbourne central business district and city fringe has been prepared, the plan does not incorporate a costed long-term preventative maintenance program.

*Paras 3.8.185 to 3.8.190*

- While the condition of some Treasury Reserve properties has been improved by recent renovation works, significant future funding allocations are still required to arrest ongoing deterioration and to enable further improvement in property utilisation.

*Para. 3.8.220*

- There has been a substantial deterioration in the average space allocation per public servant since the last audit review in 1990, indicating continuing inefficient utilisation of accommodation.

*Paras 3.8.193 to 3.8.197*

- Audit identified "dead rent", i.e. actual or imputed rent incurred on vacant accommodation space of a lettable size, amounting to \$12 million for the 18 month period to December 1995.

*Paras 3.8.210 to 3.8.218*

**Financial standing of WorkCover**

- When the Government announced the reforms to WorkCover, it anticipated that the scheme would be fully-funded within 5 years of its inception, i.e. it would have sufficient funds to fully cover all outstanding liabilities by December 1997. However, this milestone has been achieved by 30 June 1995, some 2½ years ahead of that anticipated.

*Paras 3.8.256 to 3.8.260*

- The key reasons for the early achievement of the scheme's fully-funded status and the resulting reduction in premiums included a change in the established entitlement criteria and benefit structure to compensate claimants for injuries sustained in the workplace, which effectively constrained compensation available to workers, the introduction of premium incentives and a change in the strategic management of the scheme.

*Paras 3.8.261 to 3.8.277***Utilisation of consultants in the public sector**

- Given that some agencies did not comply with the annual reporting requirements relating to disclosure of consultancy services, it is important that action be taken by the Department of Treasury and Finance to re-inforce the reporting requirements and therefore improve disclosure to the Parliament in future years.

*Paras 3.8.295 to 3.8.297***Amendment to the casino licence**

- The Government allowed Crown Casino Ltd to increase the number of gaming tables at the new Casino from 200 to 350 for an additional licence fee of \$85 million.

*Paras 3.8.303 to 3.8.320*

- The Department of Treasury and Finance estimated that the additional profit over and above a return on investment to Crown Casino Ltd from the additional 150 tables was between \$194 million and \$259 million (in present value terms), prior to the payment of the additional licence fee. However, there was inadequate support provided to audit for the Department's decision for Crown to retain any of these monopoly profits.

*Paras 3.8.321 to 3.8.324*



**Women in public office**

- While it is essential that selection processes be equitable and based on merit, there is scope for a higher representation of women on Boards of Management and in Chief Executive Officer positions within public sector agencies.

*Para 4.1.1*

- Of the agencies examined, 32 agencies (or 12 per cent) did not have a woman on their Board of Management.

*Para 4.1.11*

- The proportion of Chief Executive Officer positions held by women increased from 5.2 per cent in 1991 to 9.6 per cent in 1995.

*Para 4.1.13*

**Outsourcing information technology**

- A formal business case to justify the decision to outsource the information technology functions of VicRoads and the Public Transport Corporation (PTC) was not prepared.

*Paras 4.2.25 to 4.2.30*

- The PTC paid the outsourcer approximately \$2.2 million in the first year of the contract for services that were not required.

*Paras 4.2.100 to 4.2.101*

**Financial accountability in the Victorian public sector**

- The timely finalisation of asset valuations will assist in ensuring that the benefits of introducing accrual accounting are realised, particularly in relation to effective asset management.

*Paras 4.3.20 to 4.3.29*

- From a public accountability perspective, consideration needs to be given to enhancing the current reporting requirements to require reporting entities to provide greater disclosure of revenues and expenditures within their financial statements.

*Paras 4.3.32 to 4.3.34*

- Agencies now have an option as to the method of disclosure to be used for government contributions utilised for capital acquisitions which could lead to inconsistencies in financial reporting and may hinder inter-period and inter-agency comparisons.

*Paras 4.3.39 to 4.3.42*

- It is desirable that audit committees within departments consist of a majority of external representatives in order to maintain a reasonable degree of independence and separation from management influence.

*Paras 4.3.51 to 4.3.53*

# Part 2



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# Parliament of Victoria



# Part 2.1

## Parliament of Victoria

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### KEY FINDING

- The audit of the financial statements of the Parliament of Victoria proved satisfactory.







**PARLIAMENT OF VICTORIA**

**2.1.1** The audit of the financial statements of the Parliament of Victoria proved satisfactory.

**SCHEDULE A  
COMPLETED/INCOMPLETE AUDITS**

| <i>Entity</i>           | <i>Financial year ended</i> | <i>Reporting to Parliament</i> | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|-------------------------|-----------------------------|--------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS</b> |                             |                                |                                              |                                        |
| Parliament of Victoria  | 30 June 1995                | No reporting requirements.     | 30 Oct. 1995                                 | 30 Oct. 1995                           |

# Part 3



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## Audit of Ministerial Portfolios



# Part 3.1

## Education

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### KEY FINDINGS

#### **Asset management in primary and secondary schools**

- The Directorate of School Education (DSE) is responsible for 1 722 primary and secondary schools which control assets with a total value of \$652 million.  
*Para. 3.1.4*
- In view of the poor stocktaking procedures in schools visited by audit the Directorate needs to reinforce to all schools the requirement for regular stocktakes of assets.  
*Paras 3.1.21 to 3.1.22*
- The Directorate needs to implement procedures that will provide quality assurance over asset data recorded in schools.  
*Paras 3.1.23 to 3.1.25*

#### **Property management at University of Melbourne**

- The University of Melbourne owns and manages a property portfolio with a combined land and building valuation of \$1 041 million at December 1995, of which the main campus in Parkville accounted for \$767 million.  
*Para. 3.1.30*
- The University has established a master plan to guide the placement of buildings for both the long and short-term, together with an annual capital management plan.  
*Paras 3.1.36 to 3.1.44*
- Over many years, the University has used a property purchasing strategy which identifies and reacts to acquisition opportunities as they arise. In some cases, when properties are acquired, lengthy delays occur in the determination of an appropriate academic or research related use. Consequently, audit identified substantial areas of valuable campus fringe properties which had been under-utilised or inappropriately utilised for lengthy periods.  
*Paras 3.1.46 to 3.1.47  
and Paras 3.1.51 to 3.1.53*



**KEY FINDINGS** - *continued*

**Property management at University of Melbourne** - *continued*

- The University should place greater emphasis on rationalising and consolidating its existing stock of property assets, including the acceleration of the sale of marketable properties, and reduce its focus on the expansion of the property portfolio. In addition, the University should implement an internal user charging system to act as an incentive to ensure the economical use of existing properties and requests for additional space.  
*Paras 3.1.51 to 3.1.53*
- The construction of the University's Information Technology and Electrical Engineering building was part-funded using a leasing arrangement which resulted in the University incurring additional costs of \$5.1 million.  
*Paras 3.1.59 to 3.1.67*
- The University has 66 lecture theatres on or near the main campus. The existing uneven pattern of lecture theatre usage, including low utilisation during early morning and mid to late afternoon on weekdays and in particular on Fridays, creates an artificial need for a larger stock of lecture theatres than would otherwise be the case. Limited lecture theatre usage outside the teaching day was also identified by audit.  
*Paras 3.1.88 to 3.1.90*
- A more even spread of lecture theatre usage during the teaching day could free up an amount of valuable main campus space for other uses. In addition, the utilisation of existing lecture theatres could be improved through appropriate marketing and related activities, greater use of summer courses and continuing education programs involving part-time studies.  
*Paras 3.1.91 to 3.1.95*



**3.1.1** Two Ministers, namely, the Minister for Education and the Minister for Tertiary Education and Training have responsibility for operations within the Education sector. These Ministers have collective responsibility for the Department of Education.

**3.1.2** Details of the specific ministerial responsibilities for public bodies within the Education sector are listed in Table 3.1A. These public bodies, together with the Department of Education, were subject to audit by the Auditor-General during 1994-95.

**TABLE 3.1A  
MINISTERIAL RESPONSIBILITIES FOR  
PUBLIC BODIES WITHIN THE EDUCATION SECTOR**

| <i>Ministerial portfolio</i>           | <i>Entities subject to audit</i>                                                                                                                                                                                                                                                       |
|----------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Education</b>                       | Board of Studies<br>Telematics Course Development Fund Trust<br>Victorian Education Foundation<br>Victorian Education Foundation Pty Ltd                                                                                                                                               |
| <b>Tertiary Education and Training</b> | Adult, Community and Further Education Board<br>Council of Adult Education<br>State Training Board<br>Post-secondary education institutions -<br>8 universities and 42 associated companies, trusts<br>and foundations<br>24 colleges/institutes of technical and further<br>education |

**3.1.3** Comment on matters of significance arising from the audit of the Department of Education and public bodies within the Education sector is provided on the following pages.

## ASSET MANAGEMENT IN PRIMARY AND SECONDARY SCHOOLS

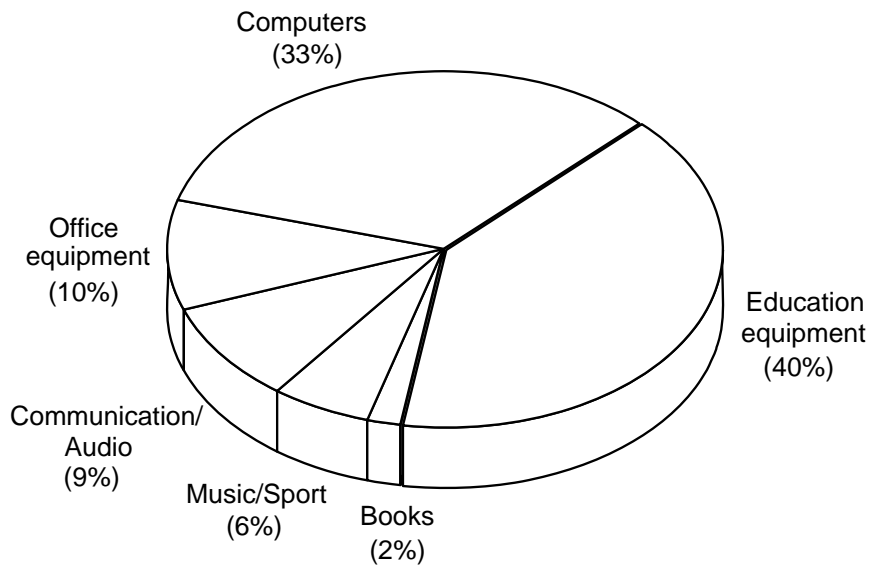
### BACKGROUND

**3.1.4** The Directorate of School Education (DSE) is responsible for 1 722 government primary and secondary schools, each of which has a school council responsible for the management of the Directorate-approved school charter. Collectively, these schools control assets with a total value, as estimated by DSE, of \$652 million. This value excludes land and buildings, which are centrally controlled by DSE, and the majority of school furniture.

**3.1.5** The Government's main initiative in the education portfolio has been the *Schools of the Future* program, the thrust of which has been to devolve greater autonomy to school councils, including the responsibility for asset management, while still requiring appropriate accountability. As fixed assets represent a significant investment by schools in meeting their objectives, sound asset management is essential.

**3.1.6** Chart 3.1B sets out a diagrammatic representation of the overall asset portfolio within government schools.

**CHART 3.1B  
ASSET PORTFOLIO WITHIN GOVERNMENT SCHOOLS**



**Previous audit reviews**

**3.1.7** The Auditor-General's May 1993 *Report on Ministerial Portfolios* drew attention to the fact that a large proportion of school asset registers were inadequate or incomplete, and that the poor standard of asset recording resulted from the lack of departmental support in providing computer assistance to schools. At a school level, there was an absence of computerised asset registers that were integrated with a centralised information system.

**3.1.8** The Directorate responded that this position would improve through the integration of the Computerised Administrative System Environment (CASES), which had been developed specifically for schools as part of *Schools of the Future* program, with the DSE's School Asset Management System (SAMS).

**3.1.9** The May 1993 *Report of the Victorian Commission of Audit* referred to the fact that while many public sector organisations were poorly managing existing assets, they were still making considerable investment in new assets. Following that report, the Victorian Government developed a *Management Improvement Initiative*, including the development of a manual entitled the *Asset Management Series* outlining the principles, policies and practices for sound asset management in the public sector.

**Directorate of School Education review**

**3.1.10** The Office of Schools Review (OSR), a unit within DSE, contracts private sector auditors to conduct an annual audit of each school, including a review of asset management. The 1994 audits highlighted a high number of deficiencies in internal control over fixed assets with a total of 922 schools (53 per cent) having shortcomings in asset management, such as deficient asset registers, irregular stocktakes and poor identification of assets.

.....

**3.1.11** Deficiencies arising from each audit were reported to the relevant school council by the auditors. The OSR reported to the Director of DSE the consolidated results of the school audits and also brought to the attention of the Regional General Managers those schools identified as having serious deficiencies.

### School Asset Management System

**3.1.12** The Directorate's School Asset Management System (SAMS) system enables the Directorate to maintain global management over the total asset base throughout all government schools. Previously, SAMS could only be updated through the manual transfer of data from schools, but in 1994 SAMS was upgraded to allow asset data in CASES to be electronically transferred to SAMS with transfers being initiated by the schools.

### Actions undertaken by DSE

**3.1.13** As a result of the matters raised in various audit reviews in respect of asset management in schools, a number of initiatives were implemented by DSE which included the following:

- CASES has been programed to record all purchases from specified school accounts as fixed assets, unless the school indicates otherwise;
- A prompt has also been programed in CASES which alerts schools to the need to transfer new data to SAMS within one month of purchase. An additional prompt occurs when a school has not updated SAMS and when CASES indicates there have been no asset purchases for 3 months.
- DSE instructed its insurance agents not to pay insurance claims by schools unless the details of assets lost were recorded on SAMS; and
- OSR issued an *Internal Control* booklet, covering asset management, to assist schools in developing best practice in financial management.

**3.1.14** The initiatives undertaken by the Directorate are seen by audit as a positive move in encouraging better asset management at the school level.

## AUDIT'S 1996 REVIEW OF ASSET MANAGEMENT AT SCHOOLS

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**3.1.15** In view of past audit reports and the initiatives undertaken by DSE, it was considered timely for audit to review the current status of asset management in schools. The review included rural and metropolitan primary and secondary schools within Victoria.

**3.1.16** While audit noted some improvement in the control of fixed assets when compared with the last review in 1993, a number of shortcomings relating to acquisition procedures and asset control were found. These matters are discussed below.



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## Acquisition procedures

**3.1.17** DSE policy requires schools to obtain written quotes for purchases over \$2 000 and tenders for purchases over \$50 000. Audit found that 81 per cent of schools examined did not obtain written quotes for purchases in accordance with the policy. DSE has advised audit that the lower threshold (\$2 000) will increase to \$5 000 in 1996. However, audit testing indicated that even if this policy had been applicable in 1995, 80 per cent of schools would still not have complied with the policy.

**3.1.18 To ensure cost-effectiveness and propriety in respect of new acquisitions, audit recommended that the policy be reiterated by DSE to all schools and that DSE conduct random compliance checks.**

*□ RESPONSE by Secretary, Department of Education*

*The DSE is finalising a Schools of the Future manual. The requirement for schools to obtain quotations for the purchase of goods and services is re-affirmed in this manual. In addition, instructions in accordance with audit recommendations will be forwarded to all schools.*

## Asset control

### Data transfer

**3.1.19** As indicated in paragraph 3.1.13, schools are required to transfer data held in the CASES asset module to SAMS on a regular basis. DSE management reports showed that:

- at 31 December 1995, 448 schools (26 per cent) had not transferred data for up to 3 months including 70 schools (4 per cent) which had not transferred data for 6 months; and
- by 10 April 1996, there had been a further deterioration in that 798 schools (47 per cent) had not transferred data in the last three months including 220 schools (13 per cent) which had not transferred data for 6 months.

**3.1.20** These figures indicate that, under current departmental policy, it is most likely that a number of new assets purchased by schools are not covered by insurance, therefore exposing schools to risk of unnecessary financial loss. **To limit this exposure, DSE needs to periodically review management reports and implement follow-up procedures aimed at ensuring that schools regularly update the SAMS database.**

*□ RESPONSE by the Secretary, Department of Education*

*The DSE does not agree that "a number of new assets purchased by schools would not be covered by insurance", as this assumes that the schools that have not submitted data have purchased assets worth more than \$500 in that time. However, DSE will consider modifications to CASES so that it automatically updates SAMS when a new asset over \$500 is recorded/purchased. As well, SAMS will be modified to automatically produce regular reports indicating schools that have not submitted new data by a specified period of time.*

.....

### Stocktaking procedures

**3.1.21** Audit examined stocktaking procedures at schools visited and found that:

- only 23 per cent of schools conducted regular stocktakes;
- while stocktakes had been performed by 33 per cent of schools they had only done so on becoming aware of the proposed audit visit;
- there was no record of a stocktake ever being performed in 29 per cent of schools;
- 15 per cent of schools had not performed a stocktake since 1994;
- the effects of not undertaking regular stocktakes was evident in that 52 per cent of schools had inaccuracies in the information contained in their asset registers; and
- individual assets had not been given a unique identification, such as a bar coded or engraved number, in 71 per cent of schools.

**3.1.22** In view of the poor state of stocktaking procedures in the schools visited, DSE needs to reinforce to all schools that regular stocktakes need to be undertaken in order to identify missing or surplus assets.

*□ RESPONSE by Secretary, Department of Education*

*The audit findings are acknowledged. Instructions will be issued to all schools in accordance with the audit recommendations.*

### Asset valuations

**3.1.23** As DSE is moving to full accrual accounting in respect of its 1995-96 financial statements, all assets are required to be identified and accurately valued. Audit found a number of anomalies in the values attached to assets recorded on CASES, which audit has been advised will be used to determine the asset values to be included in DSE's financial statements. The anomalies included:

- 25 per cent of schools did not assign any value to the majority of assets recorded on CASES; and
- other schools had excessively overvalued a number of assets, e.g. 30 calculators valued at \$22 million and a desk valued at \$1 billion. In response to the audit findings, DSE identified further assets with excessive valuations.

**3.1.24** The failure to assign values to individual assets understates the value of assets to both the school community and for financial reporting purposes. Similarly, overstatement of asset values renders meaningful analysis impossible.

**3.1.25** DSE needs to interrogate the current database to identify assets that have incorrect values and implement edit procedures that will, in the future, provide quality assurance over the input of data at schools.



**□ RESPONSE by Secretary, Department of Education**

*The DSE will introduce a number of changes to CASES which will assist in alleviating the problem. First, CASES will be modified so that it will not be possible to input a zero or null value in the purchase cost field. Second, a prompt will be included that questions the operator where the value being input is greater than a predetermined value to ensure that unrealistic values are checked.*

**Classroom furniture**

**3.1.26** Apart from the school building, classroom furniture would be the most significant class of asset required for a school to be able to operate. DSE policy is that schools are not to include these items in their asset registers.

**3.1.27** The audit review identified inconsistencies in compliance with the policy in that a minority of schools recorded and valued these assets in their registers. By excluding classroom furniture the value of assets in DSE's financial statements will be understated and school councils will not have complete asset information for decision-making purposes.

**3.1.28** **It is audit's view that the Directions under the *Financial Management Act 1994*, Australian Accounting Standards and general business practice would require such assets to be valued and included in the balance sheet, and there is a need for the Directorate's current policy to be re-examined.**

**□ RESPONSE by Secretary, Department of Education**

*The Accrual Accounting Manual issued by the Department of Finance in February 1995 indicated that assets with a value of \$1 000 or more must be recorded in an asset register or where the asset or group of similar assets would be material to the accounts of the Department or if the replacement value of all assets at a location exceeds \$250 000.*

*Given that the replacement value of desks and chairs in the average primary school would not exceed \$30 000, this group of assets is not considered material to the accounts of the Department.*

**Overall conclusion**

**3.1.29** Audit acknowledges that improvements have taken place in asset recording since the introduction of CASES, however, there are still important asset management issues at schools which have existed for a number of years and need to be addressed. Schools need to recognise the significant investment made in assets and accordingly manage the assets individually and collectively in a responsible way. The apparent low priority assigned to asset management principles by schools threatens the effective implementation and underlying principles of the *Schools of the Future* philosophy of self-autonomy. To ensure the *Schools of the Future* program is not compromised it is necessary for schools to achieve a balance between educational leadership, and contemporary approaches to governance and managerial responsibility.



## PROPERTY MANAGEMENT AT UNIVERSITY OF MELBOURNE

### Overview of University of Melbourne's property portfolio

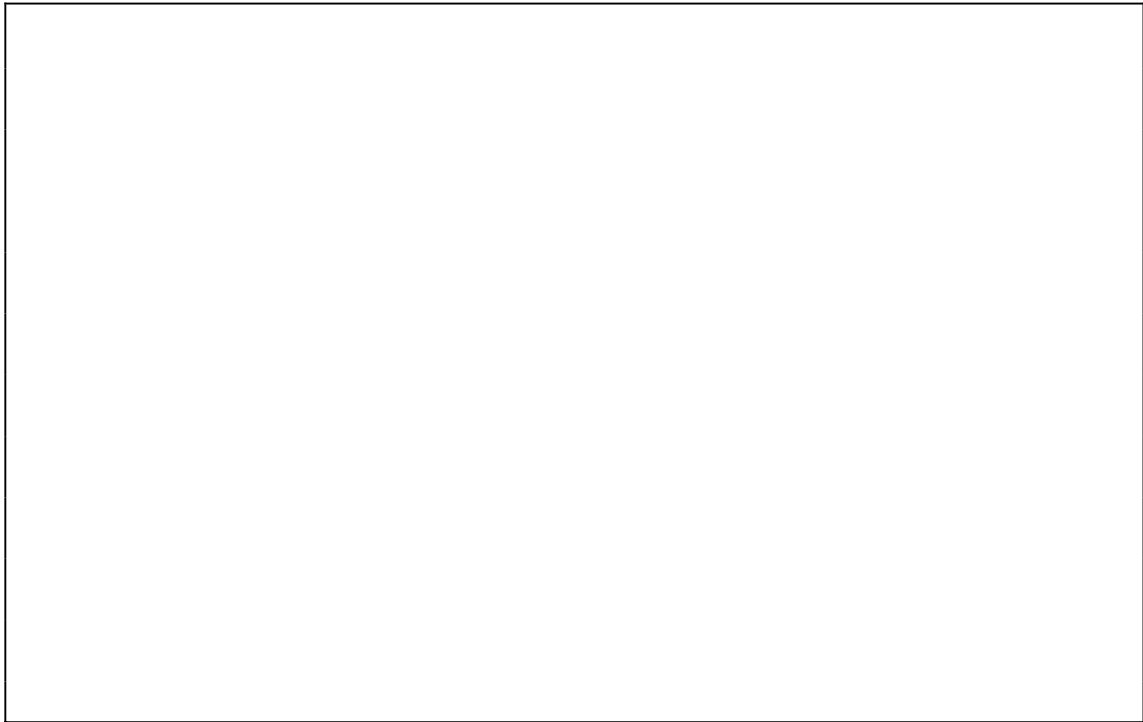
**3.1.30** The University of Melbourne owns and manages 464 buildings with a combined land and building value in excess of \$1 billion. These buildings are located both on the main campus in Parkville as well as a number of other locations throughout the State. The age and condition of these buildings varies significantly as do the roles they fulfil. Table 3.1C lists details of the University's property portfolio.

**TABLE 3.1C  
MELBOURNE UNIVERSITY'S PROPERTY PORTFOLIO**

| <i>Property/Location</i>                                                                                                                  | <i>Number of buildings</i> | <i>1995 valuation</i> |
|-------------------------------------------------------------------------------------------------------------------------------------------|----------------------------|-----------------------|
|                                                                                                                                           |                            | (\$'000)              |
| Main Campus (excluding residential colleges)                                                                                              | 81                         | 767 388               |
| Carlton and Parkville - non-residential style properties                                                                                  | 21                         | 106 626               |
| Victorian College of Agriculture and Horticulture                                                                                         | 149                        | 48 240                |
| Student and staff houses (Carlton, Parkville, Brunswick, Collingwood and Fitzroy) and Halls of Residence (excluding residential colleges) | 37                         | 28 551                |
| Royal Dental Hospital and Annex                                                                                                           | 2                          | 20 081                |
| Carlton and Parkville - residential style properties                                                                                      | 51                         | 19 612                |
| "South Telecom" site, which is occupied by the Victorian College of the Arts, an affiliate of the University                              | 1                          | 12 862                |
| "North Telecom" site                                                                                                                      | 6                          | 7 707                 |
| Veterinary Precinct, Parkville                                                                                                            | 3                          | 7 496                 |
| Werribee Veterinary School                                                                                                                | 22                         | 7 419                 |
| Melbourne Theatre Company                                                                                                                 | 2                          | 3 992                 |
| Mount Derrimut Field Station                                                                                                              | 60                         | 3 957                 |
| Strathfieldsaye Estate                                                                                                                    | 13                         | 1 700                 |
| MacGeorge Estate, Ivanhoe                                                                                                                 | 2                          | 1 519                 |
| School of Forestry, Creswick                                                                                                              | 2                          | 956                   |
| Melbourne University Ski Facility, Mt Buller                                                                                              | 1                          | 582                   |
| Melbourne University Boat House                                                                                                           | 1                          | 373                   |
| Other                                                                                                                                     | 10                         | 1 567                 |
| <b>Total</b>                                                                                                                              | <b>464</b>                 | <b>1 040 627</b>      |



**3.1.31** By way of comparison, the University of Sydney had land and buildings valued at \$866.1 million and the University of Adelaide had land and buildings valued at \$295.4 million at December 1994.



*University of Melbourne, main campus.*

**Staff and student housing**

**3.1.32** The University owns 28 residential houses for student housing (valued at \$5.6 million in December 1995), 3 halls of residence (valued at \$21.4 million in December 1995) and a further 9 houses for temporary staff accommodation (valued at \$1.5 million in December 1995). Many properties are located in the Carlton/Parkville area, although a number are also located in outlying suburbs. In addition, student accommodation is available at 10 residential colleges.

**Residential colleges**

**3.1.33** There are 10 residential colleges affiliated with the University which occupy a substantial area adjacent to the main campus. The colleges are independently governed and owned, consequently, they are not included in Table 3.1C. The 10 residential colleges are:

- Trinity College;
- Ormond College;
- Queen's College;
- Newman College;
- St Mary's College;
- University College;

- St Hilda's College;
- Whitley College;
- Janet Clarke Hall; and
- Ridley College.

### Property and Buildings Department

**3.1.34** The Property and Buildings Department of the University of Melbourne maintains and services the physical amenities of the University. It has a total staff complement of more than 200 and was allocated a recurrent budget for 1995-96 of \$10.2 million. The Department's responsibilities include:

- building construction, refurbishment and maintenance;
- mechanical services and energy management;
- grounds landscaping and maintenance;
- cleaning;
- security and building supervision;
- parking and traffic management;
- space and property planning and management;
- conference management and audio-visual support;
- hiring of facilities;

### Audit review of property management by the University of Melbourne

**3.1.35** The overall objective of the audit review was to provide information and recommendations for the more effective, efficient and economic management of property by the University of Melbourne with special regard to:

- strategic planning and policy;
- utilisation of property; and
- information systems and performance management.

## STRATEGIC PLANNING

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### Master Plan

**3.1.36** In 1971, the Council of the University adopted the *Master Plan Report 1970*. This report had the stated aim of providing guidance in the placement of buildings with specific plans for both the long-term and short-term, based on a survey and analysis of existing conditions and future trends. The Report noted that "... *there is a limit beyond which it [the University] should not be allowed to spread, no matter how much land is available*". The Report concluded that, overall, the University needed more land and as such the site should be expanded wherever possible. The Report showed projected development by triennial stages up to 1985.

*Master Plan Report 1981*

**3.1.37** The Master Plan Report 1981 reviewed developments within the University grounds since the 1970 Report. The Report noted that the University needed more land partly because, in the shorter-term, existing building sites were unavailable for redevelopment. The sites were occupied by existing low-density buildings which were either not at the end of their economic life or they could not be removed until new space was available for decanting. Further, other buildings were protected by historic, aesthetic or sentimental values.

**3.1.38** The Plan endorsed the University's intention to consolidate its site acquisitions in 2 areas of Carlton, namely, the area across Swanston Street from the main campus and the South Carlton area across Grattan Street from the main campus.

*Master Plan Report 1991*

**3.1.39** The main development of the Master Plan Report 1991 was the integration of the education precinct into the Master Plan and the Recreation Grounds Reserve. This resulted from the amalgamation of the University with the Melbourne College of Advanced Education, which has now been incorporated into the University grounds as the Institute of Education.

**3.1.40** The 1991 Report also referred to the creation of the "*Knowledge Precinct*", south of the University. This was one of 6 high technology precincts created by the then State Government in 1987. These precincts were intended to facilitate the transfer of technology by higher education institutions to "spin-off" companies created to convert research ideas into manufactured or saleable items.

*Departmental master plans*

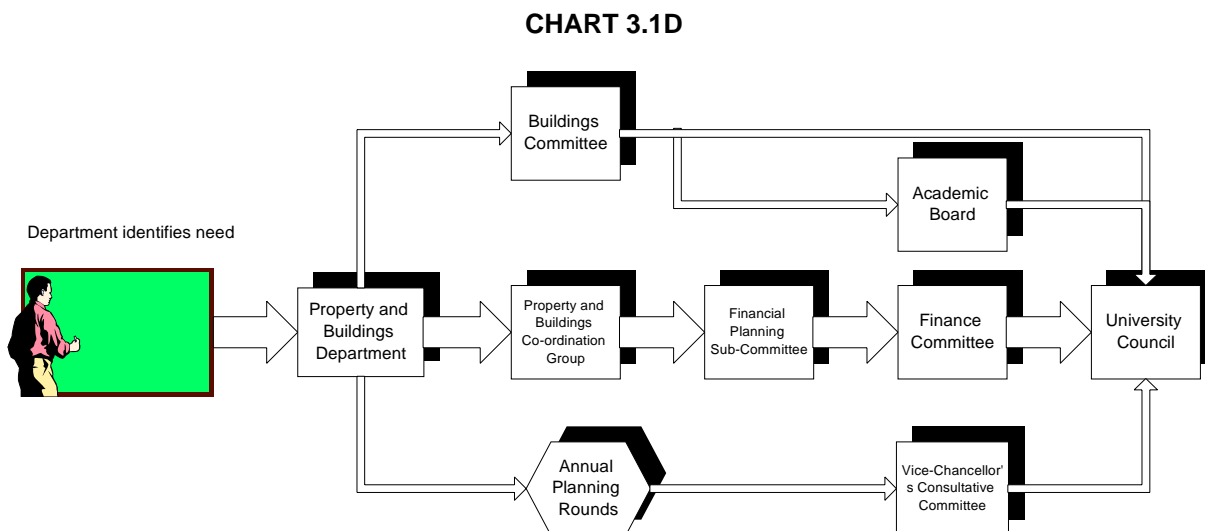
**3.1.41** In order to facilitate the planning process, a number of the University's departments have, from time to time, produced their own planning reports covering a medium term of approximately 5 years.

**Annual Capital Management Plan**

**3.1.42** The University prepares an annual Capital Management Plan. The Capital Management Plan is devised after an examination of both immediate space requirements and long-term strategic directions. Several key factors are taken into account in the preparation of the Plan, including approved plans for academic development and growth, planned shifts in the balance and location of the student load, and likely changes in the styles of teaching and research. The 1995 Capital Management Plan included cash flow projections.

Annual planning process

**3.1.43** Several groups or committees are involved in the annual capital planning processes as outlined in Chart 3.1D.



**3.1.44** Audit was advised at the time of its review that the then existing structure of the University and its many committees were undergoing revision. A rationalisation of the groups or committees involved in the annual planning processes and the planning process itself could realise substantial efficiencies for the University.

**□ RESPONSE** provided by Registrar, University of Melbourne

*The revised Governance Structure of the University was implemented by Council on 1 April 1996. The conclusion drawn in this report concerning the planning process of the University is unsubstantiated.*

## PROPERTY UTILISATION

### Introduction

**3.1.45** In order to provide an indication of the extent to which property assets are being used by the University, the review considered overall utilisation of properties off the main campus (valued at \$273 million at December 1995) and utilisation of lecture theatres on campus. The utilisation of properties has been considered in the light of an asset's potential capacity and the extent to which its current usage contributes to the University's objectives.

### Underutilised and inappropriately utilised properties

**3.1.46** Over many years, the University has purchased a number of city fringe properties as part of an expansion off the campus proper into Parkville, Carlton and surrounding areas, particularly to the south of the University. The majority of these purchases have been consistent with the University's broad strategic directions for expansion, as set out in its master plan.





**3.1.47** The audit review has identified a number of underutilised or inappropriately utilised properties which are summarised in Table 3.1E. The underutilised or inappropriately utilised nature of these properties is a consequence of several factors, including:

- a long-term purchasing strategy which identifies and reacts to acquisition or development opportunities as they arise; and
- very lengthy delays in some cases in the determination of an appropriate academic or research-related use for such properties.

**TABLE 3.1E  
UNDERUTILISED OR INAPPROPRIATELY UTILISED PROPERTIES**

| <i>Property<br/>(valuation at December 1995)</i>                                                                  | <i>Usage</i>                                                                                                                                                                          |
|-------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 234 Queensberry Street, Carlton<br>(\$13 448 800)                                                                 | Ground floor and most of the 2nd and 3rd floors, of a total of 6 floors, have been mostly vacant since purchased in 1993.                                                             |
| 207-221 Bouverie Street, Carlton<br>(\$32 303 100)                                                                | Since construction in 1993, approximately 2½ levels of a total of 6 levels were vacant until March 1996.                                                                              |
| 119-129 Barry Street, Carlton<br>(\$1 692 200)                                                                    | Housing of archives since 1982.                                                                                                                                                       |
| 168 Leicester Street, Carlton<br>(\$937 000)                                                                      | Housing of archives since 1977, pending redevelopment.                                                                                                                                |
| 164-170 Pelham Street, Carlton<br>(\$453 400)                                                                     | Used to store furniture since 1991, pending redevelopment.                                                                                                                            |
| 176-180 Leicester Street, Carlton<br>(refer 193-195 Bouverie Street,<br>Carlton which is a combined<br>valuation) | Used to store furniture and archives. Partially vacant since 1994, pending redevelopment.                                                                                             |
| 193-195 Bouverie Street, Carlton<br>(\$1 856 800)                                                                 | Purchased in 1994, vacated by a private tenant during 1995, awaiting redevelopment.                                                                                                   |
| 864 Swanston Street, Carlton<br>(\$286 900)                                                                       | Mainly vacant since 1986.                                                                                                                                                             |
| 375 Cardigan Street, Carlton<br>(\$120 400)                                                                       | Used to store geological rocks since 1976, pending redevelopment.                                                                                                                     |
| 351 Cardigan Street, Carlton<br>(\$191 400)                                                                       | Vacant since 1994 pending redevelopment, previously used by the Mountaineering Club since 1989.                                                                                       |
| "North Telecom" site, South<br>Melbourne (\$7 706 900)                                                            | Site acquired in 1991 and includes vacant buildings, vacant land and some commercial tenants. Part of the site is used temporarily, at no cost, by the Victorian College of the Arts. |

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*Marketable properties*

**3.1.48** As part of the ongoing planning and analysis of the property portfolio the University's Property and Buildings Department identified, during 1995, a number of properties valued at \$31.7 million which it has categorised as "marketable properties". Marketable properties represent a source of funding for property development as required. These properties, with the exception of the North Telecom site, are in addition to the underutilised or inappropriately utilised properties identified by audit in Table 3.1E.

**3.1.49** Audit was advised that the existence of marketable properties within the portfolio has arisen due to a number of factors including:

- amalgamations with other educational institutions;
- changed course structures; and
- changed technology.

**3.1.50** The Department has categorised its listing of marketable properties according to their possible availability for sale, refer Table 3.1F.

**TABLE 3.1F  
LISTING OF MARKETABLE PROPERTIES**

| <i>Property</i>                                                   | <i>Market value</i> | <i>Current use</i>                            | <i>Immediate sale (1-2 yrs)</i> | <i>Medium-term sale (5 yrs)</i> | <i>Long-term sale (10 yrs)</i> |
|-------------------------------------------------------------------|---------------------|-----------------------------------------------|---------------------------------|---------------------------------|--------------------------------|
|                                                                   | (\$'000)            |                                               |                                 |                                 |                                |
| Various properties in Carlton, Fitzroy, Brunswick and Collingwood | 990                 | Student housing                               | ✓                               |                                 |                                |
| 260 Elgin Street, Carlton                                         | 140                 | Staff transit                                 | ✓                               |                                 |                                |
| 28-38 Storey Street, Parkville                                    | 1 800               | Tenant                                        | ✓                               |                                 |                                |
| 723 Swanston Street, Parkville                                    | 7 700               | Leased                                        | ✓                               |                                 |                                |
| North Telecom Site, South Melbourne                               | 7 590               | Part leased                                   | ✓                               |                                 |                                |
| 19-25 Russell Street, Melbourne                                   | 1 267               | Melb. Theatre Co.                             | ✓                               |                                 |                                |
| 397 Toorak Road, South Yarra                                      | 700                 | Tenant                                        | ✓                               |                                 |                                |
| 435 Cardigan Street, Carlton                                      | 250                 | Tenant                                        |                                 | ✓                               |                                |
| 437-439 Cardigan Street, Carlton                                  | 300                 | Manager, Grounds                              |                                 | ✓                               |                                |
| 33-35 Royal Parade, Parkville                                     | 750                 | Leased to Trinity College                     |                                 | ✓                               |                                |
| Two properties in Kew                                             | 5 200               | Institute of Early Childhood Development      |                                 | ✓                               |                                |
| Station Road, Deer Park                                           | 4 000               | Mt Derrimut Agriculture and Forestry Research |                                 | ✓                               |                                |
| 21-27 Royal Parade, Parkville                                     | 1 035               | Music and Agriculture and Forestry            |                                 |                                 | ✓                              |
| <b>Total</b>                                                      | <b>31 722</b>       |                                               |                                 |                                 |                                |

Overall comment

**3.1.51** The challenge for the University's management of property is to balance its longer-term strategic plans against the interim cost of holding underutilised or inappropriately utilised properties. This opportunity cost is best represented by the impact of substantial amounts of financial capital being tied up and unavailable for academic or research purposes of the University. A key issue is the very lengthy delays in the determination of an appropriate academic or research related use for these properties.

**3.1.52** It is considered that the University should place greater emphasis on rationalising and consolidating its existing stock of property assets, including accelerating the sale of marketable properties, and reduce its focus on the expansion of the property portfolio. In this context, audit notes that consideration is been given to the further expansion of the University onto the Royal Woman's Hospital site, should it become available.

**3.1.53** Key factors underpinning this view are:

- the existing level of underutilised or inappropriately utilised properties;
- the existence of "marketable properties" amounting to \$31.7 million within the University's portfolio;
- the existing maintenance backlog on the University's property portfolio requires substantial funding (estimated by the University at \$33 million in 1994);
- the University currently has a higher ratio of area to equivalent full-time students compared with the mean average for Australian universities;
- the implications of emerging trends in distance learning programs, such as the "open learning" program which uses free-to-air television or possible use of the internet, which could have potentially dramatic impacts on the University's space needs; and
- the impact on future space needs of the University arising from the recently proposed *Guidelines to be used in Pursuing a University-wide Timetable* that note it may be necessary, in the future, to timetable subjects on Saturdays and later on weeknights.

□ **RESPONSE** provided by Registrar, University of Melbourne

*The list of marketable properties was prepared on the basis that proceeds could be utilised for other purposes. It did not imply that the activities currently undertaken in those properties could be terminated. It was intended as an analysis to see whether some rationalisation could be undertaken, but without examining commensurate alternate accommodation options.*

*Properties in the University's area of strategic interest have been acquired on an 'as available' basis over many, many years. Opportunities arise infrequently. They do not necessarily match the immediate need, nor current capital allocations which would allow immediate development.*

*The University therefore does not accept that the level of properties which have been classified as inappropriately or underutilised is excessive. It follows therefore that the University does not agree that holding costs are excessive.*



*In more recent times, property values have been severely depressed and the University has taken advantage of low prices to further its long term strategic goals. Properties in the Eastern Precinct (Cardigan, Elgin, Swanston and Faraday Streets) and in the block bounded by Berkeley, Bouverie, Pelham and Grattan Streets are seen as being in the primary are of interest for the main Parkville campus.*

*The acquisition of the North and South Telecom site allowed achievement of very substantial academic goals for the Victorian College of the Arts, an independent component of the University of Melbourne.*

*The maintenance backlog on University buildings in recent years is higher than preferred, but a long term life cycle costing system is being introduced. In anticipation of the system being adopted, allocations shown in capital programs for building maintenance have been increased substantially. The maintenance backlog is not connected with the utilisation of space.*

*While some buildings are not being fully utilised, the reason for the lower ratio of area to equivalent full-time students, is attributable to the extensive number of higher degree students and research activities, requiring access to laboratory facilities, carried out at the University compared with other higher education institutions.*

*It is unreasonable to criticise decisions taken more than two years ago about the technological advances in open learning, which may at some future time reduce the need for more space.*

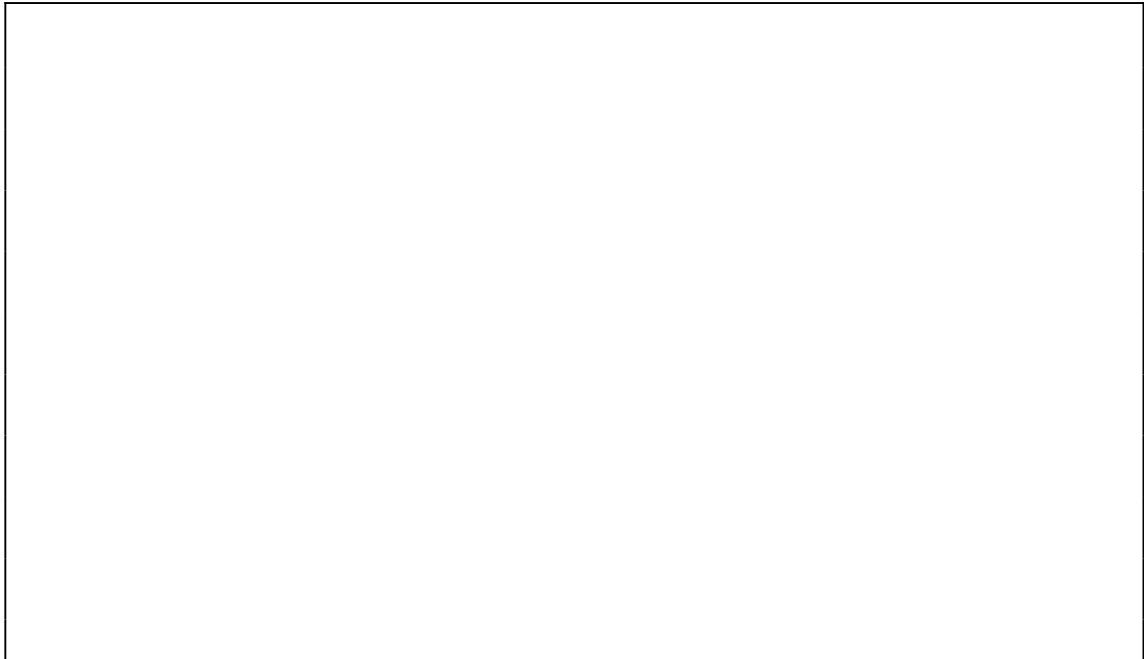
**3.1.54** Comment on some of the key underutilised or inappropriately utilised properties is included below.

**234 Queensberry Street, Melbourne**

**3.1.55** The property at 234 Queensberry Street, Melbourne was purchased in 1993 and is valued at \$13.5 million (at December 1995). It was proposed that the University Archives and at least 2 Arts Faculty departments relocate to the building. Audit was advised that the building was also considered appropriate to be used for temporary accommodation purposes, however, it was not fitted out or used for that purpose.

**3.1.56** As part of the purchase arrangement, the University also acquired ownership of a State school adjoining the property (228 Queensberry Street) which was valued at \$2.8 million at December 1995. The school is currently being used as a child care centre.

**3.1.57** The 234 Queensberry Street property is currently partly occupied by the Department of Criminology and Social Work and the Centre for Public Policy Studies. A significant proportion of the 2nd and 3rd floors have been empty since purchased in 1993 and the entire ground floor is vacant, other than when used for examinations.



*234 Queensberry Street, Melbourne.*

**3.1.58** Full occupation of the 234 Queensberry Street building is dependent upon the University settling on final uses for the space and funding being made available to effect refurbishment.

*207-221 Bouverie Street, Carlton*

**3.1.59** Construction of the Information Technology and Electrical Engineering Building, a 6 level building (with car parking facilities) was completed during 1993. At 31 December 1995, the property was valued at \$32.3 million.

**3.1.60** The construction cost of the first 3 levels of the building were met by the University using Commonwealth funding. These levels are currently occupied by various University departments.

**3.1.61** The construction of the top 3 levels was funded by a private company which then leased the building to the University using a long-term lease arrangement. The lease arrangement obligated the University to make yearly rental payments to the private company over the period of the lease (an initial period of 12 years had been set). The accounting for this lease arrangement by the University as an operating lease was the subject of an audit qualification of its 1993 financial statements on the basis that the leasing arrangement, in audit opinion, should have been reported as a finance lease in the University's balance sheet.

**3.1.62** The University had originally intended to occupy the top 3 levels with fee-paying private tenants, to service its lease payments. However, market rental rates were found to be about half of that originally projected which made it less attractive for the University to pursue its original strategy of tenanting half the building. Consequently, the University elected to occupy the entire space itself.

**3.1.63** Of the top 3 levels, approximately 2 levels were not occupied until March 1996. A further half level remained unoccupied at the date of preparation of this Report. The remaining one half of a level was occupied during December 1993, building construction having been completed in June 1993.

**3.1.64** The University terminated the lease arrangement during October 1994 at a cost of \$16.3 million.

**3.1.65** Actual costs incurred by the University in connection with the building, amounting to \$33.1 million in total, are detailed in Table 3.1G.

**TABLE 3.1G**  
**COST OF THE INFORMATION TECHNOLOGY**  
**AND ELECTRICAL ENGINEERING BUILDING (a)**

| <i>Cost</i>                                 | <i>\$million</i> |
|---------------------------------------------|------------------|
| Net building costs met by the University    | 14.8             |
| Lease payments                              | 2.0              |
| 1994 payment to terminate lease arrangement | 16.3             |
| <b>Total</b>                                | <b>33.1</b>      |

(a) The building was valued at \$29.2 million at December 1994 (\$30.1 million in December 1995).

**3.1.66** During 1992 the University's Finance Committee considered funding options for that part of the construction cost of the building not met by Commonwealth funding. If the University had taken the option of directly funding the shortfall, using its own cash reserves, audit estimates that the cost of the building to the University would have been \$25.3 million (in 1992 dollar value terms). This compares with the actual cost incurred by the University, also expressed in 1992 dollar value terms, of \$30.4 million, equivalent to \$33.1 million in nominal dollar terms.

**3.1.67** In summary:

- the building has cost the University \$5.1 million more than if it had contributed internal cash reserves to the cost of construction of the building;
- valuable city fringe space has remained underutilised since construction in June 1993;
- the University has had to make an unplanned diversion of funds from other uses to pay out the building in 1994; and
- the entire facility is now available to the University for academic or research purposes, some of the additional space being refurbished for use by the University during 1996.



**□ RESPONSE** provided by Registrar, University of Melbourne

*The University decided to terminate the operating lease on the building due to the audit qualifications. This was done using internal funding sources. Having funded the total building from internal sources the University decided to transfer the use to academic purposes and ceased negotiations with outside tenants.*

*The University terminated the operating lease arrangements in October 1994 as the University had been advised that the audit qualification to its 1993 accounts would continue as long as the operating lease continued.*

*The University has paid \$31.1 million for a building which it estimates cost the Special Purpose Vehicle \$29.5 million. The University acknowledges that a premium was paid to*

- *Fund the project through an operating lease facility as the Victorian Government of the day denied the University access to Loan Council allocations to enable it to borrow the money required.*
- *Terminate the facility earlier than planned due to the continuation of audit qualifications in its annual accounts by the Victorian Auditor-General.*

**Archives Repository**

**3.1.68** For many years, the University has maintained an Archives Repository. The objective of this repository, as set out in the Archives Policy on Acquisitions, is to acquire historical records, particularly those relating to commerce, industry, business and the professions, as well as records concerning the University.

**3.1.69** The archive collection currently comprises letters, photographs, diaries, ledgers, minutes and books. Most items have not been published and therefore are not held in the University's main library collection. The collection is considered by the University to be of world standard and requires suitable space to ensure its preservation and availability to students and other interested parties for research purposes.

**3.1.70** The collection has grown over time and is currently housed over several locations, including the following Carlton locations:

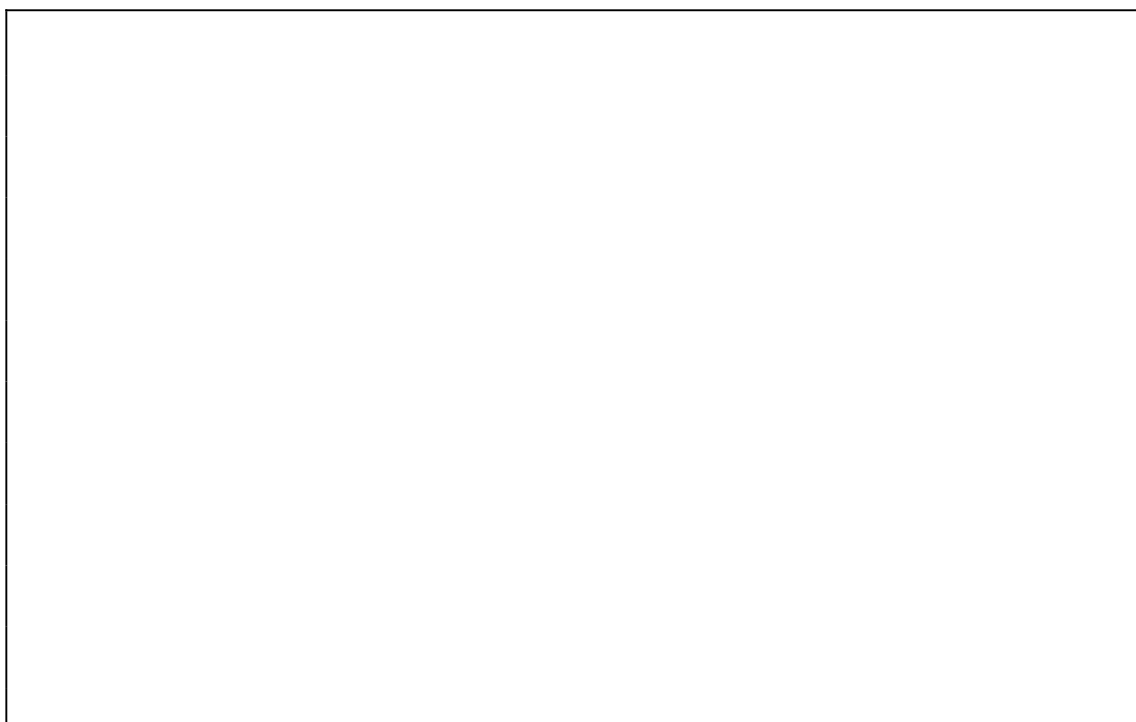
- 168 Leicester Street;
- 119-129 Barry Street; and
- 176-180 Leicester Street (basement only)

**3.1.71** In addition, a portion of the collection is under the custodianship of the Records Services Branch and is held in the basement of the Raymond Priestly Building on the main campus. The Records Services Branch is responsible for the short to medium-term storage of financial, student, personnel and other records.

**3.1.72** Audit inspection of the various locations noted that:

- some storage areas were found to be overcrowded and disorganised, as indicated by boxes stacked on floors, tables and the top of cabinets; and
- the collection presented a fire hazard at the 168 Leicester Street location due to blocked pathways and exits in the building.

**3.1.73** Most of the collection is housed in premises not designed or modified to store records and other valuable historic artefacts, i.e. the Leicester Street buildings, and, as a consequence, the preservation of the collection may be at risk.



*Part of archive collection at 168 Leicester Street, Carlton.*

**3.1.74** The use of expensive city fringe locations, close to the main campus, to house the collection needs to be justified on an academic/research and economic basis. The capital value of the main Carlton properties used to house the collection amounted to over \$2.6 million at December 1995 and they provided approximately 1,300 m<sup>2</sup> of useable space. This represents a considerable amount of capital tied up in premises, some of which are not designed to satisfactorily achieve their current role.

**TABLE 3.1H  
LOCATIONS USED  
TO HOUSE THE ARCHIVE COLLECTION**

| <i>Building</i>               | <i>Valuation<br/>at December<br/>1995)</i> | <i>Used for<br/>Archiving<br/>purposes<br/>since -</i> |
|-------------------------------|--------------------------------------------|--------------------------------------------------------|
|                               | (\$'000)                                   |                                                        |
| 119-129 Barry Street, Carlton | 1 692                                      | 1982                                                   |
| 168 Leicester Street, Carlton | 937                                        | 1977                                                   |
| <b>Total</b>                  | <b>2 629</b>                               |                                                        |

**3.1.75** In addition, a portion of the collection is housed in the basements of 176-180 Leicester Street, Carlton and the Raymond Priestly Building on the main campus.





**3.1.76** The use of multiple locations, including non-purpose designed buildings, for the storage of the archive collection presents difficulties of access to the collection by users and occupies prime city fringe space which could otherwise be utilised for other high priority University needs.

*Consultant's report*

**3.1.77** In June 1995, a consultant from the University of Sydney completed a report on the future of the collection. Findings included:

- a recommendation to lease space from an existing archive repository to house the collection;
- the need for a more vigorous microfilming program; and
- provision of a reading room at Baillieu Library on the main campus with regular delivery of records from the relocated repository.

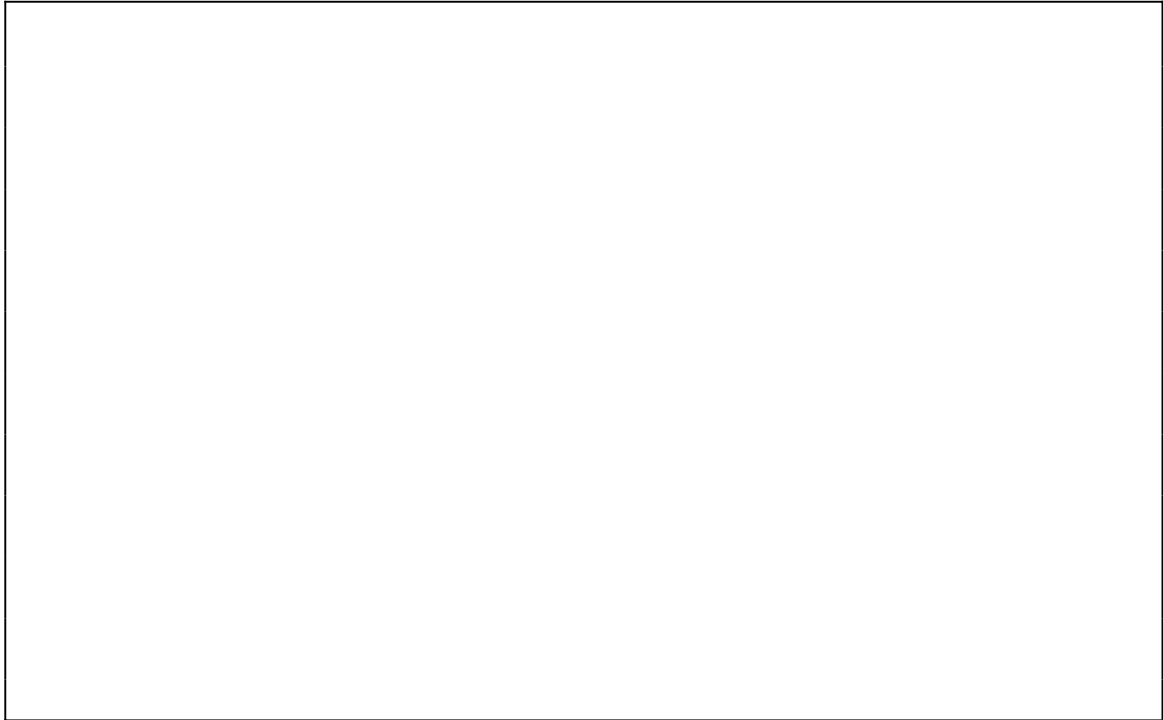
**3.1.78** This was followed-up by an internal report in January 1996 which detailed space and cost estimates of a relocated archive collection. At the time of preparation of this Report, the University had not finalised its position on the housing of the archive collection.

**3.1.79** The rationalisation of the existing arrangements for the housing of the archive collections should maximise:

- access to, and preservation of, the collection;
- future needs of the collection;
- cost-effective use of the University's resources; and
- utility of the University's city fringe buildings.

*Furniture storage*

**3.1.80** The properties at 164-170 Pelham Street and a portion of 176-180 Leicester Street, Carlton, are currently being used to store furniture. These properties were valued at \$453 400 and \$1 856 800, respectively (at December 1995).



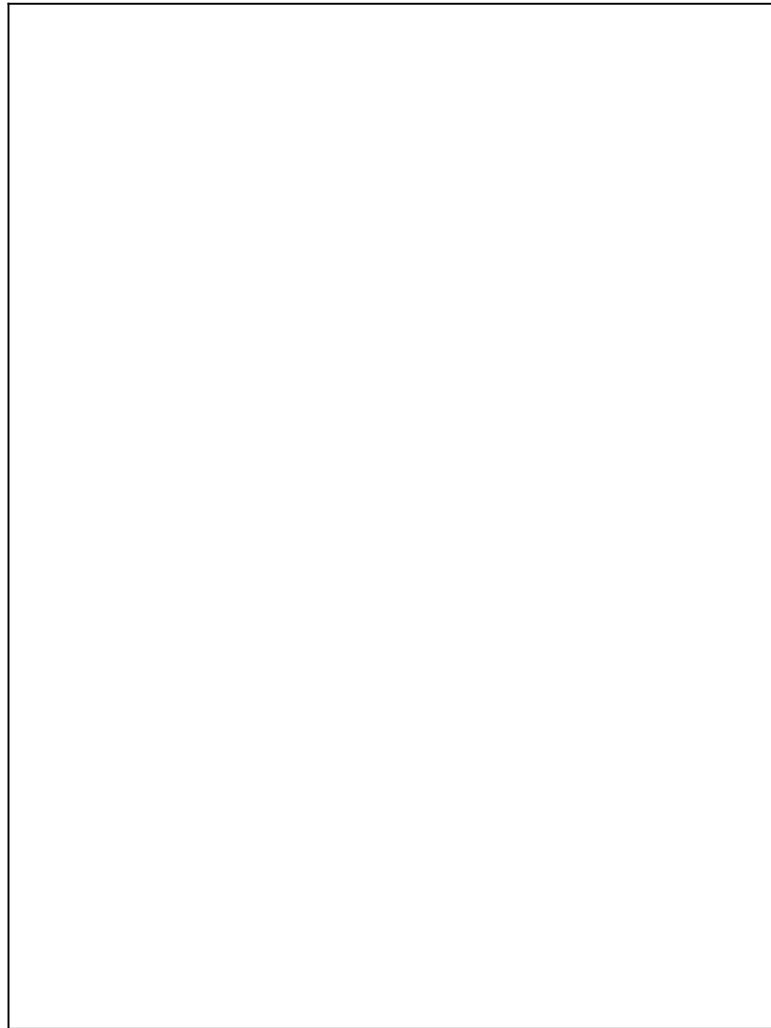
*Furniture stored at Pelham Street, Carlton.*

**3.1.81** It is considered that the use of valuable city fringe properties for the storage of disused furniture represents an uneconomic use of the University's economic resources. These properties, including the 193-195 Bouverie Street property, are awaiting redevelopment.

*The Eastern Precinct*

**3.1.82** Throughout the 1960s and 1970s, the University acquired most of the properties to the east of the University in the area bounded by Cardigan, Elgin, Faraday and Swanston streets. This area became known as the "Eastern Precinct".

**3.1.83** Audit review of Eastern Precinct properties identified 2 underutilised or inappropriately utilised properties, being those properties located at 351 and 375 Cardigan Street, Carlton. **The property located at 375 Cardigan Street (valued at \$120,400) has been used to store geological rocks since 1976 while the property located at 351 Cardigan Street has been vacant since 1994 having been previously used by the Mountaineering Club since 1989. Both of these properties are in poor physical condition due to a lack of regular maintenance.**



*351 Cardigan Street, Carlton.*

*"North and South Telecom" sites*

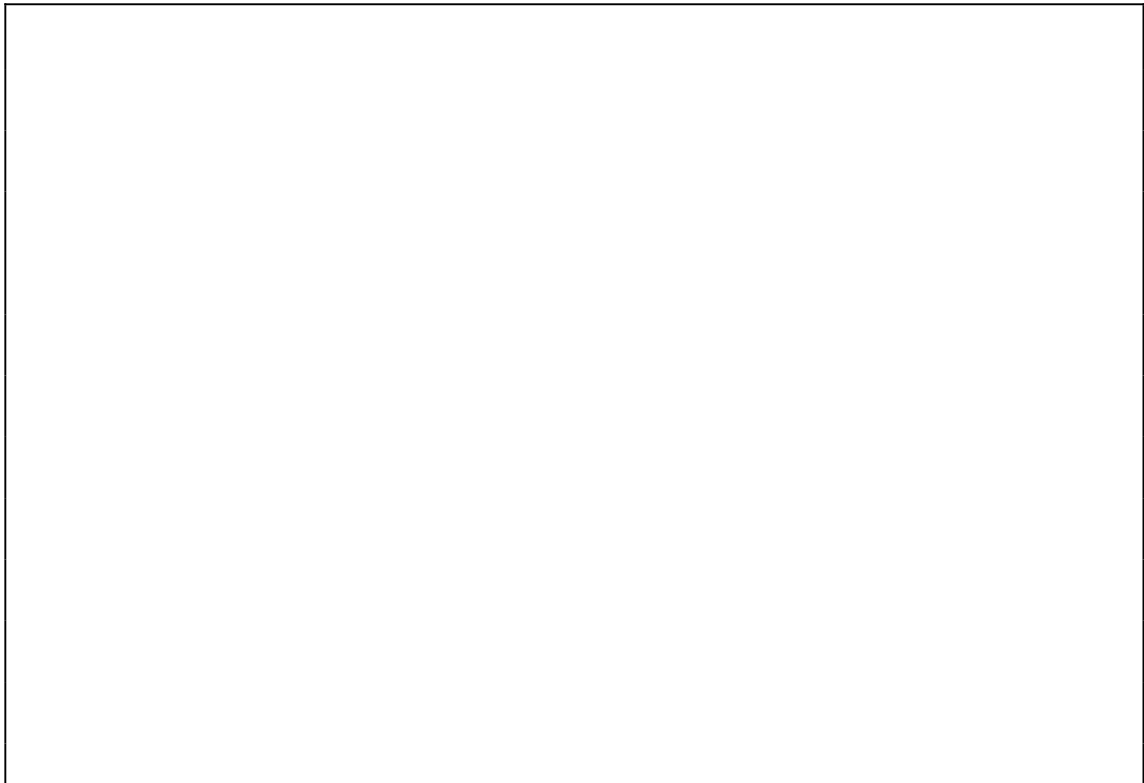
**3.1.84** In 1991, the University acquired 2 adjacent sites known as North and South Telecom which are contained within the area bounded by Southbank Boulevard, Grant Street, Dodds Street, and Sturt Street, South Melbourne. The sites cover an area of 13 369 square meters and are valued at \$7.7 million and \$12.9 million, respectively (at December 1995). The acquisition of the sites was achieved through a complicated property transaction, key elements of which were:

- the University purchased the South Telecom site for \$6 million using internal funds;
- the University received \$15.6 million of Commonwealth funding to redevelop certain sites, including the South Telecom site, for use by the Victorian College of the Arts, an affiliate of the University;
- the University received a Crown grant from the State Government for the North Telecom site (at no further cost to the University); and
- the University received long-term access to an area within the Parkville Veterinary Precinct not formerly occupied by the University.

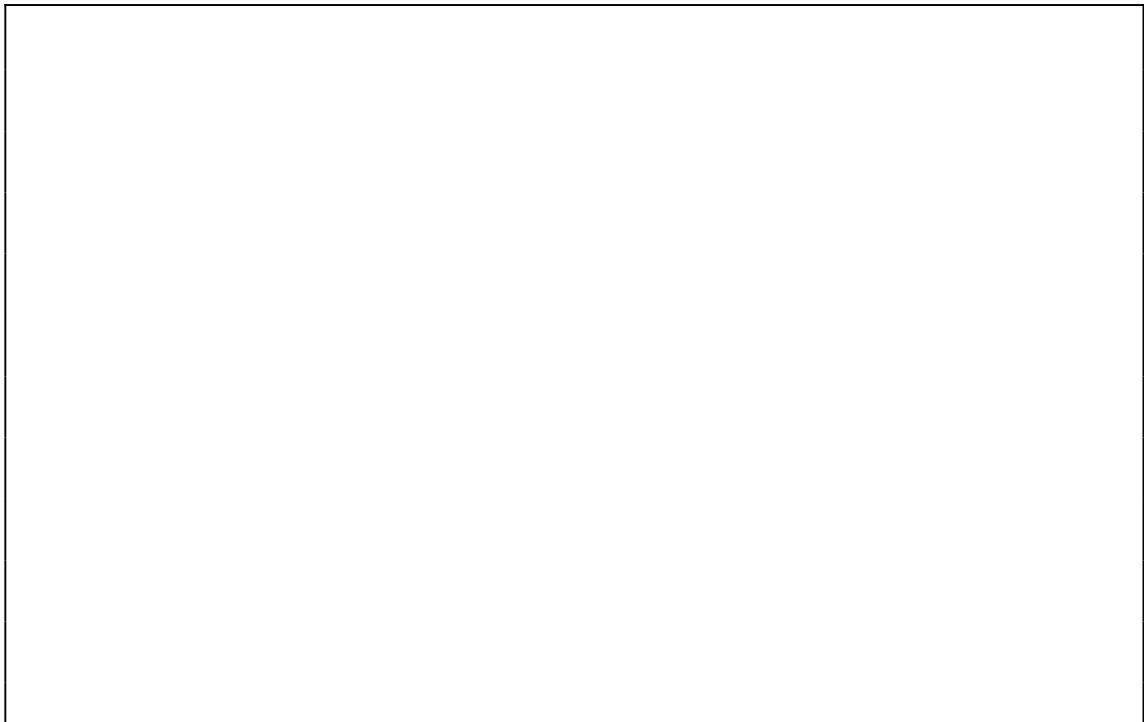


**3.1.85** The "North Telecom" site has not been redeveloped for use by the University. It presently contains vacant buildings, vacant land (currently being used for car parking by the Victorian College of the Arts), several commercial premises leased by private tenants and the Victorian College of the Arts Drama school. Annual rental from the private tenants amounts to less than \$40 000.

**3.1.86** The University does not receive any rental payments from the Victorian College of the Arts for the use of the redeveloped "South Telecom" site or for that part of the "North Telecom" site used by the College. The Victorian College of the Arts does generate revenue from the car park utilised by its staff and derives substantial benefit from the use of both the South and North Telecom sites.



*Vacant Building - North Telecom Site.*



*Car park - North Telecom Site.*



*Private tenant - North Telecom Site.*

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**3.1.87** Since the site was acquired, several uses for the property have been considered including sole use for academic purposes, part or whole use for commercial ventures or sale. Funding options have included both internal funding by the University and commercial development. At the time of preparation of this Report, however, the University had not finalised its plans for the site. Redevelopment or sale are considered to be unlikely in the short-term. **Until the University finalises its position, the site will continue to be underutilised, representing a significant cost to the University in terms of capital tied up in a non-teaching or research activity.**

### Utilisation of lecture theatres

**3.1.88** The Australian Government's 1995 Higher Education Management Review "*Report of the Commission of Inquiry*" (the Hoare Report), concluded that "... *there was substantial potential for university assets to be used more intensely*". The Report's suggestions for more intensive use of assets included:

- more efficient allocation of lecture theatres, main teaching rooms and tutorial rooms; and
- greater use of summer courses and continuing education courses.

**3.1.89** The University has 66 lecture theatres on or near the main campus (in the Carlton/Parkville area). The capacity of these theatres ranges from 50 students for the Thomas Cherry Theatre up to 493 students for the Copeland Theatre.

**3.1.90** A review of lecture theatre bookings for the second half of 1995 found:

- **current average usage is 66 per cent of available lecture theatre space during normal hours**, assuming 9 one hour periods a day;
- **wide variation in the level of utilisation throughout the day, with low utilisation during early morning and mid to late afternoon;**
- **extremely low levels of utilisation on Fridays, averaging only 41 per cent of available lecture theatre space during normal hours**, assuming 9 one hour periods;
- **an uneven pattern of lecture theatre usage which creates an artificial need for a larger stock of lecture theatres than would otherwise be the case; and**
- **limited utilisation of lecture theatres outside normal working hours.**

**3.1.91** During July 1993, the University's Property and Buildings Department undertook an analysis of lecture theatre usage and identified similar issues concerning usage of lecture theatres. In addition the University Timetabling Co-ordination Group also met during 1995 to discuss issues related to timetabling and room allocation and related strategies.

**3.1.92** Lecture theatre utilisation is one of a number of key factors to be balanced in the wider and very complex issue of timetabling within the University. Nevertheless, lecture theatres represent a key cost and scarce resource for the University.



**3.1.93** Three measures are proposed by the University to improve usage of lecture theatres:

- computer software has been purchased to produce a University-wide subject timetable and to handle room allocation;
- *Guidelines to be used in Pursuing a University-wide Timetable* have been developed; and
- the limited term appointment of an officer to co-ordinate University timetabling.

**3.1.94** The above measures will hopefully facilitate better co-ordination and information on lecture theatre utilisation, in particular, the *Guidelines to be used in Pursuing a University-wide Timetable* proposes a better spread of teaching activities across the teaching day and week. However, by themselves, these actions may not increase overall utilisation of lecture theatres.

**3.1.95** A more even spread of lecture theatre usage during the teaching day could free up an amount of valuable main campus space for other uses. The utilisation of existing lecture theatres could be increased by a greater emphasis on external marketing of the University's facilities and/or greater use of summer courses and continuing education courses involving part-time studies.

□ *RESPONSE* provided by Registrar, University of Melbourne

*The comments about lecture theatre usage are acknowledged. With 25 000 students, 4 500 staff including 2 000 academic staff, 13 000 rooms, 8 000 possible courses, and furthermore, a desire to provide maximum choice for students so that the University's ability to deliver the products wanted by students, lecture theatre usage problems are no longer solvable by using existing techniques. For a number of years searches have been undertaken across the world for appropriate software. None was available which did not have major functionality restrictions. We have now purchased Syllabus Plus, which we believe is very likely to meet our needs. Our lead in this area is being following by a number of other Australian universities.*

*It is acknowledged that some further opportunities may exist for the letting of University facilities to external organisations. The University has some very high quality lecture theatres, and this year video conferencing linkages to other sites are available. In December last year development of a business plan for the use of these facilities was commenced. The elements of the business plan which address the new Competition Policy have yet to be finalised.*

*It has been found that the conference market hardly exists on weekends and with limited windows of opportunity through the year, mainly in semester breaks, the opportunities for hiring of out <sic> facilities is quite limited.*

## INFORMATION SYSTEMS AND PERFORMANCE MANAGEMENT

### Information systems

**3.1.96** Key property-related information systems and sources within the University include the Space Inventory Database, the Property Register, a lecture theatre and classroom booking system, the General Maintenance System, the Building Works and Information System, Building Automation Systems and the Melbourne University Financial Accounting System. In addition, a number of other information systems with implications for property management are currently under consideration, including a subject timetabling and room allocation system and a property maintenance information system.

**3.1.97** Comments on some of the property-related information systems follow.

#### *Space Inventory Database*

**3.1.98** The Property and Buildings Department maintains a database system which records space details for almost all academic and administrative buildings. In addition, a further system (AutoCAD) is used to record most floor plan diagrams. These systems, together with other proprietary software, are used to plan and manage space within the University, including the design of new buildings or refurbishment projects.

**3.1.99** The Property and Buildings Department is currently considering the purchase of a new system which will link the Space Inventory Database and AutoCAD, and which will have expanded capabilities.

#### *Property Register*

**3.1.100** The Property and Buildings Department of the University maintains a manual property register which records certain details relating to all properties owned.

**3.1.101** **The use of a manual property register for a property portfolio of some 464 buildings, with a combined land and buildings value of over \$1 billion, is considered by audit to be not efficient as it:**

- does not facilitate ready access to property-related information;
- results in duplication of information held in other computerised information systems, such as the Space Inventory Database which contains similar data; and
- cannot be as readily updated as a computerised system.

**3.1.102** **In addition, it was also found that relevant planning details from the master plan, bequests and other restrictions on property usage were not recorded in the register.** Restrictions on property usage can arise from bequests, the Historic Buildings Council and the Melbourne City Council and such caveats should be recorded in the property register.



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*Lecture Theatre and Classroom Booking System*

**3.1.103** The Property and Buildings Department currently maintains a computer-assisted booking system for lecture theatres and classrooms. However, a computerised subject timetabling and room allocation system is under development. Room allocation and related timetabling issues and strategies have been under consideration since 1993.

**3.1.104** The introduction of a computerised room allocation system which optimises room usage, together with other reforms, will facilitate better co-ordination and information on lecture theatre and classroom utilisation throughout the University.

*Maintenance information systems*

**3.1.105** Maintenance issues assume a high priority, particularly in the case of an ageing property portfolio of the magnitude controlled by the University.

**3.1.106** The University currently uses an in-house developed information system, the General Maintenance System, to record and manage maintenance projects. In addition, the Building Works and Information System, a works management program, was acquired in 1995 and is under development. It will record costs of maintenance and major/minor works projects on a project and building basis to assist in life cycle monitoring. Audit was advised that consideration is currently being given to the purchase or development of a new maintenance system, which will record maintenance data and flag planned maintenance needs. These information system developments should enhance property maintenance-related information available for the management of the Portfolio.

**3.1.107** An integrated building maintenance information system would fulfil a number of requirements, including prioritisation of maintenance projects, management of maintenance projects, automatic scheduling of preventative maintenance, facilitate cost analysis and project cost estimation, indicate condition of buildings and highlight the extent of any maintenance backlog.

*Information systems development*

**3.1.108** It is considered that future property-related information systems development should include greater emphasis on the need to:

- **integrate (or link) the various manual and computerised systems currently in operation;**
- **minimise information or systems duplication;**
- **facilitate information access by all appropriate staff within the University;**
- **record and facilitate preventative and routine maintenance programs;**
- **provide greater property-related information, including details of any restrictions on property usage, planning decisions by the University, maintenance programs, minor and other property-related works and maintenance backlog; and**
- **facilitate preparation of performance management information, such as key performance indicators, for the University's Council and its Committees.**

□ *RESPONSE provided by Registrar, University of Melbourne*

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*The improvements listed above were included in this year's departmental development activities at the beginning of the year. To date, necessary data collection for the 13 000 rooms for example, has been proceeding but is no small task. Resources for such tasks must always be carefully weighed against the ever present urgent matters and the relevance of the activities to the important strategic goals of the University.*

## Performance management

### Property cost control

**3.1.109** The General University Costs Sub-Committee conducts, in accordance with its terms of reference, periodic and systematic reviews of individual general university costs and considers reports of budget variances. General University costs are those costs which are not allocated to a departmental (or other similar) budget. They include many property outgoings such as energy costs (e.g. gas and electricity).

**3.1.110** Ongoing routine cost control, for property-related expenditure, is predominantly from the perspective of cost type rather than a cost centre perspective, such as individual buildings or groups of buildings. Inefficient buildings are more readily identifiable if cost control is focused on a building by building basis. In addition, cost control at committee level predominantly centres on comparisons with budget, rather than including regular benchmarking or other comparisons.

**3.1.111** Further, the University does not prepare regular financial reports detailing net operating costs on a building-by-building basis, excluding student housing. Consequently, the total net costs of operating individual buildings is not routinely measured and assessed, excepting analysis of individual cost types.

**3.1.112** It is noted that with the introduction of the Building Works and Information System in 1995, it is possible to record certain costs, such as maintenance and major/minor works, on a project and a building basis. It is not currently planned to expand this to include the full cost of all property outgoings and non-cash expenses, such as depreciation.

**3.1.113** The University accounting system does generate, however, a monthly record of cash receipts and payments for each student house. At the end of each year, a consolidated "profit and loss" statement is produced for all of the houses and submitted to the University Council. Minor cash surpluses have been recorded over the previous 3 years. However, this statement reflects cash transactions only. Accruals, depreciation, internal cost of capital and other non-cash costs are not brought to account. To do so would convey a completely different picture of the net cost of providing student housing. The existing reports therefore do not convey the full cost of owning and operating these properties with the result that uneconomic properties cannot be readily identified.



**3.1.114** The absence of a full cost-based system could lead to less than optimal management information for decision-making purposes in respect of all accommodation. It is considered that the University should undertake regular preparation of monthly "net operating cost" statements on a building-by-building basis to identify both efficient and inefficient building practices. The statements should include all revenue (such as external hire revenue) and all expenditure on a full cost basis which will enable the University to readily review the relative efficiency of each property and of the portfolio as a whole in order that uneconomic properties may be identified and appropriate action taken.

□ *RESPONSE provided by Registrar, University of Melbourne*

*Knowing the full operating costs on a building by building basis will allow comparisons to be made as suggested above. The correction of observed inefficiencies, however, must take place as part of a plan which encompasses all other University priorities. Cost effectiveness is an important aspect in determining these priorities. The major component of building operating costs, that of energy consumption, is known on an individual building basis, and minimisation of heating to essential working hours at an acceptable temperature is carefully monitored. Compiling other costs on a building by building basis will create considerable clerical work but not lead to a commensurate improvement in savings.*

*Student housing operating costs, on the other hand, will be restructured as suggested. These properties can be easily sold if not performing adequately. This option is not available for most University buildings, however.*

User charges

**3.1.115** During 1990, a consultant engaged by the University recommended charging departments for the space they occupy as a means of providing departments with an incentive to be economical in their requests for, and management of, space. In response to the consultant's report, the University's Buildings Committee agreed to explore the merits of implementing a detailed system of space management. At the time of preparing this Report, an internal charging system for the occupation of University space had not been implemented.

**3.1.116** The arguments supporting the internal charging of departments for their occupation of space remains compelling, and include:

- Charging for space would provide users with an incentive to act more economically in the use of existing space and in making requests for further space. This avoids departments treating space as a "free" resource;
- Departmental budgets will more fully represent the total cost of their activities;
- Better resource allocation decisions would result if proposals for funding are based on the full costs, including the cost of space;
- Responsibility for space-related costs are placed with the users who are best able to control them;
- A greater awareness or focus on accommodation costs should occur at the user level, including the implications from the acquisition of new accommodation for ongoing maintenance and other costs;



- A reduction in capital resource requirements, and therefore operating costs, could result;
- Accommodation planning would be improved; and
- Departments will be more accountable for, and aware of, the total resources at their disposal.

**3.1.117** Some Australian and overseas University's have used an internal charging system for several years and charging for accommodation provided in the Victorian budget sector, using an imputed "rent" based on Valuer-General valuations, has also operated for several years.

**3.1.118** The benefits of charging for space, however, also bring with them a level of administrative burden and internal debate over the equity and accuracy of cost allocation methods to be used.

**3.1.119** A number of possible options for implementing an internal charging system for space costs have been suggested to the University.

**3.1.120** **It is considered that the University should implement a space charging system to act as an incentive to ensure the economical use of existing properties and requests for additional space. In audit opinion, a charging system which seeks to allocate the full cost of space to user departments based on total existing property holdings will achieve the maximum benefit for the University.**

*□ RESPONSE provided by Registrar, University of Melbourne*

*The concept of charging for space so as to achieve efficiency in utilisation of accommodation assets has been a cherished goal of University property managers for a long time. The statement that some Australian Universities have used an internal charging system for several years is disputed.*

*We could create a lot of activity in measuring and distributing costs for accommodation but still miss the main aim of ensuring that our space resources are used for the highest priority activities.*

*Nonetheless, it is acknowledged that efficient use of space can probably only be achieved by a space charging system and that if departments and facilities recognise opportunities to "sell off" some space in order to support other activities, then better utilisation of existing space will result. Further analysis will be undertaken.*

*Performance indicators*

**3.1.121** In addition to comparisons of actual expenditures against budget, the Property and Buildings Department collates and undertakes some analysis of comparative property-related statistical data. The data has been sourced from a number of other universities and is currently undergoing a period of refinement to ensure comparability. However, **no formal and regular reporting of key property related performance indicators and associated analysis of the comparative data is presented to the University's Council or its committees.** A variety of property and other statistical data is prepared by the University and submitted annually to the Commonwealth Department of Employment, Education and Training and the Association of Physical Plan Administrators of the United States.

**3.1.122** The University should institute regular reporting and time series analysis against targets and benchmarks (sourced from like institutions and industry groups) of a series of property related performance indicators for provision to the University Council and its Committees. A number of possible performance indicators have been suggested to the University.

□ *RESPONSE* provided by Registrar, University of Melbourne

*Unlike most other sectors of higher education administration, property managers have been comparing data for many years, well before benchmarking became popular. The performance indicators have been used to seek opportunities for comparison and subsequent improvement.*

**LOSSES, THEFTS AND IRREGULARITIES**

**Directorate of School Education**

**3.1.123** Table 3.1N summarises particulars of losses, thefts and other irregularities, including property damage, which occurred in 1995 and which were reported to audit by the Department of Education.

**TABLE 3.1N  
LOSSES, THEFTS  
AND OTHER IRREGULARITIES  
(\$)**

| <i>Item</i>                                                   | <i>Amount</i>    |
|---------------------------------------------------------------|------------------|
| Funds                                                         | 5 544            |
| Equipment and property damage                                 | 3 414 910        |
| <b>Total reported losses, thefts and other irregularities</b> | <b>3 420 454</b> |

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**3.1.124** Major incidences of losses and thefts of funds and equipment and property damage are detailed below:

- A number of fires at schools were reported by the Department of Education. The suspected cause of many of these was arson and the police were notified in all cases. Major fires reported and estimated damages were Yarrawonga Secondary College (\$825 000), James Harrison Secondary College (\$262 000), Olympic Village Primary School (\$100 000) and Sunshine Secondary College (\$60 000).
- Water damage (\$200 000) to the library and adjacent computer room occurred at Epping Secondary College. Two humidifiers were used to extract water from the books, saving many in the process.
- Three youths completely vandalised the computer room and adjoining storeroom at Wheelers Hill Secondary College, causing \$26 000 worth of damage. The police were notified and action has been taken by the college to prevent re-occurrence.
- Computer equipment and associated items valued at \$25 000 were stolen from Kealba Secondary College.
- Three separate burglaries occurred at Melbourne High School during major refurbishment from February to March. Computer equipment valued at \$13 000 was stolen.
- Four separate burglaries occurred at Aberfeldie Primary School during the period of mid-January to early March. Computer equipment valued at \$10 000 was stolen.

SCHEDULE A  
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS

| <i>Report</i>                                                                    | <i>Subject</i> | <i>Status at date of preparation of this Report</i> |
|----------------------------------------------------------------------------------|----------------|-----------------------------------------------------|
| <i>All matters previously raised by audit have been satisfactorily resolved.</i> |                |                                                     |

SCHEDULE B  
COMPLETED/INCOMPLETE AUDITS

| <i>Entity</i>                                | <i>Financial year ended</i> | <i>Reporting to Parliament</i>                                      | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|----------------------------------------------|-----------------------------|---------------------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS</b>                      |                             |                                                                     |                                              |                                        |
| Department of Education                      | 30 June 1995                | 31 Oct. <i>Financial Management Act 1994</i> , s.45.                | 6 Oct. 1995                                  | 6 Oct. 1995                            |
| <b>EDUCATION</b>                             |                             |                                                                     |                                              |                                        |
| Board of Studies                             | 30 June 1995                | 30 Sept. <i>Financial Management Act 1994</i> , s.46.               | 18 Sept. 1995                                | 29 Sept. 1995                          |
| Telematics Course Development Fund Trust     | 31 Dec. 1994                | No reporting requirements. Audit conducted at request of Treasurer. | 27 Mar. 1995                                 | 2 June 1995                            |
| Victorian Education Foundation               | 30 June 1995                | 31 Oct. <i>Financial Management Act 1994</i> , s.53A.               | 19 Sept. 1995                                | 9 Oct. 1995                            |
| Victorian Education Foundation Pty Ltd       | 30 June 1995                | " "                                                                 | 19 Sept. 1995                                | 9 Oct. 1995                            |
| <b>TERTIARY EDUCATION AND TRAINING</b>       |                             |                                                                     |                                              |                                        |
| Adult, Community and Further Education Board | 30 June 1995                | 30 Sept. <i>Financial Management Act 1994</i> , s.46.               | 25 Sept. 1995                                | 29 Sept. 1995                          |
| Council of Adult Education                   | 31 Dec. 1995                | 30 April. <i>Financial Management Act 1994</i> , s.46.              | 26 Mar. 1996                                 | 29 Mar. 1996                           |
| State Training Board                         | 30 June 1995                | 30 Sept. <i>Financial Management Act 1994</i> , s.46.               | 19 Sept. 1995                                | 28 Sept. 1995                          |

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**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                             | <i>Financial<br/>year<br/>ended</i> | <i>Reporting to Parliament</i>                                           | <i>Financial<br/>statements<br/>signed by<br/>entity</i> | <i>Auditor-<br/>General's<br/>report<br/>signed</i> |
|-----------------------------------------------------------|-------------------------------------|--------------------------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------------|
| <b>COMPLETED AUDITS - continued</b>                       |                                     |                                                                          |                                                          |                                                     |
| <b>Post-secondary education institutions</b>              |                                     |                                                                          |                                                          |                                                     |
| <i>Universities and associated companies</i>              |                                     |                                                                          |                                                          |                                                     |
| Australian Music Examination Board (Vic) Ltd              | 31 Dec.<br>1995                     | 30 April. <i>Melbourne University Act 1958, s.41.</i>                    | 12 Mar.<br>1996                                          | 1 April<br>1996                                     |
| Australian National Academy of Music Ltd.                 | 31 Dec.<br>1995                     | " "                                                                      | 15 Mar.<br>1996                                          | 1 April<br>1996                                     |
| Citytech Pty Ltd                                          | 31 Dec.<br>1995                     | 30 April. <i>Royal Melbourne Institute of Technology Act 1992, s.39.</i> | 22 Mar.<br>1996                                          | 1 April<br>1996                                     |
| Deakin University                                         | 31 Dec.<br>1995                     | 30 April. <i>Deakin University Act 1978, s.35.</i>                       | 18 Mar.<br>1996                                          | 21 Mar.<br>1996                                     |
| Deakin University Foundation Ltd                          | 31 Dec.<br>1995                     | 30 April. <i>Deakin University Act 1974, s.34A.</i>                      | 18 Mar.<br>1996                                          | 25 Mar.<br>1996                                     |
| Deakin University Foundation Trust                        | 31 Dec.<br>1995                     | 30 April. <i>Deakin University Act 1974, s.34A.</i>                      | 18 Mar.<br>1996                                          | 25 Mar.<br>1996                                     |
| Hawthorn Institute of Education Ltd                       | 31 Dec.<br>1995                     | 30 April. <i>Financial Management Act 1994, s.46.</i>                    | 29 Mar.<br>1996                                          | 2 April<br>1996                                     |
| Institute for Innovation and Enterprise Ltd               | 31 Dec.<br>1995                     | 30 April. <i>Swinburne University of Technology Act 1992, s.44.</i>      | 14 Feb.<br>1996                                          | 13 Mar.<br>1996                                     |
| La Trobe University                                       | 31 Dec.<br>1995                     | 30 April. <i>Latrobe University Act 1971, s.37.</i>                      | 28 Mar.<br>1996                                          | 4 April<br>1996                                     |
| La Trobe University Housing Ltd                           | 31 Dec.<br>1995                     | " "                                                                      | 18 Mar.<br>1996                                          | 29 Mar.<br>1996                                     |
| La Trobe Marketing Pty Ltd                                | 31 Dec.<br>1995                     | " "                                                                      | 15 Feb.<br>1996                                          | 29 Mar.<br>1996                                     |
| Meltech Services Pty Ltd                                  | 31 Dec.<br>1995                     | 30 April. <i>Royal Melbourne Institute of Technology Act 1992, s.39.</i> | 25 Mar.<br>1996                                          | 1 April<br>1996                                     |
| Milake Pty Ltd                                            | 31 Dec.<br>1995                     | 30 April. <i>Deakin University Act 1974, s.34A.</i>                      | 1 Mar.<br>1996                                           | 20 Mar.<br>1996                                     |
| Monash University                                         | 31 Dec.<br>1995                     | 30 April. <i>Monash University Act 1958, s.36.</i>                       | 4 Mar.<br>1996                                           | 22 Mar.<br>1996                                     |
| Monash - ANZ Centre of International Briefing Pty Ltd (a) | 31 Oct.<br>1995                     | 30 April. <i>Monash University Act 1958, s.35B.</i>                      | 15 Nov.<br>1995                                          | 21 Mar.<br>1996                                     |
| Monash International Pty Ltd                              | 31 Dec.<br>1995                     | " "                                                                      | 6 Mar.<br>1996                                           | 19 Mar.<br>1996                                     |
| Monash IVF Pathology Services Pty Ltd                     | 31 Dec.<br>1995                     | " "                                                                      | 16 Jan.<br>1996                                          | 19 Mar.<br>1996                                     |



**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                                          | <i>Financial<br/>year<br/>ended</i> | <i>Reporting to Parliament</i>                                                   | <i>Financial<br/>statements<br/>signed by<br/>entity</i> | <i>Auditor-<br/>General's<br/>report<br/>signed</i> |
|------------------------------------------------------------------------|-------------------------------------|----------------------------------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------------|
| <b>COMPLETED AUDITS - continued</b>                                    |                                     |                                                                                  |                                                          |                                                     |
| <b>Post-secondary education institutions - continued</b>               |                                     |                                                                                  |                                                          |                                                     |
| <i>Universities and associated companies - continued</i>               |                                     |                                                                                  |                                                          |                                                     |
| Monash IVF Pty Ltd                                                     | 31 Dec.<br>1995                     | 30 April. <i>Monash University<br/>Act 1958, s.35B.</i>                          | 16 Jan.<br>1996                                          | 19 Mar.<br>1996                                     |
| Monash IVF Pathology Services<br>Trust                                 | 31 Dec.<br>1995                     | " "                                                                              | 16 Jan.<br>1996                                          | 19 Mar.<br>1996                                     |
| Monash Language Centre Pty.<br>Ltd.                                    | 31 Dec.<br>1995                     | " "                                                                              | 6 Mar.<br>1996                                           | 21 Mar.<br>1996                                     |
| Monash Merchandising<br>Company Pty Ltd                                | 31 Dec.<br>1995                     | " "                                                                              | 9 Feb.<br>1996                                           | 20 Mar.<br>1996                                     |
| Monash Merchandising Unit<br>Trust                                     | 31 Dec.<br>1995                     | " "                                                                              | 9 Feb.<br>1996                                           | 20 Mar.<br>1996                                     |
| Monash - Mt Eliza Graduate<br>School of Business and<br>Government Ltd | 31 Dec.<br>1995                     | 30 April. <i>Monash University<br/>Act 1958, s.35B.</i>                          | 20 Feb.<br>1996                                          | 19 Mar.<br>1996                                     |
| Monash Ultrasound Pty Ltd                                              | 31 Dec.<br>1995                     | " "                                                                              | 16 Jan.<br>1996                                          | 19 Mar.<br>1996                                     |
| Monash Ultrasound Trust                                                | 31 Dec.<br>1995                     | " "                                                                              | 16 Jan.<br>1996                                          | 19 Mar.<br>1996                                     |
| Monash University Foundation<br>Pty Ltd                                | 31 Dec.<br>1995                     | " "                                                                              | 4 Mar.<br>1996                                           | 22 Mar.<br>1996                                     |
| Monash University Foundation<br>Trust                                  | 31 Dec.<br>1995                     | " "                                                                              | 4 Mar.<br>1996                                           | 22 Mar.<br>1996                                     |
| Montech Pty Ltd                                                        | 31 Dec.<br>1995                     | " "                                                                              | 24 Jan.<br>1996                                          | 19 Mar.<br>1996                                     |
| Mycell International Pty Ltd                                           | 31 Dec.<br>1995                     | 30 April. <i>Latrobe University<br/>Act 1964, s.37A</i>                          | 18 Mar.<br>1996                                          | 29 Mar.<br>1996                                     |
| Neurometric Systems Pty Ltd                                            | 31 Dec.<br>1995                     | 30 April. <i>Swinburne<br/>University of Technology<br/>Act 1992, s.44.</i>      | 29 Feb.<br>1996                                          | 13 Mar.<br>1996                                     |
| Opening Learning Agency of<br>Australia Pty Ltd                        | 31 Dec.<br>1995                     | 30 April. <i>Monash University<br/>Act 1958, s.35B.</i>                          | 25 Jan.<br>1996                                          | 19 Mar.<br>1996                                     |
| RMIT                                                                   | 31 Dec.<br>1995                     | 30 April. <i>Royal Melbourne<br/>Institute of Technology Act<br/>1992, s.42.</i> | 25 Mar.<br>1996                                          | 1 April<br>1996                                     |
| RMIT Foundation                                                        | 31 Dec.<br>1995                     | 30 April. <i>Royal Melbourne<br/>Institute of Technology Act<br/>1992, s.39.</i> | 25 Mar.<br>1996                                          | 1 April<br>1996                                     |
| RMIT Ltd                                                               | 31 Dec.<br>1995                     | " "                                                                              | 22 Mar.<br>1996                                          | 1 April<br>1996                                     |

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**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                            | <i>Financial<br/>year<br/>ended</i> | <i>Reporting to Parliament</i>                                                   | <i>Financial<br/>statements<br/>signed by<br/>entity</i> | <i>Auditor-<br/>General's<br/>report<br/>signed</i> |
|----------------------------------------------------------|-------------------------------------|----------------------------------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------------|
| <b>COMPLETED AUDITS - continued</b>                      |                                     |                                                                                  |                                                          |                                                     |
| <i>Post-secondary education institutions - continued</i> |                                     |                                                                                  |                                                          |                                                     |
| <i>Universities and associated companies - continued</i> |                                     |                                                                                  |                                                          |                                                     |
| RMIT Malaysia                                            | 31 Dec.<br>1995                     | 30 April. <i>Royal Melbourne<br/>Institute of Technology Act<br/>1992, s.39.</i> | 22 Mar.<br>1996                                          | 1 April<br>1996                                     |
| RMIT Union                                               | 31 Dec.<br>1995                     | " "                                                                              | 25 Mar.<br>1996                                          | 1 April<br>1996                                     |
| School of Forestry Creswick Ltd                          | 31 Dec.<br>1995                     | 31 April. <i>Melbourne<br/>University Act 1958, s.41.</i>                        | 13 Feb.<br>1996                                          | 29 Feb.<br>1996                                     |
| Sir John Monash Business<br>Centre Pty Ltd               | 31 Dec.<br>1995                     | 30 April. <i>Monash University<br/>Act 1958, s.35b.</i>                          | 6 Feb.<br>1996                                           | 9 Feb.<br>1996                                      |
| Swinburne Ltd                                            | 31 Dec.<br>1995                     | 30 April. <i>Swinburne<br/>University of Technology<br/>Act 1992, s.45.</i>      | 6 Mar.<br>1996                                           | 29 Mar.<br>1996                                     |
| Swinburne University of<br>Technology                    | 31 Dec.<br>1995                     | 30 April. <i>Swinburne<br/>University of Technology<br/>Act 1992, s.45.</i>      | 6 Mar.<br>1996                                           | 29 Mar.<br>1996                                     |
| Technisearch Ltd                                         | 31 Dec.<br>1995                     | 30 April. <i>Royal Melbourne<br/>Institute of Technology Act<br/>1992, s.39.</i> | 22 Mar.<br>1996                                          | 1 April<br>1996                                     |
| Unilink                                                  | 31 Dec.<br>1995                     | 30 April. <i>Deakin University<br/>Act 1974, s.34A.</i>                          | 1 Mar.<br>1996                                           | 20 Mar.<br>1996                                     |
| Unimelb Ltd                                              | 31 Dec.<br>1995                     | 30 April. <i>Melbourne<br/>University Act 1958, s.41.</i>                        | 18 Mar.<br>1996                                          | 1 April<br>1996                                     |
| University of Ballarat                                   | 31 Dec.<br>1995                     | 30 April. <i>University of<br/>Ballarat Act 1993, s.40.</i>                      | 27 Mar.<br>1996                                          | 28 Mar.<br>1996                                     |
| University of Melbourne                                  | 31 Dec.<br>1995                     | 30 April. <i>Melbourne<br/>University Act 1958 s.41.</i>                         | 10 April<br>1996                                         | 10 April<br>1996                                    |
| Victoria University of<br>Technology                     | 31 Dec.<br>1995                     | 30 April. <i>Victoria University<br/>of Technology Act 1990,<br/>s.44.</i>       | 22 Mar.<br>1996                                          | 28 Mar.<br>1996                                     |
| Victoria University of<br>Technology Foundation Ltd      | 31 Dec.<br>1995                     | 30 April. <i>Victoria University<br/>of Technology Act 1990,<br/>s.42.</i>       | 29 Mar.<br>1996                                          | 1 April<br>1996                                     |
| Victorian College of Agriculture<br>and Horticulture Ltd | 31 Dec.<br>1995                     | 30 April. <i>Financial<br/>Management Act 1994,<br/>s.46.</i>                    | 18 Mar.<br>1996                                          | 20 Mar.<br>1996                                     |
| Victorian College of the Arts                            | 31 Dec.<br>1995                     | " "                                                                              | 7 Mar.<br>1996                                           | 20 Mar.<br>1996                                     |
| Western Melbourne Business<br>Developments<br>Pty Ltd    | 31 Dec.<br>1995                     | 30 April. <i>Victoria University<br/>of Technology Act 1990,<br/>s.42.</i>       | 22 Mar.<br>1996                                          | 28 Mar.<br>1996                                     |

**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                                        | <i>Financial<br/>year<br/>ended</i> | <i>Reporting to Parliament</i>                                | <i>Financial<br/>statements<br/>signed by<br/>entity</i> | <i>Auditor-<br/>General's<br/>report<br/>signed</i> |
|----------------------------------------------------------------------|-------------------------------------|---------------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------------|
| <b>COMPLETED AUDITS - continued</b>                                  |                                     |                                                               |                                                          |                                                     |
| <b><i>Institutes/Colleges of Technical and Further Education</i></b> |                                     |                                                               |                                                          |                                                     |
| Barton (b)                                                           | 31 Dec.<br>1995                     | 30 April. <i>Financial<br/>Management Act 1994,</i><br>s.46.  | 28 Feb.<br>1996                                          | 19 Mar.<br>1996                                     |
| Box Hill                                                             | 31 Dec.<br>1995                     | " "                                                           | 29 Feb.<br>1996                                          | 20 Mar.<br>1996                                     |
| Casey (c)                                                            | 31 Dec.<br>1995                     | " "                                                           | 22 Mar.<br>1996                                          | 26 Mar.<br>1996                                     |
| Central Gippsland                                                    | 31 Dec.<br>1995                     | " "                                                           | 27 Mar.<br>1996                                          | 15 April<br>1996                                    |
| Driver Education Centre of<br>Australia Ltd                          | 31 Dec.<br>1995                     | 30 April. <i>Financial<br/>Management Act 1994,</i><br>s.53A. | 22 Mar.<br>1996                                          | 22 Mar.<br>1996                                     |
| East Gippsland                                                       | 31 Dec.<br>1995                     | " "                                                           | 15 Mar.<br>1996                                          | 20 Mar.<br>1996                                     |
| Gordon Institute                                                     | 31 Dec.<br>1995                     | " "                                                           | 7 Mar.<br>1996                                           | 14 Mar.<br>1996                                     |
| Goulburn Valley                                                      | 31 Dec.<br>1995                     | 30 April. <i>Financial<br/>Management Act 1994,</i><br>s.46.  | 13 Mar.<br>1996                                          | 20 Mar.<br>1996                                     |
| Holmesglen                                                           | 31 Dec.<br>1995                     | 30 April. <i>Financial<br/>Management Act 1994,</i><br>s.46.  | 13 Mar.<br>1996                                          | 22 Mar.<br>1996                                     |
| John Batman                                                          | 31 Dec.<br>1995                     | " "                                                           | 14 Mar.<br>1996                                          | 26 Mar.<br>1996                                     |
| Kangan (d)                                                           | 31 Dec.<br>1995                     | " "                                                           | 13 Mar.<br>1996                                          | 25 Mar.<br>1996                                     |
| Loddon-Campaspe                                                      | 31 Dec.<br>1995                     | " "                                                           | 5 Mar.<br>1996                                           | 19 Mar.<br>1996                                     |
| Melbourne College of Textiles                                        | 31 Dec.<br>1995                     | " "                                                           | 5 Mar.<br>1996                                           | 19 Mar.<br>1996                                     |
| Northern Metropolitan                                                | 31 Dec.<br>1995                     | " "                                                           | 21 Feb.<br>1996                                          | 29 Feb.<br>1996                                     |
| Outer Eastern                                                        | 31 Dec.<br>1995                     | " "                                                           | 22 Mar.<br>1996                                          | 26 Mar.<br>1996                                     |
| Peninsula Institute (e)                                              | 31 Dec.<br>1995                     | " "                                                           | 26 Feb.<br>1996                                          | 19 Mar.<br>1996                                     |
| School of Mines and Industries<br>Ballarat Ltd                       | 31 Dec.<br>1995                     | " "                                                           | 21 Feb.<br>1996                                          | 23 Feb.<br>1996                                     |
| South West                                                           | 31 Dec.<br>1995                     | " "                                                           | 13 Mar.<br>1996                                          | 25 Mar.<br>1996                                     |

SCHEDULE B  
COMPLETED/INCOMPLETE AUDITS - *continued*

| <i>Entity</i>                                                                    | <i>Financial<br/>year<br/>ended</i> | <i>Reporting to Parliament</i>                                | <i>Financial<br/>statements<br/>signed by<br/>entity</i> | <i>Auditor-<br/>General's<br/>report<br/>signed</i> |
|----------------------------------------------------------------------------------|-------------------------------------|---------------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------------|
| <b>COMPLETED AUDITS - <i>continued</i></b>                                       |                                     |                                                               |                                                          |                                                     |
| <b><i>Institutes/Colleges of Technical and Further Education - continued</i></b> |                                     |                                                               |                                                          |                                                     |
| Sunraysia                                                                        | 31 Dec.<br>1995                     | 30 April. <i>Financial<br/>Management Act 1994,<br/>s.46.</i> | 13 Mar.<br>1996                                          | 25 Mar.<br>1996                                     |
| Wangaratta                                                                       | 31 Dec.<br>1995                     | " "                                                           | 15 Mar.<br>1996                                          | 19 Mar.<br>1996                                     |
| Western Metropolitan                                                             | 31 Dec.<br>1995                     | " "                                                           | 19 Mar.<br>1996                                          | 25 Mar.<br>1996                                     |
| William Angliss                                                                  | 31 Dec.<br>1995                     | 30 April. <i>Financial<br/>Management Act 1994,<br/>s.46.</i> | 20 Mar.<br>1996                                          | 26 Mar.<br>1996                                     |
| Wimmera Community                                                                | 31 Dec.<br>1995                     | " "                                                           | 5 Mar.<br>1996                                           | 22 Mar.<br>1996                                     |
| Wodonga                                                                          | 31 Dec.<br>1995                     | " "                                                           | 26 Mar.<br>1996                                          | 26 Mar.<br>1996                                     |

(a) Monash ANZ Centre of International Briefing Pty Ltd ceased operation on 31 Oct. 1995. Net assets transferred to Monash International Pty Ltd.

(a) Barton Institute of TAFE was previously known as Moorabin College of TAFE.

(b) Casey Institute of TAFE was previously known as Dandenong College of TAFE.

(c) Kangan Institute of TAFE was previously known as Broadmeadows College of TAFE.

(d) Peninsula Institute of TAFE was previously known as Frankston College of TAFE.

# Part 3.2

## Human Services

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**KEY FINDINGS**

**Related party disclosures in the public hospital sector**

- The failure by 5 public hospitals to disclose necessary details of business dealings with director-related parties resulted in an audit qualification of their financial statements.  
*Paras 3.2.4 to 3.2.6*

**Follow-up review of visiting medical officer arrangements at public hospitals**

- While a number of hospitals have made significant steps to improve controls over payments to Visiting Medical Officers (VMOs), further work needs to be done, particularly in improving the standard of record keeping and adhering to established procedures. To facilitate the process, the Department of Human Services should, as a condition of funding, require hospitals to have in place appropriate accountability procedures.  
*Paras 3.2.18 to 3.2.24*
- Significant savings can be made by medium-sized regional hospitals moving to revised VMO engagement arrangements. There is a need for the Department to work with these hospitals to ensure that uneconomic fee-for-service arrangements do not continue.  
*Paras 3.2.25 to 3.2.30*
- There is scope for the Department to be involved in encouraging hospitals to develop appropriate information systems which capture sufficient and reliable data to enable the workload of individual VMOs to be monitored on an ongoing basis.  
*Paras 3.2.37 to 3.2.40*
- The Department should re-assess and clarify its responsibilities in ensuring a strong and consistent accountability framework in the public hospital system.  
*Paras 3.2.41 to 3.2.44*



**3.2.1** The Minister for Health, the Minister for Aged Care, the Minister for Youth and Community Services, the Minister for Housing and the Minister responsible for Aboriginal Affairs, have responsibility for operations within the Human Services sector. These Ministers have collective responsibility for the Department of Human Services.

**3.2.2** Details of the specific ministerial responsibilities for public bodies within the Human Services sector are listed in Table 3.2A. These public bodies, together with the former Departments of Health and Community Services, and Planning and Development were subject to audit by the Auditor-General during the 1994-95 financial year.

**TABLE 3.2A  
MINISTERIAL RESPONSIBILITIES FOR PUBLIC BODIES  
WITHIN THE HUMAN SERVICES SECTOR**

| <i>Ministerial portfolio</i> | <i>Entities subject to audit</i>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
|------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Aboriginal Affairs</b>    | -                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |
| <b>Aged Care</b>             | -                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |
| <b>Community Services</b>    | -                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |
| <b>Health</b>                | Advanced Dental Technicians Qualifications Board<br>Ambulance Officers' Training Centre<br>Ambulance Services (7)<br>Anti-Cancer Council of Victoria<br>Chiropodists Registration Board<br>Chiropractors and Osteopaths Registration Board<br>Dental Board of Victoria<br>Dental Technicians Licensing Committee<br>Health Computing Service Victoria Ltd.<br>Medical Practitioners Board of Victoria<br>Mental Health Review Board<br>Nurses Board of Victoria<br>Optometrists Registration Board<br>Pharmacy Board of Victoria<br>Physiotherapists Registration Board<br>Prince Henry's Institute of Medical Research<br>Psychologists Registration Board<br>Psychosurgery Review Board<br>Public hospitals and nursing homes (138)<br>Trustees of the Anderson's Creek Cemetery Trust<br>Trustees of the Ballarat General Cemetery Trust<br>Trustees of the Bendigo Cemeteries Trust<br>Trustees of the Cheltenham Cemeteries Trust<br>Trustees of the Fawkner Crematorium and Memorial Park<br>Trustees of the Geelong Cemeteries Trust<br>Trustees of the Keilor Cemetery Trust<br>Trustees of the Memorial Park Altona<br>Trustees of the Mildura Cemetery Trust<br>Trustees of the Necropolis Springvale<br>Trustees of the Preston Cemetery Trust<br>Trustees of the Templestowe Cemetery Trust<br>Trustees of the Werribee Cemetery Trust<br>Trustees of the Lilydale Memorial Park and Cemetery<br>Victorian Health Promotion Foundation<br>Victorian Psychological Council |
| <b>Housing</b>               | -                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |
| <b>Youth</b>                 | -                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |



**3.2.3** Comment on matters of significance arising from the audit of entities within the Human Services sector is provided below.

**RELATED PARTY DISCLOSURES IN THE PUBLIC HOSPITAL SECTOR**

**3.2.4** The Minister for Finance has set out the financial reporting framework for public sector entities, including public hospitals, in Directions issued pursuant to the *Financial Management Act 1994*. Under the Directions, a hospital is required to disclose in its financial statements information regarding transactions that have occurred between the hospital and a member of its Board of Directors or any party related to a director. Information to be disclosed includes the aggregate amount and nature of each type of transaction and the names of the directors concerned.

**3.2.5** During the financial audit of Victorian public hospitals for the 1994-95 financial year, it was found that a number of hospital boards did not disclose details of business dealings with director-related parties on the grounds that such transactions were commercially confidential. While the required information was eventually included in most hospital financial statements, 5 hospitals failed to disclose the aggregate amount of each service provided to the hospital by a director and/or director-related party as required by the Directions. The failure to disclose all of the required information resulted in an audit qualification of their financial statements.

**3.2.6** Directors hold positions of great responsibility within public hospitals and therefore it is important for all details relating to transactions between hospitals and directors (or director-related parties) to be appropriately disclosed in the financial statements as required by the Directions of the Minister for Finance. **These Directions follow representations by my Office in the May 1994 Report on Ministerial Portfolios and the Minister for Finance is to be commended for taking appropriate action to improve corporate governance in the public sector. The argument advanced by several hospitals that such dealings are commercially confidential is, in my opinion, patently absurd.**





**FOLLOW UP REVIEW OF VISITING MEDICAL OFFICER ARRANGEMENTS AT PUBLIC HOSPITALS**

**Introduction**

**3.2.7** Medical services within the Victorian public hospital system are provided by approximately 2 400 medical officers as well as private practitioners engaged by hospitals as Visiting Medical Officers (VMOs).

**3.2.8** For many years, VMOs have been paid either under the:

- fee-for-service system where VMOs are paid for each medical service provided to public patients; or
- sessional system where VMOs are engaged to attend public patients for specified sessions, usually of 3½ hours duration.

**3.2.9** Within the next few years it is expected that a new system, to be known as the "fractional system", will be introduced by public hospitals to replace existing sessional and certain fee-for-service arrangements. Under a fractional system, VMOs are engaged on the basis of an estimated weekly time commitment required to meet defined public hospital responsibilities. However, VMOs will not, necessarily, be required to attend the hospital at specified times. The fractional system encompasses other responsibilities such as management duties, quality assurance processes and education and training commitments which were not adequately addressed under the sessional or fee-for-service systems.

**Previous audit report on VMO arrangements**

**3.2.10** The Auditor-General's April 1993 *Special Report No. 21 - Visiting Medical Officer Arrangements*, identified serious deficiencies in the controls and accountability arrangements exercised by public hospitals over expenditure on VMO services. Many of these deficiencies had previously been identified by the Parliament's Economic and Budget Review Committee (EBRC) in its report issued in 1985 titled *Report of the Inquiry into the method of Remuneration for visiting medical staff at Public Hospitals*.

**3.2.11** Key findings of the Auditor-General's Special Report on VMOs included:

- Payments for VMO services were not supported by documentary evidence that such services had been provided;
- There was significant potential to reduce public health costs through the use of sessional VMO arrangements by medium-sized hospitals, as opposed to their use of the fee-for-service system; and
- Even though deficiencies in accountability and monitoring arrangements had been known to exist for many years only minimal action had been taken by the former Department of Health and Community Services to address identified deficiencies. Further, when individual hospitals had attempted to introduce enhanced arrangements, support was not forthcoming from the Department.



Other reviews

**3.2.12** Since the initial audit review there have been reviews undertaken by the Parliament and the Minister for Health, which have examined the accountability and monitoring arrangements for VMOs.

**3.2.13** The Parliament's Public Accounts and Estimates Committee (PAEC), in view of the ongoing nature of the problems identified in the Auditor-General's 1993 Special Report and other concerns, conducted a further inquiry into VMO arrangements. The PAEC review confirmed the audit findings and, among the many recommendations included in its May 1994 report, suggested that the Department include in the conditions of hospital funding specific clauses requiring improved VMO accountability processes.

**3.2.14** In August 1994, the Minister for Health established a panel to review a broad range of issues relating to medical staffing in the public hospital system. The Panel's June 1995 report (the Lochtenberg report) made a number of recommendations aimed at increasing the flexibility available to hospitals in medical staffing and improving accountability in engagement arrangements. In relation to engagement arrangements, it was recommended that a fractional system be introduced to replace sessional appointment of specialists and those fee-for-service appointments where services are provided by specialists and general practitioners on a regular and substantial basis.

**3.2.15** The Lochtenberg report findings are currently being implemented by the Metropolitan Healthcare Networks and regional hospitals using sessional arrangements. Implementation of the recommendations at regional hospitals using fee-for-service arrangements has been deferred for a 2 year period, until July 1997, under a moratorium granted by the Minister for Health.

Current audit review

**3.2.16** It was against a background of wide-ranging reforms in the healthcare sector, including the introduction of casemix funding and the establishment of Metropolitan Healthcare Networks, that the Auditor-General determined to carry out a follow-up review of VMO arrangements to assess whether improvements in accountability had been made. The decision to undertake the review was strongly supported by the PAEC.

**3.2.17** Comments on findings from the 1996 audit review follow.

*Fee-for-service arrangements*

**3.2.18** Fee-for-service arrangements are used in the majority of Victoria's non-metropolitan hospitals and in the small and medium-sized hospitals within the Metropolitan Healthcare Networks.



**3.2.19** The Auditor-General's 1993 Special Report found that Hospitals using fee-for-service arrangements had inadequate VMO claims monitoring and accountability processes, and that there was *prima facie* evidence of over-servicing of public patients. Given that the hospitals had encountered difficulty in implementing change due to strong resistance by certain VMOs, audit suggested there was a need for the Department to assist hospitals to address the accountability deficiencies identified and to utilise system-wide statistical data to guard against over-servicing.

**3.2.20** **The current audit review of a number of regional hospitals found that some hospitals had taken significant steps to improve controls over payments to VMOs.** Procedures implemented by hospitals included:

- VMOs to record details of each service delivered;
- the update of patient medical records by VMOs at each visit;
- the matching of VMO claims to patient medical records prior to payment of claims;
- medical staff to review and monitor VMOs claims; and
- financial and clinical audits of VMO claims.

**3.2.21** However, audit found that there were inconsistencies in the standard of record keeping and that established procedures were not always followed.

**3.2.22** In respect to measures taken to guard against over-servicing, the current review found that, although the total outputs of the various specialist services could be monitored by hospital management, information systems did not enable the managers to regularly review the outputs of individual VMOs. Accordingly, managers were not in a position to review individual VMO claim patterns as a means of detecting potential over-servicing.

**3.2.23** Furthermore, while the Department had indicated in its response to the Auditor-General's 1993 Special Report that it intended to consider using statistical data to detect potential over-servicing, the current audit review found that no action had been taken in this area.

**3.2.24** **Given that the fee-for-service system will continue in the smaller regional hospitals, the Department of Human Services should include, in conditions of funding, specific clauses requiring hospitals to have in place appropriate accountability procedures.**

*Fee-for-service arrangements in medium-sized public hospitals*

**3.2.25** The Auditor-General's Special Report identified that there was potential for medium-sized fee-for-service hospitals with increasing patient throughput to reduce their VMO costs by introducing sessional arrangements. The Report stated that "*... the failure of the Department to act on the EBRC's recommendation to introduce sessional VMO arrangements at the Mornington Peninsula Hospital and 15 other hospitals has resulted in the State forgoing savings in excess of \$50 million since 1986. These savings are predicated on the immediate acceptance by VMOs of sessional arrangements at these hospitals.*"



**3.2.26** Since that Report, the Mornington Peninsula Hospital moved to a modified fee-for-service system and, in November 1995, began progressively implementing fractional appointment contracts for a large portion of its VMO requirements. When compared with the cost of VMO arrangements in 1993-94, the revised arrangements are expected to result in a saving of \$1.7 million in 1995-96.

**3.2.27** The other 15 hospitals referred to are still operating on a fee-for-service system. Of these, 5 now form part of the Metropolitan Healthcare Networks and are to progressively convert to fractional appointments. The remaining 10 are regional hospitals which have been unable to negotiate a move to a sessional system.

*Continuation of the uneconomic fee-for-service system*

**3.2.28** An analysis of the VMO costs incurred by the 10 regional hospitals for the period 1 July 1993 to 31 December 1995 revealed that under their existing fee-for-service arrangements they were paying their VMOs substantially in excess of the related casemix payment. **On average, the hospitals were currently spending around 50 per cent more on VMO costs than the related funding element. The hospitals have estimated that losses on their VMO arrangements for the 1995-96 year will total around \$12 million.** The unfunded VMO costs will be met from funding provided for other hospital activities.

**3.2.29** Issues relating to uneconomic fee-for-service arrangements were first raised by the EBRC in 1985. The introduction of casemix funding has further highlighted the financial impact on individual hospitals. However, the issue of a moratorium regarding the introduction of fractional arrangements in regional Victoria effectively prevents hospitals from taking immediate action to address the problem.

**3.2.30** **In audit view, there is a critical need for the Department of Human Services to commence work with these hospitals to ensure that uneconomic fee-for-service arrangements do not continue beyond the moratorium period of 30 June 1997.**

*□ RESPONSE provided by Secretary, Department of Human Services*

*Each public hospital provides specialist medical services by either directly employing the medical officers on a full-time or sessional basis, or by contracting on a fee for service basis.*

*Generally, larger metropolitan and rural hospitals find it more practical and economic to obtain medical services by directly employing medical partitioners. Conversely, medium and smaller rural hospitals find it more economic to purchase medical services on an output basis rather than through the employment of a medical officer, although the availability of medical practitioners in rural areas will in most cases restrict their choice to the latter. Many contractors have indicated to hospital boards that they would not enter into sessional arrangements relating to more efficient engagement of medical partitioners in both large and medium hospitals.*

*The hospitals estimates that fee-for-service arrangements will cost \$12 million in 1995-96 is higher than other available estimates. Data published in "Victorian Hospital Comparative Data 1003/94" (at the time of writing 1994-95 data was not available) details the following average medical costs for hospital Groups.*



MEDICAL TREATMENT COST  
PER "PUBLIC WIES"

|          |       |
|----------|-------|
| Group A1 | \$598 |
| Group A2 | \$462 |
| Group B  | \$555 |

*The figures above indicate that the costs of medical services supplied at Group B hospitals (including those large rural hospitals examined in the Auditor-General's Report) are about 7 per cent less than Group A1 (large metropolitan hospitals) and about 20 per cent more than group A2 (large specialist metropolitan hospitals) with the latter hospitals directly employing medical practitioners.*

**Sessional arrangements**

**3.2.31** Sessional arrangements operate in the larger hospitals within the Metropolitan Healthcare Networks as well as the Geelong, Ballarat and Bendigo Hospitals. Under sessional arrangements, VMOs remuneration is based on rates applicable to specialist full-time medical officers and includes a 37.5 per cent loading to cover travelling time, self-funded superannuation and other related expenses.

**3.2.32** Where VMOs are rostered to provide medical services outside normal hours, referred to as out-of-hours sessions, they are entitled to receive:

- on-call payments, generally equivalent to 25 per cent of the standard sessional rate, to be paid where VMOs are available to be consulted by a hospital but are not necessarily required to physically attend the hospital; and
- re-call payments, in the event that a VMO is required to return to duty to attend public patients the VMO receives the applicable sessional on-call payment together with an additional allowance to cover time spent at the hospital and travelling time.

**3.2.33** The Auditor-General's 1993 Special Report identified a number of weaknesses in the accountability arrangements for sessional VMOs. In particular, audit found that:

- sessional hospitals did not have documentation and monitoring mechanisms in place to ensure that VMOs had actually provided services claimed prior to making payment for those services; and
- the majority of hospitals had not developed systems to monitor out-of-hours work conducted by VMOs.

**3.2.34** In the current review, audit was pleased to find that a number of Hospitals had taken steps to improve controls over payments to VMOs. For example, VMOs claims were required to be supported by details of sessional attendance and on-call and re-call services provided. In a number of cases, these details were then checked and verified by medical administrators before payments were made.



**3.2.35** While acknowledging that significant improvements have been made in the accountability arrangements for VMOs, audit is of the view that further enhancements could be implemented. In particular:

- There were inconsistencies in the standard of record keeping and checking by Hospitals. For example, VMOs' claims were often accepted even though all required information was not provided; and
- Although information detailing sessional costs, the extent of on-call and re-call hours and number of patients treated for each speciality was generally available, this information was typically recorded on separate systems and was not routinely consolidated into management reports. Accordingly, the effectiveness of this information as a management and monitoring tool was restricted, particularly in regard to monitoring the relative outputs of each VMO to ensure an optimal allocation of sessions.

**3.2.36** Audit was advised that hospitals will replace current sessional arrangements with the new fractional system. In audit view, the abovementioned deficiencies will adversely impact on the level of accountability provided by hospitals under the new system. Therefore, **hospitals will need to improve current information systems to enable the outputs of VMOs to be monitored under the fractional system.**

*□ RESPONSE provided by Secretary, Department of Human Services*

*The Department has established an industry-based committee to oversee and identify the information technology needs of hospitals. Considerable progress has already been made in establishing business rules, and functional specifications and identifying potential technology platforms.*

*Fractional appointments*

**3.2.37** The Lochtenberg report recommended that hospitals introduce a fractional system to replace the sessional appointment of specialists and those fee-for-service arrangements for specialist services required on a regular and substantial basis. The panel considered that fractional appointments would overcome the difficulty of verifying VMOs' attendance and envisaged that the monitoring of VMOs' performance would be through a quality assurance and peer review process established by the hospital. The panel also outlined a mechanism for the annual performance appraisal of VMOs together with the need for variations to their fractional allocation, based on actual workload and the ongoing needs of the hospital, at the conclusion of each year.

**3.2.38** Audit agrees that quality assurance and peer review processes are important to ensure the quality of services provided by VMOs. However, the inability of current hospital information systems to capture sufficient and reliable data, to enable the workload of individual VMOs to be monitored on an ongoing basis, will restrict a hospital's capacity to conduct the annual performance assessment of its VMOs. This will seriously undermine the hospital's control over the fractional appointments system.



**3.2.39** While audit acknowledges that a number of hospitals are in the process of refining existing systems and procedures to capture such information, there are concerns that the need for a consistent industry-wide approach to the problem is not being addressed. Moreover, the cost of addressing this problem on a hospital-by-hospital basis is likely to be substantially more than if an industry-wide approach was utilised.

**3.2.40** In audit view, there is scope for the Department of Human Services to be involved in specifying minimum data requirements and encouraging the development of appropriate information systems, to ensure that the outputs of fractionally appointed VMOs can be adequately monitored, at the hospital level, on a basis that is consistent throughout the industry.

**Role of the Department in the management of public hospitals**

**3.2.41** In response to audit comments in the Auditor-General's Special Report regarding the role of the Department in ensuring hospitals have adequate VMO accountability procedures, the Department maintained that, under the *Health Services Act 1988*, public hospitals are given the status of autonomous corporate bodies. In these circumstances, the Department was of the view that it was not appropriate for the Department to specify detailed accountability requirements for the hospitals.

**3.2.42** In recent years, the Department has also changed the focus of its role to that of a purchaser of services from public hospitals rather than being a service provider itself through the public hospital system. It considers that the introduction of casemix funding, based on outputs, and a service agreement, which specifies the level and type of services purchased from individual hospitals, reinforces this role. It maintains that taxpayers have some protection from waste and mismanagement through casemix funding which ensures hospitals are paid on a consistent basis for medical services supplied.

*Departmental activities contradict its stated role*

**3.2.43** Although the Department maintained that it was not appropriate to issue policy directives to public hospitals in regard to VMO accountability arrangements, the audit review found that notwithstanding this position:

- the Department had issued around 130 guidelines and policy directives to public hospitals during the last 3 years in regard to regulatory, clinical, funding and other matters;
- most Health Service Agreements between the Department and individual public hospitals included clauses specifying performance measures and accountability requirements in regard to certain other hospital activities such as aged care programs; and
- the Department had been involved in providing additional assistance and directions to certain public hospitals which had financial viability problems arising from various factors, including difficulties relating to the engagement of VMOs.



**3.2.44** In audit opinion, the Department needs to re-assess and clarify its responsibilities in managing the public hospital system to ensure the operation of a strong and consistent accountability framework for all areas of public hospital activity.

*□ RESPONSE provided by Secretary, Department of Human Services*

*The Report correctly notes that the Department views itself as a purchaser of services from public hospitals, and not as a direct service provider. This is supported by section 40A of the Health Services Act 1988 which states that hospitals are independent entities managed by a Board of Directors. The Department has accountability requirements concerning outputs, quality, expenditure of government funds and financial viability to support its role as a purchaser, but hospitals are expected to make their own arrangements when dealing with inputs such as staff, contractors or other suppliers. Therefore, it is not considered appropriate to detail specific accountability for one particular input. The review acknowledges that hospitals have been responsible for making significant improvements in accountability arrangements. The management and implementation of all policies are the statutory responsibility of hospital boards. Each hospital's external auditors should bring to the attention of hospital boards all sub-standard accounting and management practices.*

**SCHEDULE A  
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS**

| <i>Report</i> | <i>Subject</i> | <i>Status at date of preparation of this Report</i> |
|---------------|----------------|-----------------------------------------------------|
|---------------|----------------|-----------------------------------------------------|

|                                             |
|---------------------------------------------|
| <b>MATTERS RESOLVED OR ACTION COMMENCED</b> |
|---------------------------------------------|

**DEPARTMENT OF HEALTH**

|                                                             |                                                                                                                                                                               |                                                                                                                                                                                        |
|-------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p><i>Ministerial Portfolios, May 1995, pp.107-108.</i></p> | <p>The real value of financial assistance provided to eligible recipients of municipal, water and sewerage rate concessions has been substantially eroded over the years.</p> | <p>The Government has established a Cabinet Sub-Committee to undertake a review of rate concessions with a view to determining their continuing relevance, structure and adequacy.</p> |
|-------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

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|--------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p><i>Ministerial Portfolios, May 1995, p.109.</i></p> | <p>No co-ordination of publicity strategies for the advertising of rate concessions on a Statewide basis resulting in variations in the quality and level of advertising across rating authorities and a lack of published material in languages other than English.</p> | <p>Responsibility for publicity awareness initiatives has been consolidated within the Concessions Unit of the Department. A number of advertising brochures outlining the operation of the concessions scheme are currently in the process of finalisation and are to be used on a Statewide basis. The Concessions Unit is currently investigating the use of additional languages in advertising brochures.</p> |
|--------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

**DEPARTMENT OF PLANNING AND DEVELOPMENT**

|                                                            |                                                                                                                                                                                                                                                                            |                                                                                                                                                                                                         |
|------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p><i>Ministerial Portfolios, May 1993, pp. 228-9.</i></p> | <p>Until such time as the Department determines the physical condition of all its properties, which may take another 7 years, it will not have a sound basis for prioritising the allocation of its maintenance funds nor for determining future funding requirements.</p> | <p>A survey of the condition of all departmental rental properties was completed in December 1995. The report is currently being reviewed by management to consider the implications of the survey.</p> |
|------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

|                                                            |                                                                                                                                                                                                                                                                         |                                                                                                                                    |
|------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------|
| <p><i>Ministerial Portfolios, May 1993, pp. 238-9.</i></p> | <p>At December 1993, the State's net financial contribution to the Home Opportunity Loans Scheme (HOLS) totalled \$34.1 million (31 December 1992, \$28.9 million) and a further \$6.5 million has been set aside to meet any cash flow difficulties of the Scheme.</p> | <p>At December 1995, the State's net financial contribution to HOLLS totalled \$75 million (31 December 1994, \$59.3 million).</p> |
|------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------|

|                                                           |                                                                                                                                          |                                                                                                                                                                                                                                       |
|-----------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p><i>Ministerial Portfolios, May 1994 pp. 324-5.</i></p> | <p>Substantial losses continue to be incurred by HOLLS due to property sales as a result of borrowers defaulting on loan repayments.</p> | <p>The Department has set aside funds in a specific purpose capital support account to meet any future funding needs of HOLLS. The total of such funds at 31 December 1995 was \$110.3 million (31 December 1994, \$90.3 million)</p> |
|-----------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

|                                                         |                                                                                                                                          |                                                                                                                                                                                                                                                                                                                                                                                                       |
|---------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p><i>Ministerial Portfolios, May 1993, p. 240.</i></p> | <p>Substantial losses continue to be incurred by HOLLS due to property sales as a result of borrowers defaulting on loan repayments.</p> | <p>The operating result of the Scheme continued to deteriorate during 1994-95 with the deficit increasing from \$13 million in 1993-94 to \$18 million in 1994-95. The increased deficit was due mainly to the high cost of long-term borrowings and a decrease in interest income received from the mortgage portfolio, which decreased from \$780 million (1993-94) to \$708 million (1994-95).</p> |
|---------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

*Ministerial Portfolios, May 1994, p. 326.*



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**SCHEDULE A**  
**STATUS OF MATTERS RAISED IN PREVIOUS REPORTS - continued**

| <i>Report</i>                                             | <i>Subject</i>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    | <i>Status at date of preparation of this Report</i>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |
|-----------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>MATTERS RESOLVED OR ACTION COMMENCED</b>               |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                   |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |
| <b>DEPARTMENT OF PLANNING AND DEVELOPMENT - continued</b> |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                   |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |
| <i>Ministerial Portfolios, May 1995, p. 176.</i>          | Further initiatives to enhance the performance and management of HOLS were considered by the Department in term of the future structure of the Scheme. The formation of a departmental interest rate review committee and the development of a risk management strategy for HOLS assets and liabilities.<br><br>In April 1995, as part of the above initiatives, the Government announced a proposal in introduce legislation to facilitate more effective risk management of the assets and liabilities of HOLS. | The <i>Treasury Corporation of Victoria (Housing Finance) Act 1995</i> received royal asset on 20 June 1995. Under the Act, HOLS will be terminated with its assets transferred to the Department and its liabilities novated to the Treasury Corporation of Victoria. This will enable the Department to directly manage interest rate risk for the mortgage assets and the liabilities.<br><br>The transfer and termination of HOLS will not be completed until various taxation issues associated with the transfer and termination are clarified by the Australian Taxation Office. |

**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS**

| <i>Entity</i>                                    | <i>Financial year/period ended</i> | <i>Reporting to Parliament</i>                        | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|--------------------------------------------------|------------------------------------|-------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS</b>                          |                                    |                                                       |                                              |                                        |
| Department of Health and Community Services      | 30 June 1995                       | 31 Oct. <i>Financial Management Act 1994</i> , s.46.  | 20 Oct. 1995                                 | 27 Oct. 1995                           |
| Department of Planning and Development           | 30 June 1995                       | " "                                                   | 28 Sept. 1995                                | 28 Sept. 1995                          |
| <b>HEALTH</b>                                    |                                    |                                                       |                                              |                                        |
| Advanced Dental Technicians Qualifications Board | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 27 Sept. 1995                                | 29 Sept. 1995                          |
| Ambulance Officers' Training Centre              | 30 June 1995                       | " "                                                   | 3 Oct. 1995                                  | 5 Oct. 1995                            |
| Alexandra and District Ambulance Service         | 30 June 1995                       | " "                                                   | 3 Oct. 1995                                  | 27 Dec. 1995                           |

**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                   | <i>Financial year/period ended</i> | <i>Reporting to Parliament</i>                       | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|-------------------------------------------------|------------------------------------|------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS - continued</b>             |                                    |                                                      |                                              |                                        |
| <b>HEALTH - continued</b>                       |                                    |                                                      |                                              |                                        |
| Ambulance Service Victoria -                    |                                    |                                                      |                                              |                                        |
| Metropolitan Region                             | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994, s.46.</i> | 1 Sept. 1995                                 | 30 Sept. 1995                          |
| North Eastern Region                            | 30 June 1995                       | " "                                                  | 15 Aug. 1995                                 | 20 Sept. 1995                          |
| North Western Region                            | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 20 Sept. 1995                          |
| South Eastern Region                            | 30 June 1995                       | " "                                                  | 15 Aug. 1995                                 | 15 Sept. 1995                          |
| South Western Region                            | 30 June 1995                       | " "                                                  | 16 Aug. 1995                                 | 22 Sept. 1995                          |
| Western Region                                  | 30 June 1995                       | " "                                                  | 16 Aug. 1995                                 | 15 Sept. 1995                          |
| Anti-Cancer Council of Victoria                 | 30 June 1995                       | " "                                                  | 27 Sept. 1995                                | 29 Sept. 1995                          |
| Chiropractors Registration Board                | 31 Dec. 1995                       | 31 Mar. <i>Financial Management Act 1994, s.46.</i>  | 12 Mar. 1996                                 | 15 Mar. 1996                           |
| Chiropractors and Osteopaths Registration Board | 31 Dec. 1995                       | " "                                                  | 16 April 1996                                | 19 April 1996                          |
| Dental Board of Victoria                        | 30 Sept. 1995                      | 31 Dec. <i>Financial Management Act 1994, s.46.</i>  | 8 Nov. 1995                                  | 10 Nov. 1995                           |
| Dental Technicians Licensing Committee          | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994, s.46.</i> | 28 Sept. 1995                                | 29 Sept. 1995                          |
| Health Computing Service Victoria Ltd.          | 30 June 1995                       | 31 Oct. <i>Financial Management Act 1994, s.53A.</i> | 8 Sept. 1995                                 | 12 Sept. 1995                          |
| Medical Practitioners Board of Victoria         | 30 Sept. 1995                      | 31 Dec. <i>Financial Management Act 1994, s.46.</i>  | 30 Nov. 1995                                 | 6 Dec. 1995                            |
| Mental Health Review Board                      | 30 June 1995                       | " "                                                  | 27 Sept. 1995                                | 29 Sept. 1995                          |
| Nurses Board of Victoria                        | 30 June 1995                       | " "                                                  | 22 Sept. 1995                                | 22 Sept. 1995                          |
| Optometrists Registration Board                 | 30 June 1995                       | " "                                                  | 18 Sept. 1995                                | 22 Sept. 1995                          |

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**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                                     | <i>Financial<br/>year/period<br/>ended</i> | <i>Reporting to Parliament</i>                              | <i>Financial<br/>statements<br/>signed by<br/>entity</i> | <i>Auditor-<br/>General's<br/>report<br/>signed</i> |
|-------------------------------------------------------------------|--------------------------------------------|-------------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------------|
| <b>COMPLETED AUDITS - continued</b>                               |                                            |                                                             |                                                          |                                                     |
| <b>HEALTH - continued</b>                                         |                                            |                                                             |                                                          |                                                     |
| Pharmacy Board of Victoria                                        | 30 June<br>1995                            | 31 Dec. <i>Financial<br/>Management Act 1994,</i><br>s.46.  | 16 Aug.<br>1995                                          | 23 Aug.<br>1995                                     |
| Physiotherapists<br>Registration Board                            | 30 June<br>1995                            | " "                                                         | 13 Sept.<br>1995                                         | 22 Sept.<br>1995                                    |
| Prince Henry's Institute of<br>Medical Research                   | 31 Dec.<br>1995                            | 31 Mar. <i>Financial<br/>Management Act 1994,</i><br>s.46.  | 26 Mar.<br>1996                                          | 26 Mar.<br>1996                                     |
| Psychosurgery Review<br>Board                                     | 30 June<br>1995                            | 30 Sept. <i>Financial<br/>Management Act 1994,</i><br>s.46. | 27 Sept.<br>1995                                         | 29 Sept.<br>1995                                    |
| Psychologists Registration<br>Board                               | 31 Dec.<br>1995                            | 31 Mar. <i>Financial<br/>Management Act 1994,</i><br>s.46.  | 30 April<br>1996                                         | 3 May<br>1996                                       |
| Trustees of the Anderson's<br>Creek Cemetery Trust                | 31 Dec.<br>1995                            | " "                                                         | 29 Mar.<br>1996                                          | 4 April<br>1996                                     |
| Trustees of the Ballarat<br>General Cemeteries and<br>Crematorium | 31 Dec.<br>1995                            | " "                                                         | 29 Feb.<br>1996                                          | 25 Mar.<br>1996                                     |
| Trustees of the Bendigo<br>Cemeteries Trust                       | 31 Dec.<br>1995                            | " "                                                         | 18 Mar.<br>1996                                          | 28 Mar.<br>1996                                     |
| Trustees of the Cheltenham<br>Cemeteries Trust                    | 31 Dec.<br>1995                            | " "                                                         | 29 Mar.<br>1996                                          | 1 April<br>1996                                     |
| Trustees of the Fawkner<br>Crematorium and Memorial<br>Park       | 31 Dec.<br>1995                            | " "                                                         | 20 Mar.<br>1996                                          | 3 April<br>1996                                     |
| Trustees of the Geelong<br>Cemeteries Trust                       | 31 Dec.<br>1995                            | " "                                                         | 26 Mar.<br>1996                                          | 11 April<br>1996                                    |
| Trustees of the Lilydale<br>Memorial Park and<br>Cemetery         | 31 Dec.<br>1995                            | " "                                                         | 26 Mar.<br>1996                                          | 29 Mar.<br>1996                                     |
| Trustees of the Necropolis<br>Springvale                          | 31 Dec.<br>1995                            | " "                                                         | 22 Mar.<br>1996                                          | 29 Mar.<br>1996                                     |
| Trustees of the Templestowe<br>Cemetery Trust                     | 31 Dec.<br>1995                            | " "                                                         | 25 Mar.<br>1996                                          | 2 April<br>1996                                     |
| Victorian Health Promotion<br>Foundation                          | 30 June<br>1995                            | 30 Sept. <i>Financial<br/>Management Act 1994,</i><br>s.46. | 18 Sept.<br>1995                                         | 22 Sept.<br>1995                                    |
| Victorian Psychological<br>Council (c)                            | 30 Dec.<br>1995                            | 31 Mar. <i>Financial<br/>Management Act 1994,</i><br>s.46.  | 30 April<br>1996                                         | 3 May<br>1996                                       |

**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                       | <i>Financial year/period ended</i> | <i>Reporting to Parliament</i>                        | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|-----------------------------------------------------|------------------------------------|-------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS - continued</b>                 |                                    |                                                       |                                              |                                        |
| <b>VICTORIAN PUBLIC HOSPITALS AND NURSING HOMES</b> |                                    |                                                       |                                              |                                        |
| Alexandra District Hospital                         | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 18 Aug. 1995                                 | 4 Sept. 1995                           |
| The Alfred Healthcare Group (b)                     | 30 June 1995                       | " "                                                   | 25 Aug. 1995                                 | 24 Sept. 1995 (a)                      |
| Altona District Hospital (b)                        | 30 June 1995                       | " "                                                   | 20 Sept. 1995                                | 25 Sept. 1995                          |
| The Angliss Hospital (b)                            | 30 June 1995                       | " "                                                   | 18 Aug. 1995                                 | 22 Sept. 1995                          |
| Anne Caudle Centre (c)                              | 30 June 1995                       | " "                                                   | 17 Aug. 1995                                 | 22 Sept. 1995                          |
| Apollo Bay and District Memorial Hospital (c)       | 31 Dec. 1994                       | 31 Mar. <i>Financial Management Act 1994</i> , s.46.  | 19 Sept. 1995                                | 28 Sept. 1995                          |
| Ararat and District Hospital (c)                    | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 30 Aug. 1995                                 | 27 Sept. 1995                          |
| Bacchus Marsh and Melton Memorial Hospital          | 30 June 1995                       | " "                                                   | 6 Sept. 1995                                 | 12 Oct. 1995                           |
| Bairnsdale Regional Health Service                  | 30 June 1995                       | " "                                                   | 23 Aug. 1995                                 | 21 Sept. 1995                          |
| Ballarat Base Hospital                              | 30 June 1995                       | " "                                                   | 24 Aug. 1995                                 | 9 Nov. 1995 (a)                        |
| Beeac and District Hospital (c)                     | 31 Oct. 1994                       | 31 Jan. <i>Financial Management Act 1994</i> , s.46.  | 11 Oct. 1995                                 | 16 Oct. 1995                           |
| The Beechworth Hospital                             | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 15 Sept. 1995                                | 16 Oct. 1995                           |
| Benalla and District Memorial Hospital              | 30 June 1995                       | " "                                                   | 31 July 1995                                 | 21 Sept. 1995 (a)                      |
| The Bendigo Hospital (c)                            | 30 June 1995                       | " "                                                   | 12 Sept. 1995                                | 28 Sept. 1995                          |
| Bethlehem Hospital Incorporated                     | 30 June 1995                       | 31 Oct. <i>Financial Management Act 1994</i> , s.53A. | 18 Aug. 1995                                 | 22 Sept. 1995                          |
| Birregurra and District Community Hospital          | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 28 Aug. 1995                                 | 21 Sept. 1995                          |
| Boort District Hospital                             | 30 June 1995                       | " "                                                   | 18 Aug. 1995                                 | 11 Sept. 1995                          |

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**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                                   | <i>Financial<br/>year/period<br/>ended</i> | <i>Reporting to Parliament</i>                              | <i>Financial<br/>statements<br/>signed by<br/>entity</i> | <i>Auditor-<br/>General's<br/>report<br/>signed</i> |
|-----------------------------------------------------------------|--------------------------------------------|-------------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------------|
| <b>COMPLETED AUDITS - continued</b>                             |                                            |                                                             |                                                          |                                                     |
| <b>VICTORIAN PUBLIC HOSPITALS AND NURSING HOMES - continued</b> |                                            |                                                             |                                                          |                                                     |
| Box Hill Hospital (b)                                           | 30 June<br>1995                            | 31 Oct. <i>Financial<br/>Management Act 1994,</i><br>s.46.  | 18 Aug.<br>1995                                          | 21 Sept.<br>1995                                    |
| Bright District Hospital and<br>Health Services                 | 30 June<br>1995                            | " "                                                         | 17 Aug.<br>1995                                          | 13 Sept.<br>1995                                    |
| Bundoora Extended Care<br>Centre (b)                            | 30 June<br>1995                            | " "                                                         | 28 Aug.<br>1995                                          | 29 Sept.<br>1995                                    |
| Burwood and District<br>Community Hospital (b)                  | 30 June<br>1995                            | " "                                                         | 5 Sept.<br>1995                                          | 28 Sept.<br>1995                                    |
| Camperdown District<br>Hospital (c)                             | 31 Dec.<br>1994                            | 31 Mar. <i>Financial<br/>Management Act 1994,</i><br>s.46.  | 16 Oct.<br>1995                                          | 13 Nov.<br>1995                                     |
| Caritas Christi Hospice<br>Limited                              | 30 June<br>1995                            | 31 Oct. <i>Financial<br/>Management Act 1994,</i><br>s.53A. | 25 Aug.<br>1995                                          | 22 Sept.<br>1995                                    |
| Casterton Memorial Hospital                                     | 30 June<br>1995                            | 30 Sept. <i>Financial<br/>Management Act 1994,</i><br>s.46. | 3 Aug.<br>1995                                           | 12 Sept.<br>1995                                    |
| Central Wellington Health<br>Service                            | 30 June<br>1995                            | " "                                                         | 6 Sept.<br>1995                                          | 29 Sept.<br>1995                                    |
| Clunes District Hospital                                        | 30 June<br>1995                            | " "                                                         | 7 Sept.<br>1995                                          | 22 Sept.<br>1995                                    |
| Cobram District Hospital                                        | 30 June<br>1995                            | " "                                                         | 19 July<br>1995                                          | 21 Aug.<br>1995                                     |
| Cohuna District Hospital                                        | 30 June<br>1995                            | " "                                                         | 8 Sept<br>1995                                           | 21 Sept.<br>1995 (a)                                |
| Colac District Hospital (c)                                     | 30 June<br>1995                            | " "                                                         | 21 Aug.<br>1995                                          | 21 Sept.<br>1995                                    |
| Coleraine and District<br>Hospital                              | 30 June<br>1995                            | " "                                                         | 28 Aug.<br>1995                                          | 7 Sept.<br>1995                                     |
| Corangamite Regional<br>Hospital Services                       | 30 June<br>1995                            | " "                                                         | 18 March<br>1996                                         | 10 April<br>1996                                    |
| Creswick District Hospital (c)                                  | 31 Dec.<br>1994                            | 31 Mar. <i>Financial<br/>Management Act 1994,</i><br>s.46.  | 11 Sept.<br>1995                                         | 13 Oct.<br>1995                                     |
| Dandenong Hospital (b)                                          | 30 June<br>1995                            | 30 Sept. <i>Financial<br/>Management Act 1994,</i><br>s.46. | 18 Aug.<br>1995                                          | 28 Sept.<br>1995                                    |
| Daylesford District<br>Hospital (c)                             | 31 Dec.<br>1994                            | 31 Mar. <i>Financial<br/>Management Act 1994,</i><br>s.46.  | 11 Sept.<br>1995                                         | 27 Dec.<br>1995 (a)                                 |

**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                                   | <i>Financial year/period ended</i> | <i>Reporting to Parliament</i>                       | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|-----------------------------------------------------------------|------------------------------------|------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS - continued</b>                             |                                    |                                                      |                                              |                                        |
| <b>VICTORIAN PUBLIC HOSPITALS AND NURSING HOMES - continued</b> |                                    |                                                      |                                              |                                        |
| Dimboola District Hospital                                      | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994, s.46.</i> | 26 Sept. 1995                                | 13 Nov. 1995                           |
| Donald District Hospital                                        | 30 June 1995                       | " "                                                  | 25 Aug. 1995                                 | 19 Sept. 1995                          |
| Dunmunkle Health Services                                       | 30 June 1995                       | " "                                                  | 4 Sept. 1995                                 | 20 Sept. 1995                          |
| Echuca Regional Health                                          | 30 June 1995                       | " "                                                  | 30 Aug. 1995                                 | 12 Oct. 1995 (a)                       |
| Edenhope and District Memorial Hospital                         | 30 June 1995                       | " "                                                  | 28 Aug. 1995                                 | 22 Sept. 1995                          |
| Fairfield Hospital (b)                                          | 30 June 1995                       | " "                                                  | 25 Aug. 1995                                 | 21 Sept. 1995                          |
| Far East Gippsland Health and Support Service                   | 30 June 1995                       | " "                                                  | 31 Aug. 1995                                 | 30 Oct. 1995 (a)                       |
| Geelong Hospital                                                | 30 June 1995                       | " "                                                  | 22 Aug. 1995                                 | 4 Sept. 1995                           |
| Gippsland Southern Health Service                               | 30 June 1995                       | " "                                                  | 28 Sept. 1995                                | 10 Oct. 1995 (a)                       |
| Goulburn Valley Base Hospital                                   | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 19 Sept. 1995                          |
| Grace McKellar Centre                                           | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 15 Sept. 1995                          |
| Hamilton Base Hospital                                          | 30 June 1995                       | " "                                                  | 17 Aug. 1995                                 | 13 Sept. 1995                          |
| Hampton Rehabilitation Hospital (b)                             | 30 June 1995                       | " "                                                  | 31 July 1995                                 | 8 Sept. 1995                           |
| Healesville and District Hospital (b)                           | 30 June 1995                       | " "                                                  | 25 Aug. 1995                                 | 20 Sept. 1995                          |
| Hesse Rural Health Service                                      | 30 June 1995                       | " "                                                  | 24 Sept. 1995                                | 19 Oct. 1995                           |
| Heywood and District Memorial Hospital                          | 30 June 1995                       | " "                                                  | 17 Aug. 1995                                 | 29 Sept. 1995                          |
| Inglewood Hospital                                              | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 15 Sept. 1995                          |
| Kaniva District Hospital                                        | 30 June 1995                       | " "                                                  | 1 Sept. 1995                                 | 9 Nov. 1995 (a)                        |
| Kerang and District Hospital                                    | 30 June 1995                       | " "                                                  | 4 Oct. 1995                                  | 13 Oct. 1995                           |

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**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                                   | <i>Financial year/period ended</i> | <i>Reporting to Parliament</i>                        | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|-----------------------------------------------------------------|------------------------------------|-------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS - continued</b>                             |                                    |                                                       |                                              |                                        |
| <b>VICTORIAN PUBLIC HOSPITALS AND NURSING HOMES - continued</b> |                                    |                                                       |                                              |                                        |
| The Kilmore and District Hospital                               | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 31 Aug. 1995                                 | 25 Sept. 1995                          |
| Kingston Centre (b)                                             | 30 June 1995                       | " "                                                   | 30 Aug. 1995                                 | 21 Sept. 1995                          |
| Koroit and District Memorial Hospital (c)                       | 31 Mar. 1995                       | 30 June <i>Financial Management Act 1994</i> , s.46.  | 23 Aug. 1995                                 | 12 Sept. 1995                          |
| Kyabram and District Memorial Community Hospital                | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 16 Aug. 1995                                 | 20 Sept. 1995 (a)                      |
| Kyneton District Health Services                                | 30 June 1995                       | " "                                                   | 18 Aug. 1995                                 | 22 Sept. 1995                          |
| Latrobe Regional Hospital                                       | 30 June 1995                       | " "                                                   | 28 Aug. 1995                                 | 22 Sept. 1995 (a)                      |
| Lismore and District Hospital (c)                               | 31 Dec. 1994                       | 31 Mar. <i>Financial Management Act 1994</i> , s.46.  | 2 Nov. 1995                                  | 26 Feb. 1996                           |
| Lorne Community Hospital                                        | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 20 Sept. 1995                                | 29 Sept. 1995                          |
| Macarthur and District Memorial Hospital (c)                    | 30 April 1995                      | 31 July <i>Financial Management Act 1994</i> , s.46.  | 3 Nov. 1995                                  | 19 Dec. 1995                           |
| Maffra District Hospital                                        | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 29 Aug. 1995                                 | 20 Sept. 1995                          |
| Maldon Hospital                                                 | 30 June 1995                       | " "                                                   | 18 Aug. 1995                                 | 25 Sept. 1995                          |
| Manangatang and District Hospital                               | 30 June 1995                       | " "                                                   | 15 Sept. 1995                                | 29 Sept. 1995                          |
| Mansfield District Hospital                                     | 30 June 1995                       | " "                                                   | 28 Aug. 1995                                 | 19 Sept. 1995                          |
| Maroondah Hospital (b)                                          | 30 June 1995                       | " "                                                   | 29 Aug. 1995                                 | 22 Sept. 1995                          |
| Maryborough District Health Service                             | 30 June 1995                       | " "                                                   | 18 Aug. 1995                                 | 25 Sept. 1995                          |
| Mclvor Health and Community Services                            | 30 June 1995                       | " "                                                   | 18 Aug. 1995                                 | 20 Sept. 1995                          |

**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                                   | <i>Financial<br/>year/period<br/>ended</i> | <i>Reporting to Parliament</i>                               | <i>Financial<br/>statements<br/>signed by<br/>entity</i> | <i>Auditor-<br/>General's<br/>report<br/>signed</i> |
|-----------------------------------------------------------------|--------------------------------------------|--------------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------------|
| <b>COMPLETED AUDITS - continued</b>                             |                                            |                                                              |                                                          |                                                     |
| <b>VICTORIAN PUBLIC HOSPITALS AND NURSING HOMES - continued</b> |                                            |                                                              |                                                          |                                                     |
| Mercy Public Hospitals Inc.                                     | 30 June<br>1995                            | 31 Oct. <i>Financial<br/>Management Act 1994,<br/>s.53A.</i> | 30 Aug.<br>1995                                          | 29 Sept.<br>1995 (a)                                |
| Mildura Base Hospital                                           | 30 June<br>1995                            | 30 Sept. <i>Financial<br/>Management Act 1994,<br/>s.46.</i> | 5 Sept.<br>1995                                          | 6 Oct.<br>1995                                      |
| Monash Medical Centre (b)                                       | 30 June<br>1995                            | " "                                                          | 18 Aug.<br>1995                                          | 26 Sept.<br>1995                                    |
| Mordialloc-Cheltenham<br>Community Hospital (b)                 | 30 June<br>1995                            | " "                                                          | 29 Aug.<br>1995                                          | 21 Sept.<br>1995                                    |
| Mornington Peninsula<br>Hospital (b)                            | 30 June<br>1995                            | " "                                                          | 3 Nov.<br>1995                                           | 30 Nov.<br>1995                                     |
| Mortlake District Hospital (c)                                  | 31 Oct.<br>1994                            | 31 Jan. <i>Financial<br/>Management Act 1994,<br/>s.46.</i>  | 18 Aug.<br>1995                                          | 19 Sept.<br>1995 (a)                                |
| The Mount Eliza Centre (b)                                      | 30 June<br>1995                            | 30 Sept. <i>Financial<br/>Management Act 1994,<br/>s.46.</i> | 18 Aug.<br>1995                                          | 21 Sept.<br>1995                                    |
| Mt Alexander Hospital                                           | 30 June<br>1995                            | " "                                                          | 18 Aug.<br>1995                                          | 27 Sept.<br>1995                                    |
| Myrtleford District War<br>Memorial Hospital                    | 30 June<br>1995                            | " "                                                          | 18 Aug.<br>1995                                          | 14 Sept.<br>1995                                    |
| Nathalia District Hospital                                      | 30 June<br>1995                            | " "                                                          | 18 Aug.<br>1995                                          | 21 Sept.<br>1995                                    |
| Nhill Hospital                                                  | 30 June<br>1995                            | " "                                                          | 25 Aug.<br>1995                                          | 8 Sept.<br>1995                                     |
| North West Hospital (b)                                         | 30 June<br>1995                            | " "                                                          | 22 Aug.<br>1995                                          | 21 Sept.<br>1995                                    |
| Numurkah and District War<br>Memorial Hospital                  | 30 June<br>1995                            | " "                                                          | 15 Aug.<br>1995                                          | 13 Sept.<br>1995                                    |
| O'Connell Family Centre<br>(Grey Sisters) Inc.                  | 30 June<br>1995                            | 31 Oct. <i>Financial<br/>Management Act 1994,<br/>s.53A.</i> | 21 Sept.<br>1995                                         | 6 Oct.<br>1995                                      |
| Omeo District Hospital                                          | 30 June<br>1995                            | 30 Sept. <i>Financial<br/>Management Act 1994,<br/>s.46.</i> | 22 Aug.<br>1995                                          | 19 Sept.<br>1995                                    |
| Otway Health and<br>Community Services                          | 30 June<br>1995                            | " "                                                          | 19 Sept.<br>1995                                         | 29 Sept.<br>1995                                    |
| Ouyen and District Hospital                                     | 30 June<br>1995                            | " "                                                          | 14 Sept.<br>1995                                         | 28 Sept.<br>1995                                    |



SCHEDULE B  
COMPLETED/INCOMPLETE AUDITS - *continued*

| <i>Entity</i>                                                          | <i>Financial year/period ended</i> | <i>Reporting to Parliament</i>                       | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|------------------------------------------------------------------------|------------------------------------|------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS - <i>continued</i></b>                             |                                    |                                                      |                                              |                                        |
| <b>VICTORIAN PUBLIC HOSPITALS AND NURSING HOMES - <i>continued</i></b> |                                    |                                                      |                                              |                                        |
| Penshurst and District Memorial Hospital                               | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994, s.46.</i> | 18 Aug. 1995                                 | 20 Sept. 1995                          |
| Peter James Centre (b)                                                 | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 15 Sept. 1995                          |
| Peter MacCallum Cancer Institute (b)                                   | 30 June 1995                       | " "                                                  | 17 Aug. 1995                                 | 9 Nov. 1995 (a)                        |
| Port Fairy Hospital                                                    | 30 June 1995                       | " "                                                  | 12 Sept. 1995                                | 29 Sept. 1995                          |
| Portland and District Hospital                                         | 30 June 1995                       | " "                                                  | 20 Aug. 1995                                 | 7 Sept. 1995                           |
| Preston and Northcote Community Hospital (b)                           | 30 June 1995                       | " "                                                  | 29 Aug. 1995                                 | 26 Sept. 1995                          |
| Queen Elizabeth Centre                                                 | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 21 Sept. 1995                          |
| Queen Elizabeth Centre Ballarat                                        | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 12 Sept. 1995                          |
| Ripon Peace Memorial Hospital                                          | 30 June 1995                       | " "                                                  | 27 Sept. 1995                                | 19 Oct. 1995                           |
| Rochester and Elmore District Health Service                           | 30 June 1995                       | " "                                                  | 4 Sept. 1995                                 | 28 Sept. 1995 (a)                      |
| Royal Children's Hospital (b)                                          | 30 June 1995                       | " "                                                  | 17 Aug. 1995                                 | 24 Sept. 1995 (a)                      |
| Royal Dental Hospital of Melbourne                                     | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 11 Sept. 1995                          |
| Royal Melbourne Hospital (b)                                           | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 20 Sept. 1995                          |
| Royal Victorian Eye and Ear Hospital (b)                               | 30 June 1995                       | " "                                                  | 15 Sept. 1995                                | 20 Sept. 1995                          |
| Royal Women's Hospital (b)                                             | 30 June 1995                       | " "                                                  | 29 Sept. 1995                                | 4 Oct. 1995                            |
| Sandringham and District Memorial Hospital (b)                         | 30 June 1995                       | " "                                                  | 25 Sept. 1995                                | 25 Sept. 1995                          |
| Seymour District Memorial Hospital                                     | 30 June 1995                       | " "                                                  | 23 Sept. 1995                                | 10 Oct. 1995                           |
| Skipton and District Memorial Hospital                                 | 30 June 1995                       | " "                                                  | 27 Sept. 1995                                | 30 Oct. 1995                           |
| South Gippsland Hospital                                               | 30 June 1995                       | " "                                                  | 11 Sept. 1995                                | 27 Sept. 1995                          |

**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                                   | <i>Financial year/period ended</i> | <i>Reporting to Parliament</i>                       | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|-----------------------------------------------------------------|------------------------------------|------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS - continued</b>                             |                                    |                                                      |                                              |                                        |
| <b>VICTORIAN PUBLIC HOSPITALS AND NURSING HOMES - continued</b> |                                    |                                                      |                                              |                                        |
| St Arnaud District Hospital                                     | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994, s.46.</i> | 1 Sept. 1995                                 | 27 Sept. 1995                          |
| St George's Hospital and Inner Eastern Geriatric Service (b)    | 30 June 1995                       | " "                                                  | 21 Sept. 1995                                | 30 Sept. 1995                          |
| St Vincent's Hospital (Melbourne) Limited                       | 30 June 1995                       | 31 Oct. <i>Financial Management Act 1994, s.53A.</i> | 30 Aug. 1995                                 | 28 Sept. 1995                          |
| Stawell District Hospital                                       | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994, s.46.</i> | 1 Sept. 1995                                 | 29 Sept. 1995                          |
| Swan Hill District Hospital                                     | 30 June 1995                       | " "                                                  | 13 Sept. 1995                                | 27 Sept. 1995                          |
| Tallangatta Hospital                                            | 30 June 1995                       | " "                                                  | 17 Aug. 1995                                 | 31 Aug. 1995                           |
| Tawonga District General Hospital                               | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 3 Oct. 1995 (a)                        |
| Terang and District (Norah Cosgrave) Community Hospital (c)     | 31 Oct. 1994                       | 31 Jan. <i>Financial Management Act 1994, s.46.</i>  | 18 Aug. 1995                                 | 19 Sept. 1995                          |
| Terang and Mortlake Health Service                              | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994, s.46.</i> | 18 Aug. 1995                                 | 19 Sept. 1995                          |
| Timboon and District Hospital                                   | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 19 Sept. 1995                          |
| Tweddle Child and Family Health Service                         | 30 June 1995                       | " "                                                  | 4 Sept. 1995                                 | 18 Sept. 1995                          |
| Upper Murray Health and Community Services                      | 30 June 1995                       | " "                                                  | 14 Aug. 1995                                 | 14 Sept. 1995                          |
| Wangaratta District Base Hospital                               | 30 June 1995                       | " "                                                  | 1 Sept. 1995                                 | 29 Sept. 1995                          |
| Waranga Memorial Hospital                                       | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 19 Sept. 1995                          |
| Warracknabeal District Hospital                                 | 30 June 1995                       | " "                                                  | 4 Oct. 1995                                  | 10 Nov. 1995                           |
| Warrnambool and District Base Hospital                          | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 31 Aug. 1995                           |
| West Gippsland Hospital                                         | 30 June 1995                       | " "                                                  | 23 Aug. 1995                                 | 21 Sept. 1995                          |

SCHEDULE B  
COMPLETED/INCOMPLETE AUDITS - *continued*

| <i>Entity</i>                                                          | <i>Financial year/period ended</i> | <i>Reporting to Parliament</i>                       | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|------------------------------------------------------------------------|------------------------------------|------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS - <i>continued</i></b>                             |                                    |                                                      |                                              |                                        |
| <b>VICTORIAN PUBLIC HOSPITALS AND NURSING HOMES - <i>continued</i></b> |                                    |                                                      |                                              |                                        |
| Western Hospital (b)                                                   | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994, s.46.</i> | 25 Aug. 1995                                 | 28 Sept. 1995                          |
| Western Highlands Health Service                                       | 30 June 1995                       | " "                                                  | 11 Sept. 1995                                | 27 Dec. 1995 (a)                       |
| Westernport Memorial Hospital (c)                                      | 30 June 1995                       | " "                                                  | 25 Aug. 1995                                 | 25 Sept. 1995                          |
| Willaura and District Hospital (c)                                     | 30 June 1995                       | " "                                                  | 29 Aug. 1995                                 | 28 Sept. 1995                          |
| Williamstown Hospital (b)                                              | 30 June 1995                       | " "                                                  | 25 Aug. 1995                                 | 22 Sept. 1995                          |
| Wimmera Base Hospital                                                  | 30 June 1995                       | " "                                                  | 4 Sept. 1995                                 | 25 Sept. 1995                          |
| Winchelsea and District Hospital (c)                                   | 31 Oct. 1994                       | 31 Jan. <i>Financial Management Act 1994, s.46.</i>  | 11 Oct. 1995                                 | 17 Oct. 1995                           |
| Wodonga District Hospital                                              | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994, s.46.</i> | 11 Aug. 1995                                 | 18 Sept. 1995                          |
| Wonthaggi and District Hospital                                        | 30 June 1995                       | " "                                                  | 5 Sept. 1995                                 | 29 Sept. 1995                          |
| Wycheproof and District Health Service                                 | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 28 Sept. 1995                          |
| Yarram and District Health Service                                     | 30 June 1995                       | " "                                                  | 3 Sept. 1995                                 | 28 Sept. 1995                          |
| Yarrawonga District Hospital                                           | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 10 Oct. 1995                           |
| Yea and District Memorial Hospital                                     | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 15 Sept. 1995                          |

**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                       | <i>Financial year/period ended</i> | <i>Reporting to Parliament</i>                       | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|-----------------------------------------------------|------------------------------------|------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>INCOMPLETE AUDITS</b>                            |                                    |                                                      |                                              |                                        |
| <b>VICTORIAN PUBLIC HOSPITALS AND NURSING HOMES</b> |                                    |                                                      |                                              |                                        |
| Austin Hospital                                     | 31 March 1995                      | 30 June. <i>Financial Management Act 1994, s.46.</i> | Audit substantially completed.               |                                        |
| Austin Repatriation Medical Centre                  | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994, s.46.</i> | " "                                          |                                        |
| Heidelberg Hospital                                 | 31 March 1995                      | 30 June. <i>Financial Management Act 1994, s.46.</i> | " "                                          |                                        |
| Trustees of the Keilor Cemetery Trust               | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994, s.46.</i> | " "                                          |                                        |
| Trustees of the Memorial Park Altona                | 31 Dec. 1995                       | 31 Mar. <i>Financial Management Act 1994, s.46.</i>  | " "                                          |                                        |
| Trustees of the Mildura Cemetery Trust              | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994, s.46.</i> | " "                                          |                                        |
| Trustees of the Preston Cemetery Trust              | 30 June 1995                       | " "                                                  | " "                                          |                                        |
| Trustees of the Werribee Cemetery Trust             | 30 June 1995                       | " "                                                  | " "                                          |                                        |

(a) Qualified audit report issued.

(b) Abolished on 31 July 1995 and now form part of the Metropolitan Healthcare Networks.

(c) Entity abolished as at reporting date and reconstituted to form new healthcare entity.

# Part 3.3

## Infrastructure

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**KEY FINDINGS**

**Analysis of Melbourne City Link project**

- The processes adopted for the assessment and selection of the private sector consortium to deliver and operate the Melbourne City Link, which is estimated to cost \$2 billion, were fair and equitable, and resulted in the engagement of Transurban, the consortium which was best suited to deliver the project in accordance with its established scope and objectives.  
*Para 3.3.13 and Paras 3.3.67 to 3.3.117*
- Evidence was not produced to audit in the form of a detailed model, comparing project costings on the basis of private sector financing versus government borrowings.  
*Para 3.3.13 and Para 3.3.91*
- While certain project responsibilities and risks have been assumed by the State, substantial risks and exposures have been transferred to Transurban and the users of the City Link.  
*Paras 3.3.14 to 3.3.19 and Paras 3.3.118 to 3.3.210*
- Under the established arrangements, the State has been granted a right to receive ownership of the City Link in a fully maintained state at the end of the contract period. However, while the users of the City Link, via toll payments, will in substance be the financiers of the project, Transurban has ultimately accepted substantial risks in relation to the delivery and operation of the project.  
*Para 3.3.15*
- The State has undertaken to implement certain traffic management measures involving specific changes to the existing road network in the vicinity of the Link (known as *Agreed Traffic Management Measures*) to enable the most efficient use of the overall road network and provide benefits to the local communities. The toll revenue estimates to be collected by Transurban are based on traffic flows after taking account of these measures.  
*Para 3.3.16 and Paras 3.3.160 to 3.3.183*
- The obligations of the State in relation to the City Link project are not sufficient to constitute, or support the recognition of, the financing of the project as a debt of the State.  
*Paras 3.3.211 to 3.3.225*
- The Government may implement future traffic enhancement measures over the life of the project which could assist Transurban in enhancing the revenues of the project. However, any revenue generated by these additional traffic management measures will be shared between the State and Transurban.  
*Para 3.3.217*



**KEY FINDINGS - continued**

**Local government reforms**

- Recent reforms to the local government sector have been without parallel in Victoria and are designed to provide a solid foundation for the industry to service the future needs of the community.

*Paras 3.3.226 to 3.3.286*

- The Government expects that substantial savings will be generated under the Compulsory Competitive Tendering regime that could be passed on to ratepayers in the form of improved services or rate reductions.

*Paras 3.3.251 to 3.3.262*

- Based on municipal council budgets, savings of \$323 million in operating expenditure will be achieved in the 1995-96 financial year with rate reductions in the order of 18 per cent incorporated into rate notices for the 1995-96 rating period.

*Paras 3.3.263 to 3.3.266*

**Financial standing of municipal councils on creation**

- Due diligence audits of newly created municipal councils, conducted at the request of their commissioners, identified a wide range of issues impacting on the financial viability of the former councils, and outlined opportunities to enhance the future management of the restructured councils.

*Paras 3.3.287 to 3.3.296*

- The matters identified in the due diligence audit process included financial exposures inherited by the new councils and inappropriate action by former councils prior to amalgamation.

*Para 3.3.293*

**Peppercorn rentals for community assets**

- A number of municipal councils had leased certain assets to third parties for nominal rentals even though the assets were utilised by the third parties for commercial purposes, such as gambling venues.

*Paras 3.3.297 to 3.3.305*

- To ensure that the ratepayers' interests are protected, it is important that municipal councils regularly review all leasing arrangements. In addition, in order to ensure the effective management of assets, councils should be aware of the extent of implicit subsidies provided to organisations or persons in instances where commercial lease rentals are not charged.

*Para 3.3.306*

**Debt levels within municipal councils**

- Debt levels of municipal councils have decreased by \$330 million since the 1991-92 financial year, representing a 31 per cent reduction over a 3 year period.

*Paras 3.3.307 to 3.3.313*



**KEY FINDINGS - continued**

**Urban Land Authority property dealings**

- The depressed real estate market in recent years adversely impacted on the value of certain of the Authority's undeveloped land holdings, resulting in a \$10.5 million write-down in the value of these holdings during the 1994-95 financial year, particularly comprising land relating to Roxburgh Park and Goonawarra Estates.

*Paras 3.3.322 to 3.3.336*

- Joint ventures have increasingly played an important part in the Authority's development program. In particular, the Authority has sought joint ventures to acquire the necessary skills and expertise to effectively redevelop strategic sites.

*Paras 3.3.342 to 3.3.343*

- Due to the disappointing level of sales associated with the joint venture at the Lynbrook Estate the project incurred a deficit in the 1994-95 financial year of \$284 000, and is projecting to incur a further deficit of \$215 000 in the 1995-96 financial year.

*Paras 3.3.350 to 3.3.354*

- The duplication of services provided by the Authority and other government agencies suggests that scope may exist for some rationalisation, with potential for cost savings and more effective use of available expertise.

*Paras 3.3.355 to 3.3.356*

**Reform of Victorian ports**

- The sale price of \$30 million for the port-related assets of the Port of Portland Authority was near the upper end of the valuation range previously provided by the Government's advisors.

*Paras 3.3.364 to 3.3.377*



**3.3.1** The Minister for Planning and Local Government, the Minister for Roads and Ports, and the Minister for Transport have responsibility for operations within the Infrastructure sector. These Ministers have collective responsibility for the Department of Infrastructure.

**3.3.2** Details of the specific ministerial responsibilities for public bodies within the Infrastructure sector are listed in Table 3.3A. These public bodies, together with the former Department of Transport, were subject to audit by the Auditor-General during the 1994-95 financial year.

**TABLE 3.3A  
MINISTERIAL RESPONSIBILITIES FOR PUBLIC BODIES  
WITHIN THE INFRASTRUCTURE SECTOR (a)**

| <i>Ministerial portfolio</i>         | <i>Entities subject to audit</i>                                                                                                                                                                                                                                                                                                                                                                             |
|--------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Planning and Local Government</b> | Architects Registration Board of Victoria<br>Building Control Commission<br>City of Melbourne Superannuation Fund Trustees (b)<br>Docklands Authority<br>Historic Buildings Council<br>Loddon-Campaspe Regional Planning Authority<br>Melbourne City Link Authority<br>Plumbers, Gasfitters and Drainers Registration Board<br>Upper Yarra Valley and Dandenong Ranges Authority (c)<br>Urban Land Authority |
| <b>Roads and Ports</b>               | Marine Board of Victoria<br>Port of Geelong Authority<br>Port of Melbourne Authority<br>Port of Portland Authority<br>Roads Corporation                                                                                                                                                                                                                                                                      |
| <b>Transport</b>                     | Public Transport Corporation                                                                                                                                                                                                                                                                                                                                                                                 |

(a) Subsequent to 1 July 1995, the Auditor-General assumed responsibility for:

- CityWide Service Solutions Pty Ltd;
- Melbourne Port Corporation;
- Melbourne Port Services Pty Ltd;
- Melbourne Wholesale Fish Market Pty Ltd;
- Municipal councils (78);
- Queen Victoria Market Pty Ltd;
- Regional library corporations (8); and
- Victorian Channel Authority.

(b) Ceased operations on 31 October 1995.

(c) Ceased operations on 30 June 1995.

**3.3.3** Comment on matters of significance arising from the audit of entities within the Infrastructure sector is provided below.







**ANALYSIS OF MELBOURNE CITY LINK PROJECT**

**OVERVIEW OF CITY LINK PROJECT**

**3.3.4** In recognition of the long-standing strategic need to integrate and upgrade Melbourne's road transport network, and following a detailed bid assessment process, in October 1995 the Government entered into a number of complex financial arrangements with a private sector consortium, involving the financing, construction and operation of the *Melbourne City Link*.

**3.3.5** At an estimated **total cost of \$2 billion**, including \$1.8 billion financed by the consortium and \$266 million of associated works financed by the State, the Melbourne City Link project represents one of the largest infrastructure projects ever undertaken in Australia. It covers some **22 kilometres of road, tunnel and bridge works** and involves linking 3 of Melbourne's most important freeways, namely, the South Eastern Arterial, and the West Gate and Tullamarine Freeways, together with the upgrading of parts of the South Eastern Arterial and the Tullamarine Freeway.

**3.3.6** In particular, the project involves the construction, operation and maintenance of 2 sections of roadway known as the Southern Link and the Western Link. The Southern Link will comprise around 8 kilometres of freeway-standard roadway, connecting the West Gate Freeway east of Kings Way to the South Eastern Arterial. The component parts of the Southern Link are:

- a 3.4 kilometre 3 lane east-bound tunnel linking the West Gate Freeway east of Kings Way to the South Eastern Arterial at Burnley Street;
- a 1.6 kilometre 3 lane west-bound tunnel linking the South Eastern Arterial at Punt Road to the West Gate Freeway east of Kings Way; and
- an upgrade of the South Eastern Arterial between the Toorak Road and Punt Road intersections.

**3.3.7** The Western Link will comprise around 13 kilometres of new and upgraded freeway-standard roadway, connecting the Tullamarine Freeway to the West Gate Freeway. The component parts of the Western Link are:

- an upgrade to 8 lanes of the existing Tullamarine Freeway between the Bulla Road and Flemington Road intersections;
- a 6 lane elevated roadway connecting the Tullamarine Freeway at Flemington Road to Footscray Road; and
- an extension of the above elevated roadway from Footscray Road to the West Gate Freeway at Graham Street. This section will also involve the construction of a bridge over the Yarra River, adjacent to the proposed Dockland Development.

**3.3.8** The expected opening date for the Western Link is April 1999 and the Southern Link is scheduled to open by December 1999.



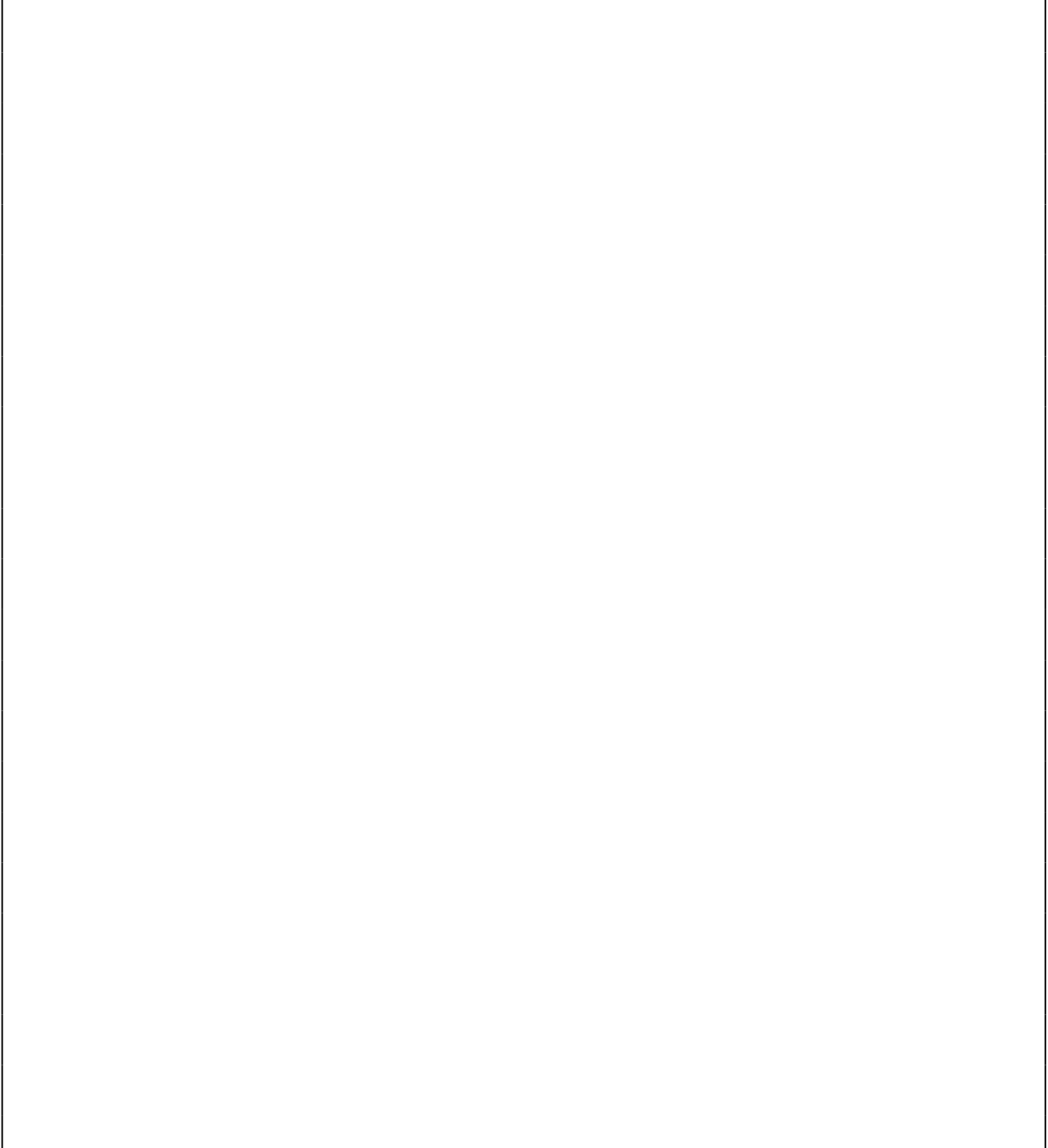
**3.3.9** The project is anticipated by the Government to generate substantial benefits to the community via reduced traffic congestion and travel times, which will result in lower pollution and fuel consumption costs. One of the key beneficiaries of the new integrated road transport network (City Link) will be the freight industry which will be able to move more freely between Melbourne's various manufacturing centres and the key export points which include the port, airport and rail freight terminals.

**3.3.10** Under the established arrangements, the private sector consortium (Transurban) will design, finance, construct, maintain and operate the City Link project. The freeway linkages and upgrade works are to be progressively completed and commissioned by the consortium, with the final completion of the project estimated to be around December 1999. The City Link is to be established by the private sector consortium on Crown land leased from the State as a public tollway for an estimated period of **34 years**, with toll revenues collected from motorists mainly applied towards its cost of construction, operation and maintenance, with a return on investment available for the investors in the project. At the end of the specified period, ownership of the City Link will revert to the State at no cost and in a fully maintained condition.

**3.3.11** The risks relating to the project are to be shared between the private sector, the State and users of the link. The general principal for risk allocation adopted by the Government is that the private sector should bear the risks for all events except for those that the State alone is able to manage. Other risks which are outside the control of both the State and the private sector are to be shared between users of the link and the private sector consortium.

**3.3.12** Audit conducted a review of the Melbourne City Link project to:

- establish whether proper evaluation and selection processes were implemented, which support the decision to engage the private sector consortium as the successful tenderer for the project;
- determine the risks and financial exposures associated with the project; and
- assess which party to the agreement substantially has responsibility for the obligations arising from the project, and determine the appropriate accounting treatment for the project by the Melbourne City Link Authority and the State.



*The City Link project.*



**OVERALL SUMMARY AND CONCLUSIONS**

**3.3.13** The audit review concluded that the processes adopted for the assessment and selection of the private sector consortium to deliver and operate the City Link were fair and equitable and resulted in the engagement of Transurban, the consortium which was best suited to deliver the project in accordance with its established scope and objectives. However, no evidence was produced to audit in the form of a detailed model, comparing project costings on the basis of private sector financing versus government borrowings.

**3.3.14** A detailed audit analysis of the complex arrangements established in relation to the project, and in particular the allocation of responsibilities and risks between the parties, revealed that **while certain project responsibilities and risks have been assumed by the State, substantial risks and exposures have been transferred to Transurban and the users of the City Link.** The risk allocation between the State, Transurban and users, relating to the various aspects of the project can be broadly summarised as follows:

- ***Operating environment*** - Given the substantial value and nature of Transurban's investment in the project, it has been imperative to establish a level of certainty for Transurban and its financiers on the general operating environment relating to the Melbourne City Link project. Consequently, certain significant events which may impact on the project have been identified in the related agreements together with a regime of available remedies to reinstate the financial position of the project if the specified events eventuate. These events can be broadly classified as:
  - actions taken by the State which hinder or prevent the delivery or operation of the project;
  - certain contamination, and Aboriginal or heritage claims relating to project land leased by the State to Transurban;
  - changes in Commonwealth law which have a specific effect on the project; and
  - certain catastrophic (force majeure) events which adversely impact on the project.

Under the available remedies established to address these events, the risks are to be mainly borne either by the users of the City Link, i.e. the motorists, or the State.

- ***Events that may cause termination of project arrangements*** - The agreements relating to the project provide for various circumstances under which the arrangements may be terminated, including abandonment of the project by Transurban, certain project defaults by Transurban which cover such circumstances as failure to complete the project by the expected completion date, and the failure to re-instate the City Link following certain uninsurable catastrophic events. In all such circumstances, Transurban has accepted the risk that the City Link (or the relevant parts thereof) will revert to the State with no compensation payable to Transurban.



**OVERALL SUMMARY AND CONCLUSIONS** - *continued*

However, the State has accepted the risk of paying compensation to Transurban in certain circumstances where either State or Commonwealth laws or requirements ultimately prevent the completion or operation of the City Link, the collection of tolls, or an Environmental Impact Statement is issued by the Commonwealth Government which materially adversely impacts on the project.

- ***Design and construction phase*** - Transurban is responsible for the cost and execution of the project design in a manner consistent with the project scope and technical requirements. In addition, Transurban must finance and implement the construction of the project in a suitable standard, in accordance with specified construction documentation. Consequently, the risks associated with the design and construction of the City Link are principally borne by Transurban.
- ***Collection of tolls*** - The key risks associated with the collection of tolls have been effectively transferred to Transurban. These risks relate to the achievement of projected traffic volumes and the development and operation of an effective and efficient electronic toll collection system. However, the State has undertaken that certain traffic management measures will be implemented and that, once the City Link is established, future transport policies will treat it as a central part of Melbourne's transport network.

To protect the taxpayers' interests, provision has been made within the arrangements for the sharing of certain toll revenues between Transurban and the State, or the early termination of the arrangements, in certain circumstances where higher than projected profits are achieved by Transurban from the operation of the City Link.

- ***Operating phase (including repairs and maintenance)*** - Transurban bears the key risks associated with the operation, maintenance and repair of the City Link. The State has a limited right to step in and remedy an *operating default* by Transurban where such an event is likely to result in a material risk to the health and safety of its users, or will result in damage to the City Link. In these circumstances, the State may operate, repair or undertake maintenance to address the risk or mitigate the consequences associated with the default, and the State must be reimbursed for any costs incurred.
- ***Financing of project*** - The key financing risks associated with the delivery and operation of City Link have been effectively transferred to Transurban. The State has not absorbed these risks, given that no indemnities have been provided to Transurban or its lenders in relation to the repayment of the project debt or the level of toll revenue. However, the State has undertaken to assume responsibility for any outstanding project debt in the event that the arrangements are terminated as a result of any changes in State or Commonwealth laws or policies which absolutely prevent Transurban from delivering or operating the City Link.



**OVERALL SUMMARY AND CONCLUSIONS** - *continued*

**3.3.15** Under the established arrangements, the State has been granted a right to receive ownership of the Melbourne City Link in a fully maintained state at the end of the contract period. However, while the users of the City Link via toll payments will, in substance, be the financiers of the project, Transurban has ultimately accepted substantial risks in relation to the delivery and operation of the project.

**3.3.16** The State has accepted certain obligations, mainly relating to the maintenance of the current overall operating environment for the project. In addition, the State has undertaken to implement certain traffic management measures involving specific changes to the existing road network in the vicinity of the Link (known as *Agreed Traffic Management Measures*) to enable the most efficient use of the overall road network and provide benefits to the local communities. The toll revenue estimates to be collected by Transurban are based on traffic flows after taking account of these measures. Furthermore, the Government may implement future traffic enhancement measures over the life of the project which could assist Transurban in enhancing the revenues of the project. However, any revenue generated by these additional traffic management measures will be shared between the State and Transurban.

**3.3.17** In audit opinion, these obligations are not sufficient to constitute, or support the recognition of, the financing of the project as a debt of the State. Significantly influencing this assessment is that, while the State may implement additional traffic enhancement measures to indirectly provide financial support to the project, it is not obligated to do so and therefore has not undertaken to 'underwrite' the revenues of the project. On the other hand, if the State was obligated to implement additional traffic management measures to assist the project under specified circumstances, such an obligation would have constituted an indemnity or guarantee which would have resulted in the assumption by the State, in substance, of the significant obligations associated with the project.

**3.3.18** Nevertheless, given the obligations and commitments of the State under the arrangements, to facilitate full accountability to the Parliament and Victorian taxpayers, it is important that the nature and extent of these obligations and commitments are disclosed in the financial statements of the Melbourne City Link Authority and the Government's Statement of Financial Operations.

**3.3.19** The State's rights to receive ongoing benefits from the project in the form of fees from Transurban which compensate the State for the consortium being able to construct and operate the tollway and for its use of associated land, should also be disclosed.



**HISTORY OF PROJECT PROPOSALS UP TO INITIAL ISSUE OF PROJECT BRIEF**

**3.3.20** Proposals for the development of links around Melbourne's Central Activities District (CAD) to alleviate congested road transport connections between the growing northern, western and south-eastern corridors, date as far back as the 1950s and 1960s. The proposals which have been considered have varied and have included the construction of a ring road around the CAD and a tunnel under the Yarra River and Kings Domain.

**3.3.21** The significantly increased road traffic activity within Melbourne, together with the unconnected freeway network which was developed during the 1970's and 1980s, comprising the West Gate and Tullamarine Freeways and the South Eastern Arterial, strengthened interest in the construction of the Links. In particular, a Western Link between the Tullamarine and West Gate Freeways, and a Southern Link between the West Gate Freeway and the South Eastern Arterial were generally proposed as the solutions to the traffic congestion problems.

**Past transport studies**

**3.3.22** Studies of inner-Melbourne's road transport needs have been undertaken by successive governments over a number of years. Comments follow on the key studies undertaken which have commented on the need to develop the proposed Western and Southern Links as an option for addressing Melbourne's traffic flow problems.

*METRAS Study - 1987*

**3.3.23** In late 1983, the Ministry of Transport commissioned the *Metropolitan Arterial Road Access Study* (METRAS), principally to assist in the preparation of a long-term arterial road development strategy for Melbourne which would support the Government's metropolitan development, economic and transport strategies and be responsive to environmental and resource constraints. The study involved assessments of the road network and consultation with other government agencies, local government and the community, and culminated in the release of a report in April 1987, setting out a proposed 10 year strategy for the development of Melbourne's arterial road system. The study identified the strategic importance of establishing the Western and Southern Links and specifically supported the commencement of construction of the Western Link during the 1990s.

*NATROV Study - 1987*

**3.3.24** The *National Roads Strategy Victoria* (NATROV) was commissioned in November 1987 by the former Road Construction Authority "... to develop a metropolitan road strategy aimed specifically at assisting State and National economic objectives". The study involved extensive consultation with industry, transport and freight distribution companies focused on the development of a strategy which serves the needs of industry and freight transport.



**3.3.25** Four broad freight movement corridors which link the existing national roads, Melbourne airport, the port at Melbourne and the new areas of manufacturing activity, were identified by the study as strategic in assisting towards the achievement of State and national economic objectives. The study concluded that 2 new road projects were essential to completing inner-Melbourne's strategic road network, namely, the Outer Ring Road from the Hume Highway to the Princes Freeway and the Western Link around the CAD. The study also commented on the Princes Highway/South-East suburbs and Docks corridor, noting that "... *the major remaining deficiency in the route will be the section between the city end of the South Eastern Freeway and the Docks area ... the main traffic route at present is via Swan Street Bridge and City Road, but these form major bottlenecks*".

**CATS Strategy - 1991**

**3.3.26** The *Central Area Transport Strategy* (CATS) was released in March 1991 by the Ministry of Transport, following a process of consultation and debate over a number of years. This strategy provided an integrated vision for central Melbourne and its associated transport network for the next 10 years and beyond and aimed to facilitate a revitalisation of the heart of Melbourne.

**3.3.27** The strategy identified that *the development and improvement of alternative routes for cross-town traffic* was a high priority and in some instances *may involve large scale works*. In particular, CATS highlighted the potential of an Western Link to divert traffic around the central activities district. As with the previous studies, CATS supported the construction of the Western Link and addressed the need to resolve the Southern Link in an environmentally sensitive manner.

**VSTS Study - 1993**

**3.3.28** The *Victorian Strategic Transport Study* (VSTS) was commissioned by the Victorian transport agencies in 1993 to identify a strategic vision, guiding principles and a series of strategic actions required for Victoria's transport system up to and beyond the year 2000.

**3.3.29** The study concluded that the strategic direction for transport system development was, inter-alia, to reinforce the role of public transport, develop a cross-town outer suburban transport corridor including a continuous high capacity road, and provide increased opportunities for private sector involvement in the development and operation of transport infrastructure. The study also concluded that the proposed inner Melbourne road links would provide the required cross-town road connections.

**Previous link proposals**

**3.3.30** Based on the results of the studies, various link proposals have been put forward for consideration.





*Western Link, Section 1 (Tullamarine Freeway to Footscray Road)*

*Early proposals*

**3.3.31** As commented earlier, the development of a Western Link between the Tullamarine Freeway to Footscray Road and ultimately the West Gate Freeway, has been under consideration for many years. A number of alternative alignments have been investigated over the years, including the construction of tunnels under Parkville and North Melbourne, surface street improvements and various link variations in close proximity to the Moonee Ponds Creek. A range of lower cost intersection improvements have also been considered to improve traffic flows. In many cases, these lower cost improvements have been implemented.

*1989 Environmental Effects Statement*

**3.3.32** In 1989, an Environmental Effects Statement on the proposed Western Link between the Tullamarine Freeway and Footscray Road was prepared, following the then Minister for Transport's announcement that the Upfield railway line would be converted to light rail, running along Royal Parade and Elizabeth Street. The favoured link alignment, which had until that time been to the east of the railway line, was moved to the railway reservation to take advantage of the land to be freed by the light rail proposal. At the same time, a clear preference within the community for a tunnel under Mt Alexander and Racecourse Roads, rather than the other options of an overpass or cutting, was included in the design of the proposed link.

**3.3.33** At the time the Environmental Effects Statement was prepared, a future extension from Footscray Road to the West Gate Freeway was not considered likely within 20 years, given that Footscray Road was at the time being upgraded to cope with long-term traffic demands. However, the proposed link made allowance for the possible future construction of a high standard connection to the West Gate Freeway. The alignment of the proposed link was kept to the east of the Moonee Ponds Creek to minimise its environmental effects.

*Recent developments*

**3.3.34** Since the 1989 Environmental Effects Statement, a number of developments have required changes to the preferred Western Link alignment, including:

- an announcement in May 1992 by the then Premier that the Upfield railway line would be retained and upgraded, which required the favoured alignment to be moved back to the east of the railway; and
- proposals for the redevelopment of the Docklands area and the port at Melbourne, which moved the favoured alignment to the west of the Moonee Ponds Creek to provide for a connection across the Yarra River to the West Gate Freeway as recommended in the *Docklands Strategy for Development*, and to maximise the land available for the Docklands development.



*Western Link, Section 2 (Footscray Road to West Gate Freeway)*

**3.3.35** Early proposals for the connection of the West Gate Freeway to Footscray Road involved the initial use of the existing Footscray Road with improvements at intersections and, ultimately, the construction of a separate road link elevated above Footscray Road.

**3.3.36** A proposal for Section 2 of the Link was not put forward in the 1989 Environmental Effects Statement due to the perceived lack of a short-term need for extra works to Footscray Road. At that time, the area now known as Docklands was also the possible site for an Olympic Village and the Southern Link was not proposed for commencement. Therefore, the expected traffic volume on Footscray Road was much less than under current proposals.

**3.3.37** In 1991, the Docklands Task Force was established to develop a strategy for rejuvenating the under-utilised Victoria Dock and Spencer Street railyard areas, with the intention of extending the commercial and residential areas at the western end of Melbourne to the Yarra River. At the same time, the Port of Melbourne Authority was developing its long-term land use plan. The plan, which was finalised by the Authority in 1993, favoured the ultimate relocation of port facilities out of Victoria Dock, combined with an extension of Appleton Dock up along the Moonee Ponds Creek. The favoured alignment for the Western Link, Section 2, proposed in the 1992 *Melbourne Docklands: Strategy for Redevelopment*, was along the Moonee Ponds Creek and across the Yarra River to join the West Gate Freeway at Graham Street, to cater for both the Docklands and Port of Melbourne proposals.

**3.3.38** While various combinations of bridges and tunnels have since been investigated for the link, the changing proposals for the Port of Melbourne and Docklands developments had caused delays in the selection of a preferred scheme.

*Southern Link*

*Previous planning studies*

**3.3.39** Proposals to develop a Southern Link of the Melbourne Central Activities District have been considered at various times. In particular, the development of an inner ring road, as a bypassing and distributor route around the Central Activities District, was included in the original *Metropolitan Planning Scheme (Interim Development Order)* of 1954.

*Pre-Metropolitan Transportation Plan*

**3.3.40** In May 1963, a report of the former Melbourne Metropolitan Board of Works (MMBW) into the then proposed Melbourne City Ring Road supported the provision of a link between St Kilda Road (near Grant Street) and Albert Street, East Melbourne. The proposed route passed through Kings Domain, crossed the Yarra River and railyards, proceeded to the Fitzroy Gardens along either Clarendon Street or Lansdowne Street and then connected to Albert Street. Connections were also proposed to be provided from the South Eastern Arterial to Wellington Street and Victoria Parade, East Melbourne. A planning scheme reservation was provided across the Domain to accommodate this proposal.



**3.3.41** The MMBW proposal was subsequently modified in 1971 to the development of a 6 lane freeway commencing at Wellington Parade, moving southwards across the Melbourne Cricket Ground parking area, Brunton Avenue, the railway yards and the Yarra River, and passing beneath the Domain and St Kilda Road and re-surfacing in Grant Street.

**3.3.42** Construction of the proposed link was scheduled to commence in the late 1970s. However, following a request from the then Minister for Local Government requesting a re-examination of the proposal, it was subsequently abandoned and the planning scheme reservation through the Domain was removed in 1975.

*Metropolitan Transportation Plan*

**3.3.43** The Metropolitan Transportation Plan was developed in 1969 by the Metropolitan Transport Committee which comprised representatives from the Government, State agencies and the Melbourne City Council. This Plan included the development for a link between the West Gate Bridge at Graham Street and the South Eastern Arterial at Burnley. The proposed link was to provide the southern leg of a City Ring Road which was considered an essential part of the proposed inner-Melbourne transport system.

**3.3.44** Prior to the abandonment of the investigation work on the Domain Tunnel proposed by the MMBW, the Board prepared a report that set out the work undertaken to date in developing the proposal. This report considered 3 options, all beginning from the West Gate Bridge at Graham Street and including a tunnel under the Domain.

**3.3.45** Although high standard road connections between the West Gate Freeway and the South Eastern Arterial were not further considered in detail until recently, several community groups including the Melbourne South Yarra Group were strong advocates of a tunnel connection.

*West Gate Freeway - South Eastern Arterial Corridor - Traffic Management Study*

**3.3.46** In 1981, a detailed traffic management study was undertaken by the former Country Roads Board to identify the most appropriate traffic management measures that should be implemented on existing roads in the West Gate Freeway to South Eastern Arterial traffic corridor. The aim of the study was to maximise the capacity of the City Road - Alexandra Avenue - Swan Street Bridge route and enable it to function as the main east-west traffic route. The study recommended a series of minor low-cost improvements, however, it also noted that ultimately there was a need for the provision of a freeway link between the West Gate Freeway and the South Eastern Arterial.

*1994 Environment Effects Statement*

**3.3.47** In August 1994, the Roads Corporation of Victoria, trading as VicRoads, released an Environmental Effects Statement on the Western Link and the Southern Link. In developing the Statement, VicRoads liaised closely with a Consultative Committee formed by the Minister for Planning, comprising representatives from Local and State Government, business and the general community.



**3.3.48** The Environmental Effects Statement considered a range of transport options for the Western and Southern Links to cater for future travel north-south and east-west, respectively, within the Melbourne metropolitan area.

**3.3.49** The development and assessment of alternatives in the Environmental Effects Statement was a 2-part process. Firstly, a broad range of transport alternatives were identified, which included a travel management alternative (based on upgrading the public transport and rail freight systems), a road improvement alternative (without the Links) and an alternative based on the Links. These alternatives were assessed against a broad range of transport, economic, social and physical environment objectives/criteria, including:

- reduction of through traffic on inner city streets;
- improvement of the environment around the river, gardens and entertainment precinct;
- optimisation of economic benefits while minimising financial costs;
- improvement of access between industry and the port, rail and airport facilities; and
- minimisation of environmental and social implications along the links and feeder roads.

**3.3.50** The second part of the Environmental Effects Statement development involved a comprehensive consultation program that aimed to give the public and interested parties the opportunity to become informed, contribute ideas and raise any issues of concern in relation to the proposed options. In doing so, VicRoads met with local councils, held community information meetings and issue-based forums, distributed bulletins and information sheets, attended meetings with individuals, groups, government departments and authorities, and provided displays of the proposed scheme.

**3.3.51** Following due consideration of all identified alternatives and the outcomes of the detailed consultative process, it was concluded that the Links provided the best solution to the traffic problems that existed to the north, west, south and south-east of Melbourne's Central Activities District.

*Public inquiry*

**3.3.52** Following public exhibition of the Environmental Effects Statement, a panel was appointed by the Minister for Planning, under the provisions of the *Environment Effects Act 1978* and the *Planning and Environment Act 1987* to inquire into and report on the Environmental Effects Statement proposals, including consideration of the associated environmental effects, and to make recommendations on such proposals.



**3.3.53** The panel's report on the public inquiry was submitted to the Minister for Planning in February 1995. In the report, the panel acknowledged that the 2 Links, and the widening of the South Eastern Arterial to Toorak Road, were the best means of achieving the project's objectives. Furthermore, the panel agreed that the process established to develop the Environmental Effects Statement was conducted satisfactorily. Other general recommendations included:

- no additional major studies be required to be carried out in connection with this project other than those mentioned in the Environmental Effects Statement, which include ongoing monitoring, consultation and studies relating to the detailed design and implementation of the project;
- the construction of the Western and Southern Links be carried out concurrently and that, due to traffic implications to the South Melbourne area, the Western Link not be opened before the Southern Link has been completed and opened to traffic;
- before any decision is made regarding the introduction of tolls on the links or any associated freeways, the wider implications be carefully assessed in consultation with the relevant parties;
- the future transport needs and appropriate transport strategies for the Melbourne metropolitan area should encourage the greater use of public transportation for passengers and freight, and that any future provision of transport infrastructure be planned having regard to the findings of the then Metropolitan Integrated Transport Strategy; and
- nothing be done as part of the Link project which might preclude or inhibit the future development and use of the non-road public transport systems, particularly heavy rail, in the Link corridor.

*Widening of Tullamarine Freeway*

**3.3.54** In the 1993-94 *Budget Papers*, the Government announced its decision to widen and upgrade the Tullamarine Freeway between Mt Alexander Road and Bell Street as part of the Better Roads Victoria Program. More recently, the Government decided that the successful bidder for the construction of the Western and Southern Links would be responsible for the widening of the Tullamarine Freeway. To allow the freeway to operate efficiently in the long-term, the project was further extended to include the widening to Bulla Road.

**3.3.55** The proposal to widen the Tullamarine Freeway was originally announced as an independent project when the development of the 1994 Environmental Effects Statement was well advanced. The Minister for Planning considered that, although the terms of reference for the associated public inquiry were deliberately broad, it was preferable that the widening of the Tullamarine Freeway be considered separately to enable more specific evaluation of the related issues and avoid matters relating to the Tullamarine Freeway being submerged by the much wider issues covering the proposal relating to the Links.



**3.3.56** The Minister further decided that an Environmental Effects Statement was not required for the Tullamarine Freeway widening, provided that VicRoads prepared a report setting out the impacts of the proposal, including a community consultation process. It was also stipulated by the Minister that the public display of the proposal be substantial and widespread to ensure that all sections of the community were informed of the project, enabling a proper evaluation of its impact.

**3.3.57** In May 1995, the Minister for Roads and Ports submitted a report to the Minister for Planning entitled *Review of Submissions and Community Comments (May 1995) Tullamarine Freeway Upgrading and Widening - Flemington Road to Bulla Road*, setting out the results of the planning process agreed by the Minister for Planning. While various submissions and comments were provided during the public consultation process, the Minister for Roads and Ports believed there were "... no new issues raised by the public that required significant modifications to the preliminary proposals prepared by VicRoads".

**3.3.58** The Minister for Planning, in his response to the report by the Minister for Roads and Ports, made reference to the 1994 Environmental Effects Statement for the Western and Southern Links which recommended that, should the widening of the Tullamarine Freeway proceed, similar design, construction and other environmental safeguards should be adopted for that project to those adopted for the Link project.

**Economic assessments of project proposals**

**3.3.59** In January 1992, the Melbourne Central Activities District Western and Southern Bypasses Inter-Departmental Committee Working Group released a *"Financial and Economic Feasibility Issues Paper"* which concluded that a freeway link of the West Gate and Tullamarine Freeways and the South-Eastern Arterial, would derive economic benefits to the community equivalent to a net present value of \$1.7 billion, and would provide significant additional environmental and social benefits.

**3.3.60** However, due to the number of alternative routes available to traffic, the Committee observed that the Link proposal did not lend itself to direct tolling. The Committee estimated that, if tolling was introduced, diversion would occur of traffic into the surrounding road network, estimated to be approximately 40 per cent of anticipated traffic volumes, and this was considered contrary to the objective of attracting through traffic onto the Links, thereby reducing the extent to which the amenity of the surrounding area could be improved. Therefore, the Committee recommended that either a shadow toll, such as a fuel levy of approximately 2 cents per litre, or a motor registration levy, would be appropriate on the basis that:

- no traffic diversion would occur, resulting in a reduction in traffic on the surrounding road networks, with subsequent environmental benefits;
- no toll plaza or collection systems would be required, resulting in reduced travel time and lower capital and operating costs; and
- cost sharing would be achieved for both users and other beneficiaries such as industry, local communities and the wider Melbourne or Victorian community, as the toll was not directed to motorists alone.



**3.3.61** In October 1992, subsequent to the above paper, a transport consultant to VicRoads also assessed the economic impacts of the Link project. The consultant concluded that the total present value of road user savings from this project would be in the vicinity of \$4.3 billion, of which 80 per cent was estimated to be savings attributed to business. After deducting the present value of project costs, the overall savings from the project, in net present value terms, was estimated to be approximately \$3.7 billion.

**3.3.62** The consultant also assessed the economic consequences of private infrastructure development, conceding that there were extra costs associated with private sector funding, such as the achievement of high investment returns for private investors, compared with funds made available by the public sector. However, the consultant identified that these additional costs would be offset by the value of economic advantages to the community, generated by the earlier completion and operation of the project.

**3.3.63** In addition, the consultant was critical of a direct manually-collected toll, due to the loss in community savings from an estimated 40 per cent traffic diversion rate. This rate was based on an analysis of the traffic flows relating to the West Gate Bridge, before and after the removal of manually-collected tolls, which identified a traffic diversion rate of 43 per cent when the tolls were in place. Therefore, the consultant proposed a shadow toll on fuel, such as an increase of 2 or 3 cents per litre, to finance the project as this would result in favourable economic consequences.

**3.3.64** In March 1993, VicRoads updated the cost-benefit ratio estimates prepared by the consultant in October 1992 for the Links, without the Burnley Tunnel. This review indicated that the previously projected travel time savings of 172 900 hours per day were excessive, mainly due to problems with the computer software used to derive the estimate, and should have been in the vicinity of 26 000 hours per day. Therefore, the net present value of the project was reduced from \$3.7 billion to \$254 million.

**3.3.65** In July 1994, VicRoads again updated its cost-benefit analysis and determined the costs and benefits of various proposals for the Links. The proposal which included the Links with the upgrading of the Tullamarine Freeway, was projected to provide a net present value of \$522 million at a discount rate of 8 per cent.

**Conclusion**

**3.3.66** While proposals for the development of the 2 Links, and the upgrading of the South Eastern Arterial and Tullamarine Freeway, have been varied and spanned many years, the conclusions drawn by transport studies (particularly focusing on the Links) and economic assessments have been consistently supportive of the development. The above proposals, now known as the City Link project, will provide a strategic road transport link and integration of Melbourne's freeway system.

**SHORT-LISTING OF  
BIDDING CONSORTIA AND CONSIDERATION OF PROJECT FINANCING**

**3.3.67** Given the consistent support of previous transport studies for the development of the Links to upgrade and integrate Melbourne's road transport network, in April 1992, the then Minister for Manufacturing and Industry Development advised VicRoads to expedite the calling for registrations of interest in the project from the private sector. Consequently, in May 1992, VicRoads issued a brief to interested parties calling for registrations of interest to build, own and operate the Links. As a result of this process, 5 proposals were received in July 1992.

**Short-listed consortia**

**3.3.68** In order to evaluate the project proposals, VicRoads established an assessment panel comprising representatives from VicRoads, the former Department of Treasury and the former Department of Manufacturing and Industry Development, together with external experts in financing and legal matters. The objective of the panel was to short-list project proposals that were sponsored by organisations or consortia which had the perceived capacity to finance and successfully complete the design and construction of the Links. The proposals were also required to present an acceptable mode of project operation which enabled the road network to be made available to the public on completion of the project and throughout the proposed franchise operation. In addition, the proposals were required to provide for the handover of the project to the State at no cost and in a fully maintained condition at the completion of the franchise period.

**3.3.69** The assessment process utilised by the panel to consider the project proposals included a detailed review of the submissions, interviews and presentations provided by each project sponsor and assessments of written responses to any issues raised by the panel. All proposals were assessed against the predetermined criteria set out in the registration of interest brief, which was provided to all potential bidders. The key criteria comprised:

- *Financial resources, funding proposal and risk allocation* - which related to the financial capacity of the consortia, the proposed business structure of the bidder, the expected provision of equity and debt funding by the consortia and the financiers, and the allocation of project risk between the State and the private sector;
- *Project management, design and construction capability* - which related to the consortia record in industrial relations management, general tunnelling experience, construction and design skills, and project management proposals in relation to costs and scheduling;
- *Development concept* - which related to conformity with government requirements, design and construction methods, and treatment of environmental, social and aesthetic issues; and
- *Operational concept* - which related to the operational capability of the bidder, how the bidder was to manage the tolls, proposed treatment of maintenance and rehabilitation, organisational structure of the bidder and the marketing proposals.





**3.3.70** Following completion of the detailed assessment process, the panel concluded that 2 separate consortia, Transurban and CHART Roads, were generally more suited to building, owning and operating the Links. The panel identified that these consortia clearly demonstrated the ability to deliver an infrastructure development of this nature, given their considerable prior experience with these types of projects.

**3.3.71** The panel conclusion was presented and accepted by VicRoads and the then Minister for Roads and Ports. Consequently, in September 1992, the then Government announced that both Transurban and CHART Roads were to be short-listed to compete for the project.

**THE SHORTLISTED CONSORTIA**

|  |                                                                                                                                                                                                                                                                                                                                                                                                                               |
|--|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|  | <p><b><i>Transurban</i></b></p> <p>Transurban is a consortium comprising Transfield Construction Pty Ltd and the Obayashi Corporation. The members of the consortium have had considerable prior road making and tunnelling experience, including the Sydney Harbour Tunnel and the M2 Motorway in Sydney.</p>                                                                                                                |
|  | <p><b><i>CHART Roads</i></b></p> <p>CHART Roads is a consortium comprising Clough Engineering Ltd, John Holland Construction and Engineering Pty Ltd, Roche Brothers Pty Ltd and Theiss Contractors Pty Ltd. The 4 members of the consortium are highly experienced civil engineering contractors, with one of the members having prior experience in the design and construction of the Melbourne Underground Rail Loop.</p> |

**Consideration of issues relating to project financing**

**3.3.72** Following the September 1992 announcement of the short-listed consortia, in October 1992, the current Government announced the establishment of the Infrastructure Project Unit within the Department of Planning and Development to review the major aspects of the proposed project, with particular emphasis on the key financial and commercial issues. The purpose of this review, instituted by the Minister for Major Projects and the Minister for Roads and Ports, was to determine as accurately as possible the financial implications of various options that the Government could pursue in progressing the project.

**3.3.73** The major findings of the review, which were reported to the City Freeway Committee of Cabinet, included:

- An adequate financial analysis had not been performed prior to the issue of the project briefs. In particular, the project had not been adequately costed to allow a meaningful financial analysis to be undertaken and basic financing options had not been canvassed;
- The introduction of a direct manually-collected toll would cause significant traffic diversion;



- It was considered unlikely that additional Commonwealth funding would be received for any part of this project; and
- The construction of a Burnley Tunnel was considered to be desirable, with substantial environmental benefits accruing to this option for relatively little additional cost. Upgrades to the Tullamarine Freeway and South Eastern Arterial should also proceed as part of this project, with the delivery of these "feeder routes" by the private sector envisaged to make the project more marketable.

**3.3.74** The funding of the project through the manual collection of tolls was not recommended to Cabinet as potential financiers indicated that they would view any toll funding option as involving higher risk which would increase the cost of the project. It was considered that manual toll collection would result in inherent delays at collection toll booths, which could result in an increase in traffic diversion rates away from the links. In particular, there were difficulties in physically locating the toll booths, especially, in relation to the Southern Link. It was also considered that electronic tolling was not sufficiently advanced to be acceptable to financiers.

**3.3.75** The Infrastructure Project Unit concluded that there was undue haste in the selection of the 2 consortia resulting from the expressions of interest process as a number of issues remained unresolved, including significant cost benefit issues. Further, the financial effects of the property acquisition and relocation program had been significantly underestimated.

**3.3.76** As a result of the project review, the Infrastructure Project Unit made recommendations which, inter alia, included:

- the bids submitted by the consortia should contain all possible direct toll options;
- the Government should recover the full cost of property acquisition from the preferred developer, by way of compensation, or by payment of an economic rental; and
- no new consortia should be introduced into the bidding process, however, the 2 shortlisted consortia should be informed that the Government is prepared to "open up" the bidding process if it considers the project costs to be unreasonable.

**3.3.77** Following consideration of the findings and recommendations of the above review, in April 1993, Cabinet deferred agreement to the construction of the Domain Tunnel and the Western bypass projects.



*Further advice to Minister on financing options*

**3.3.78** In June 1993, the Infrastructure Project Unit advised the Minister for Roads and Ports of the various financing options available to the Government for the Links, involving varying degrees of private and public sector participation. The Unit recommended that the preferred financing option should possess the following key attributes:

- maximum private sector participation in the design, construction and operation of the project;
- completion of the project as timely as possible;
- State debt not to increase;
- if possible, the project should fall outside the Loan Council arrangements; and
- the lowest overall cost should be achieved.

*Final government decision on project financing*

**3.3.79** In May 1994, the Cabinet reached an "in-principle" agreement that the Links should proceed as a private sector infrastructure project, with a scheduled completion date in the year 2000. The project was to be financed from a combination of toll collection and government support via contributions from the Better Roads Victoria Program. The key reasons for the change in the proposed financing structure were identified as follows:

- recent advances in technology made electronic tolling a feasible option, which overcame inherent delays in manual toll collection and problems in the physical location of the toll booths; and
- shadow tolls, such as fuel levies, were not considered appropriate as the financing of the project may become subject to Loan Council requirements.

**3.3.80** The net effect of these developments was to significantly reduce the attractiveness of using fuel levies and to increase the feasibility of direct electronic toll collection.

**3.3.81** The above financing option for the project was considered to be the most appropriate on the basis that the project would yield efficiencies generated by the private sector. In addition, the risk to the State was considered to be minimal as the key risks associated with the project, relating to construction, operation, financing and toll collection were expected to be transferred to the private sector.



**3.3.82** The project was to proceed as a private sector infrastructure development established on a build, own, operate and transfer (BOOT) basis in accordance with the Government's Infrastructure Investment Policy. The successful private sector consortium was to assume responsibility for the design, construction, ownership, financing and operation of the project for a specified period, with a transfer of the asset to the State at the completion of that period at nil cost. It was also envisaged at that time that:

- The Southern Link would connect the West Gate Freeway directly with the South Eastern Arterial, with tunnelling under St Kilda Road and the Kings Domain;
- Stage 1 of the Western Link would connect the Tullamarine Freeway to Footscray Road. Improvements would also be made to Footscray Road intersections which would provide an interim link to the West Gate Freeway, pending the subsequent development of the Western Link (Stage 2) which would provide the connection to the West Gate Freeway;
- The preferred financing option would be a combination of direct tolls and Government support, such as capital grants;
- The Commonwealth Government would be requested to make a contribution towards the cost of the project; and
- A project brief be prepared for release to the 2 short-listed consortia for the preparation of bids.

*Preliminary project feasibility analyses*

**3.3.83** Following the Government's "in principle" decision to proceed with the project, an interim management structure known as the *Southern and Western By-passes Co-ordination Team* was established to co-ordinate the development and implementation of the project. The team reported directly to the Minister for Roads and Ports, and comprised representatives from the Departments of Transport, Premier and Cabinet, and Treasury and Finance, and consultants specialising in financial, engineering and legal matters.

**3.3.84** In August 1994, the co-ordination team prepared a financial model to determine the financial viability of the Links and, in particular, to ascertain the likely levels of government budget support that would be required, and to examine the impact of including the Western Link, Section 2 and the Tullamarine Freeway upgrading within the project. The results of this model led to the conclusion that the best outcome from the Government's perspective was to build a continuous freeway system. In particular, traffic projections indicated that more traffic would accrue to the Links if the total Western Link system was constructed. Furthermore, if the total Link system was to be tolled, the analysis indicated that the Western Link, Section 2 could be constructed with little negative impact on the level of government support required.

**3.3.85** Consequently, Cabinet agreed to expand the scope of the project to include the Western Link, Section 2 and the upgrading and widening of the Tullamarine Freeway, and agreed that a toll on the Tullamarine Freeway would be acceptable.



**3.3.86** At the same time, a private sector accounting firm was appointed by the Department of Transport to perform the role of process auditor and, in particular, to ensure that the processes adopted for all government dealings with the 2 short-listed consortia were fair and equitable and executed in a manner which could ensure the probity of the processes.

*Establishment of the Melbourne City Link Authority*

**3.3.87** Also in August 1994, the Government decided that a public authority would be established to assume responsibility for the development and management of the project. It was agreed that the project would be known as the *Melbourne City Link* and the Authority would be called the Melbourne City Link Authority.

**3.3.88** The Authority was formed in December 1994 under the auspices of the *Melbourne City Link Authority Act 1994*, with primary responsibility for the development and delivery of the project.

**3.3.89** The Authority's initial role was to evaluate the project submissions, undertake negotiations with the short-listed consortia and recommend to the Government a preferred consortium.

**3.3.90** Following the appointment of the preferred consortium and execution of the agreements between the State and the consortium, the Authority is to be responsible for any required co-ordination or consultation with other government agencies involved in the development of the project. The Authority is also responsible for ensuring the obligations of the successful consortium under the agreements are met and that the project is completed and delivered in accordance with the project documents.

**Conclusion**

**3.3.91** Based on the audit review of the short-listing of the preferred consortia and the determination of project financing, it was concluded that the selection processes were appropriate. However, it was identified that a detailed financial model had not been developed to compare project costings on the basis of private sector financing versus government borrowings.

**ISSUE OF FINAL PROJECT BRIEF,  
AND EVALUATION AND SELECTION OF SUCCESSFUL BIDDER**

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**Issue of the final project brief**

**3.3.92** In September 1994, Cabinet approved the issue of the project brief to the 2 short-listed consortia, namely, Transurban and CHART Roads.

**3.3.93** Consistent with the Government's infrastructure investment policy, the project brief was not prescriptive in nature but rather specified the project requirements in functional and performance terms, giving the private sector maximum scope to innovation in the development of project proposals. The 2 consortia were required to submit conforming bids by 31 January 1995.



*Project specification*

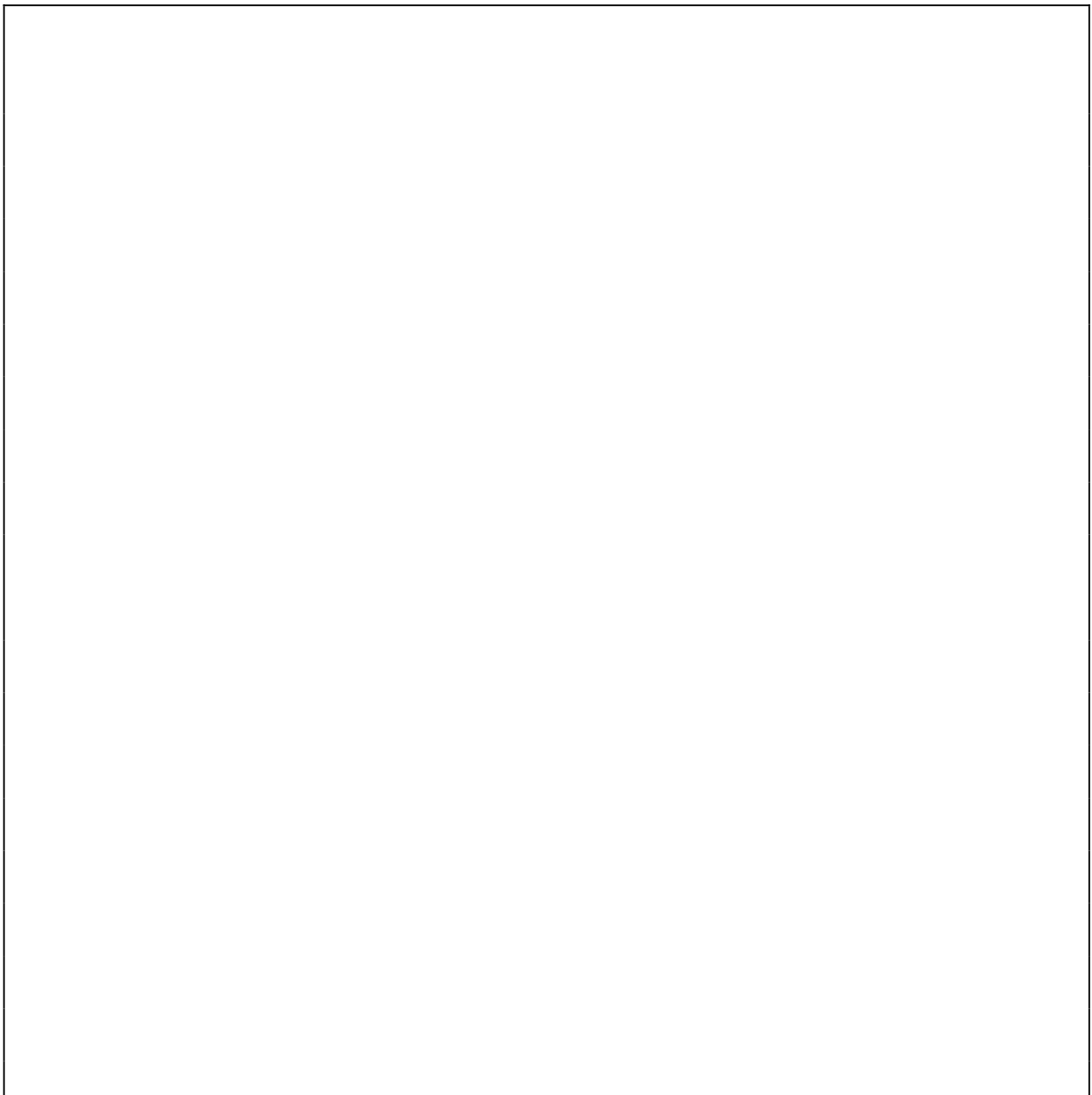
**3.3.94** The brief identified that the project was to proceed as a build, own, operate and transfer (BOOT) arrangement and that the successful consortium was required to bear substantial commercial risk and, in particular, responsibility for:

- the design and timely construction of the Links while causing as little traffic disruption as possible;
- the operation of the Links during the contract period, including the installation, operation and maintenance of the tolling system; and
- financing and economic risks in connection with the design, construction and operation of the project.

**3.3.95** The brief also set out the basis of risk allocation for the project, i.e. the risks should be allocated to the parties best able to control them, and specified that the project was to be principally funded by a revenue stream generated by a tolling system. The system of revenue generation was not to impede the flow of traffic onto the Links and was to operate so that vehicles could travel at normal speeds when entering, travelling along and leaving the Links without being required to slow down or stop. In addition, the right to use the technology adopted for revenue generation was to be available to the Government for other projects.

**3.3.96** To encourage the consortia to bid competitively, the Government nominated a maximum level of financial contribution it was willing to provide to the project. However, the specified maximum level of financial support was not revealed to the consortia.

**3.3.97** The project brief required that the development was to comprise the construction of the Links which would connect the Tullamarine and West Gate Freeways and the South Eastern Arterial, together with certain upgrade works on the Tullamarine Freeway and the South Eastern Arterial.



*Southern and Western Links location map - as per project brief.*

**3.3.98** Following receipt of the project proposals from the consortia, it was anticipated by the Government that the detailed evaluation and negotiation process would take several months to conclude. **It was the Government's intention to progress both bidders to executable documentation stage prior to announcing the successful consortia, with the losing bidder being compensated by the awarding of a monetary sum to partially cover contract preparation costs, estimated to be in excess of \$5 million.**

**Evaluation of project submissions**

**3.3.99** The bid submissions were received from the 2 consortia on 31 January 1995. The Government's criteria for the selection of the successful submission required the submission to be of an outstanding quality in all aspects and achieve excellence in the areas of planning, design, construction, operation, finance and management. The level of certainty in being able to deliver each aspect of the proposal was considered to be vital.

**3.3.100** The project brief required that each submission:

- comply with the mandatory technical requirements;
- be accompanied by the necessary taxation rulings;
- be accompanied by completed schedules detailing financial modelling criteria, traffic flows, financial structuring, commercial viability of the project, construction costs, and the tolling process;
- be accompanied by a design proposal;
- contain warranties and indemnities for the Government;
- not restrict the Government's use of the intellectual property;
- contain restrictions on the structure of the project companies;
- provide adequate insurance for all facets of construction and operation; and
- provide a business plan.

**3.3.101** It was a mandatory requirement that the level of government contribution proposed by the consortia must not exceed the amount that the Government was prepared to provide. Also, if the requested level of proposed government contribution was less than or equal to the amount that the Government was prepared to provide, the assumptions used by the consortia were required to be acceptable to the Government.

*Bid Assessment Group*

**3.3.102** In order to facilitate the evaluation of the submissions, the Melbourne City Link Authority established a Bid Assessment Group, comprising a number of Authority personnel and consultants specialising the areas of finance, law, engineering and urban design. The role of the Group was to synthesise the assessments of the Bid Assessment Teams, which were established to examine specific elements of the submissions and to provide assessments of the merits of each proposal against applicable selection criteria, for the purpose of the Group recommending a preferred proposal to the Authority's Board. The Bid Assessment Group was also responsible for establishing consistent guidelines within which the Bid Assessment Teams were to operate.

*Selection criteria*

**3.3.103** Each assessment team was involved in the development of detailed assessment criteria based on the broader criteria included in the project brief. The key considerations of the teams when assessing the proposals were:

- Evaluation of how the consortia dealt with a range of architectural and landscape design and environmental issues;





- Assessment of bid compliance with the Government's Infrastructure Investment Policy and the fundamental functional design of the bid. In addition, an assessment was undertaken against functional and performance parameters, such as the detailed checking of standards for the specific design, construction, operation and maintenance of the network;
- Evaluation of the following financial and commercial issues:
  - conformity with the overall objectives and requirements of the project brief;
  - required level of government support;
  - length of the proposed overall project period, including the possibility of extensions, and proposals for Government participation in super profits;
  - extent of the financing and economic risks borne by the consortia;
  - ability of bidders to connect new toll roads and existing roads on a competitive basis;
  - assessment of the proposed financial structure of the project vehicle;
  - level and nature of equity and debt financing;
  - ability of consortia to manage a complex project;
  - strength and certainty of the proposed financial structure;
  - assessment of the bidders ability to design and construct the project in a shorter time and at a lower cost than the Government; and
  - analysis of the financial costs and benefits to the wider community of the proposed method of delivering the project.
- Assessment of the bids' compliance with the requirements of the project brief relating to legal issues, the proposed risk profile and the divergence of each consortium's amended project documentation from that proposed by the Government.

**3.3.104** In March 1995, the Authority's Board was advised by the Bid Assessment Group that while the 2 consortia had submitted detailed and complex bids, with each incorporating at least one proposal which conformed with the mandatory requirements of the project brief, weaknesses were identified in each submission which were considered to be sufficiently serious for the Group to recommend to the Board that it was premature to recommend a preferred consortium at that stage. Neither proposal fully conformed with the requirements of the project brief.

**3.3.105** Given the shortcomings identified by the Bid Assessment Group in the project submissions, the Authority's Board determined that discussions would take place with the 2 consortia to improve the standard of their submissions. Consequently, a listing of the shortcomings was provided to the consortia together with a request for the provision of amended submissions by 26 April 1995.

**3.3.106** Subsequently, both consortia provided the amended submissions by the due date.



*Final Bid Assessment Group recommendation*

**3.3.107** In May 1995, following consideration of the detailed evaluations undertaken by the assessment teams of the final project submissions, the Bid Assessment Group provided its final report to the Board of the Authority.

**3.3.108** **The Bid Assessment Group recommended that Transurban be nominated as the preferred consortium as the objectives and criteria of the project brief were better met by the Transurban than the CHART Roads consortium.** However, the Group also considered that certain weaknesses in Transurban's submission needed to be addressed in subsequent negotiations in order to arrive at a fully acceptable position. Therefore, it was considered desirable for the CHART Roads consortium to be placed on "active reserve" status, pending resolution of the outstanding matters.

**3.3.109** At that time, the Process Auditor who was engaged by the Authority to overview the probity of the processes associated with the arrangements, also reported that the processes followed for the assessment of the bids were fair and equitable and that it was appropriate for the Authority's Board to proceed with a recommendation to the Minister on the appointment of the preferred consortium, and deal with any outstanding issues with the consortium at a later time.

**3.3.110** Given the above advice, in May 1995, the Authority recommended to the Minister for Roads and Ports that Transurban be appointed as the preferred consortium, which was subsequently endorsed by the Government.

**Economic evaluation of the project**

**3.3.111** The recommendation to the Minister on the appointment of the preferred consortium was also supported by the results of a May 1995 evaluation of the impact of the project on the economy over its construction and operational phases, which was undertaken by a consultant engaged by the Melbourne City Link Authority. The consultant identified that significant direct benefits would accrue from the City Link project, as follows:

- *Lower travel time*, resulting from a significant increase in average travel speeds in the inner city area, particularly to the south and west of the Central Business District, resulting in related annual savings of approximately \$200 million (in 1993 dollars) in 2001. By the year 2011, this would increase to over \$300 million annually;
- *Lower vehicle operating costs*, with a reduction of over \$5 million a year in 2001, due to lower fuel, tyre and vehicle maintenance costs, offset by the extra travel on the network due to the better service provided by the new road system;
- *Lower accident rates*, in that the new road system will lead to fewer accidents a unit of travel and lower costs per accident, resulting in accident cost savings of \$20 million a year in 2001;



- *More efficient fleet mix*, in that the construction of City Link should lead to proportionately more articulated trucks on the road. Because articulated trucks have a significantly lower freight carrying cost than rigid trucks, this change in the truck fleet mix should bring freight savings estimated to be almost \$75 million a year in 2001; and
- *Off-road savings* would accrue across industries and primarily result in the lowering of inventory holdings costs, expected to be worth \$60 million a year in 2001.

**3.3.112** In summary, the consultant estimated that the project would boost Victoria's economy by \$360 million (in 1993 dollars) in the year 2001. In addition, the impact on Victorian employment and productivity during the construction and operational phases of the project was expected to be substantial. While the benefits of the construction phase were substantially one-off, the benefits to be accrued during the operating phase, over and above the servicing costs of the finance of the project, were regarded as permanent.

**Announcement of the preferred consortium**

**3.3.113** Following the Government announcement on 29 May 1995 that Transurban had been selected as the preferred consortium for the development of the City Link project, a Memorandum of Understanding was entered into in July 1995 between the Melbourne City Link Authority and Transurban. This document outlined the key principles which were to form the basis of the subsequent contractual arrangements between the parties. While the document detailed the responsibilities and obligations of the State and Transurban in relation to the project, it did not constitute a legally binding agreement. In accordance with the Memorandum of Understanding, the project would proceed on the following basis:

- Transurban to have responsibility for the construction of the City Link;
- Related property acquisitions, specified roads works and landscaping to be financed by the State at an estimated cost of \$266 million;
- The land on which the project is constructed is to be leased to Transurban by the State, with the State receiving additional revenue if actual cash flows exceeded the determined projected figures; and
- Transurban to collect road tolls over a 34 year period for public usage of the 22 kilometre length of the City Link. At the end of this period, the ownership of the City Link will revert to the State at no cost.

**3.3.114** In October 1995, the Government and Transurban entered into a Concession Deed, being the primary contractual document setting out the basis on which the project is to proceed. Subsequently, in December 1995, the *Melbourne City Link Act 1995* was passed by the Parliament, which incorporated the Concession Deed, gave the Melbourne City Link Authority certain powers in relation to land and roads affected by the project, and empowered the charging and collection of tolls on the City Link.



**3.3.115** The Concession Deed contains certain conditions which must be met by the State and Transurban prior to the project proceeding. These conditions were subsequently satisfied by the respective parties in March 1996, which in turn enabled the project to commence.

**3.3.116** A payment of \$3 million was made by the Authority to CHART Roads, the unsuccessful bidder, as part compensation for costs incurred in the bidding process. This payment was consistent with the Government's earlier advised intention.

**Conclusion**

**3.3.117** Based on the audit review of the processes adopted by the Government for the assessment and selection of the preferred consortium, the selection of Transurban was fair and equitable, resulting in the engagement of the consortium best suited to deliver the project, consistent with the established project scope and objectives.

**ANALYSIS OF PROJECT RESPONSIBILITIES AND FINANCIAL RISKS**

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**3.3.118** The arrangements for the financing, delivery and operation of the project are set out in the *Melbourne City Link Act 1995* and a number of complex agreements between the State, Transurban and the project financiers. The Concession Deed is the key agreement outlining the roles and responsibilities of the respective parties in relation to the project. Further, the enabling legislation facilitates the project's construction and establishes the management framework for the project's operation.

**3.3.119** Under the arrangements, the private sector consortium known as Transurban, consisting of Transurban City Link Limited (the company) and Transurban City Link Unit Trust (the Trust), is responsible for initially financing the project. City Link is estimated to cost the consortium \$1.8 billion which is to be financed from a combination of equity raisings ultimately of \$510 million and debt financing of \$1.3 billion.

**3.3.120** An agreement has been entered into with Transurban to design, construct, maintain and operate the Link, and to levy tolls on motorists for its usage. Under the terms of the concession, the link is to be constructed on land leased from the State over a period estimated to be around 34 years (known as the concession period), which may be shortened or lengthened in certain circumstances. In particular, the circumstances for a shorter concession period relate primarily to the project producing significantly greater than projected financial returns to Transurban. On the other hand, in certain circumstances the concession period may be extended to redress for certain events that may adversely affect the project.

**3.3.121** Transurban is required to pay to the State annual fees (known as concession fees) to compensate the State for the financial assistance of around \$219 million (in June 1995 dollars) provided to the project by way of land and funding of certain works associated with the project. The State may also receive additional fees from Transurban under certain circumstances where toll revenues collected from motorists exceed initial projections.



**3.3.122** Transurban is to be responsible for the day-to-day operations and maintenance of the Link over the concession period. However, at the end of this period, the ownership of the Link is to transfer to the State at no cost.

**3.3.123** A detailed analysis of the key responsibilities, risks and financial exposures of the State and Transurban in relation to the various aspects of the project follows.

**Operating environment**

**3.3.124** Given the significant monetary investment required from the private sector to deliver and operate the Link, and the extensive period of the associated arrangements, the establishment of a level of certainty regarding the broad environment under which the project was to operate was considered fundamental by all parties to the arrangements. This was considered particularly important by Transurban and its financiers, given the power of the State and the Commonwealth Governments and their related agencies to take certain action that could have an adverse impact on the project through policy or legislative change, and the existence of certain uncontrollable risks impacting on the project, such as uninsurable catastrophic events.

**3.3.125** To establish a level of certainty regarding the broad environment under which the project is to operate, a number of events which may have a material adverse effect on the financial viability of the project have been identified and included in the Appendix to the Concession Deed, together with the methods of redress that are to be available for negotiation between the parties to address the effect of these events. The events which are set out in the Appendix can be summarised as follows:

- acts or policies by the State or its agencies which prevent or hinder the implementation of the project;
- changes in or new State laws and Victorian Government agency requirements, or changes in the application of existing State laws, which have a demonstrable effect on the project, but excluding tax changes which effect business generally;
- changes in or new Commonwealth laws and Commonwealth Government agency requirements, or changes in the application of existing Commonwealth laws, which have a specific and demonstrable effect on the project, but excluding tax changes which effect business generally;
- the removal of certain agreed traffic management measures by the State;
- failure by the State to provide support to the Link equivalent to the support afforded to other freeways, and changes to the transport network or in transport policy which could adversely impact on the Link;
- industrial action directed at the project resulting from State Government acts or policies;
- riots, blockades or other forms of civil commotion on the Link or other freeways and principal traffic routes which are undertaken to oppose the implementation of the project, or which result from an act of the State or its agencies;
- establishment of a heavy rail link between the City and the Tullamarine airport for the purpose of transporting freight;



- pollution or contamination on project land made available by the State, where the existence of such pollution or contamination was not known by Transurban or was not recorded by the Environmental Protection Authority prior to the parties entering into the arrangements;
- Aboriginal and heritage-type claims over the project land;
- significant insurable or catastrophic (force majeure) events where, under the arrangements, in certain limited circumstances lenders apply the proceeds of the insurance to reduce debt rather to reinstate the Link;
- catastrophic (force majeure) events on freeways or other principal traffic routes indirectly impacting on the Link;
- a combination of 2 or more of the above events which together have a material adverse effect; and
- removal, prior to project completion, of advertising rights granted under planning scheme amendments.

*Methods of redress available*

**3.3.126** Under the arrangements, for any of the above events to be considered for redress, it must have a demonstrable material adverse effect on the project. Once this test is satisfied, a number of methods are available to remedy the adverse effect of the event, including:

- amending the toll calculation method, i.e. increasing tolls;
- increasing the concession period;
- altering the risk allocation between the parties under the arrangements;
- rescheduling or altering concession payments due to the State;
- requesting the project lenders to restructure the financing arrangements;
- financial contribution by the State, generally only available as a measure of last resort; and
- other methods of redress as agreed between the parties.

**3.3.127** In addition, the State has an option of introducing a *Government Directed Benefit* to overcome the material adverse event, i.e. a specific change in any part of the transport network or its management to overcome the adverse effect of the event, provided that it is not a general obligation on the State and gives Transurban an advantage over and above what the State would be generally obliged to provide.

**3.3.128** Under the regime established within the arrangements for dealing with material adverse effects, the option for the State to make a financial contribution is the last method of redress to be utilised, except where the stipulated events relate to the removal of an agreed traffic management measure within 10 years of completion of the Link. In addition, State financial contributions and alterations of risk allocation are not options available for redressing the material adverse effect of changes in Commonwealth law and force majeure events.



**3.3.129** In all situations, the value of the remedy is not required to be larger than the value of the material effect. The specific outcome required to be achieved for the stipulated events specifically relating to the State is the restoration of the ability of Transurban to repay the project debt and the ability of equity investors to achieve a return commensurate with that achievable but for the occurrence of the event. The outcome required to be achieved for the stipulated events relating to Commonwealth Government action, catastrophic situations and Aboriginal and heritage claims, is the restoration of the ability of Transurban to repay the project debt and the ability of equity investors to achieve a return equal to the lower of that achievable but for the event and the projected real internal rate of return after tax of the project.

**3.3.130** In essence, the effect of the above contractual provisions is to establish certainty for Transurban and its financiers that particular significant events which may impact on the general operating environment in relation to City Link, will be redressed to reinstate the financial position of the project. Accordingly, the risks relating to the stipulated events are not to be borne by Transurban, but are to be mainly borne either by the users of the City Link, i.e. the motorists, or the State.

**Events that may cause termination of project arrangements**

**3.3.131** As previously commented, the Concession Deed is the key agreement that grants Transurban the right to construct and operate the Link. While the Deed is anticipated to operate for a defined period, there are several circumstances that could result in the concession being terminated prior to the end of the specified period. Comments follow on a number of the circumstances that could result in the concession being terminated.

*Project abandonment by Transurban*

**3.3.132** Transurban will be deemed to have abandoned the project if, following notice by the State that satisfactory efforts are not being made by Transurban to progress the Link's construction, Transurban still does not make efforts in good faith to diligently pursue its completion. **In this case, the Concession Deed may be terminated and the project will revert to the State at no cost.**

*Project and events of default*

**3.3.133** The Concession Deed may also be terminated if there is a default in relation to an element of the project (known as an *event of default*) or in relation to the entire project (known as a *project default*) and Transurban does not diligently pursue a remedy of the breach. An *event of default* is a breach of an obligation, representation or warranty by Transurban under the arrangements. Breaches and untrue representations will only constitute an event of default if the State is unable to obtain adequate redress by other means, such as damages. On the other hand, *Project defaults* are breaches of obligations or warranties, or incorrect representations by Transurban which materially and adversely effect, for a period of more than 30 days, access to, or the condition of, the Link, the level of service available to users of the Link, or the level of safety of users or those in the vicinity of the Link.

**3.3.134** Prior to the State being able to terminate the Concession Deed as a result of the above defaults, Transurban and its financiers are entitled within specified periods to



remedy the defaults. However, if the defaults are not remedied and the Concession Deed is terminated, **the project will revert to the State and Transurban will not be entitled to any compensation from the State.**

*Absolute prevention to complete and operate the Link*

**3.3.135** The project arrangements provide for the possibility of Transurban being ultimately prevented from either completing, operating or collecting tolls from the project (or parts of the project) as specified in the project documents, due to changes in either State or Commonwealth laws or requirements.

**3.3.136** The State has accepted the risk associated with these circumstances and is required to provide redress to Transurban. The methods of redress available to the State include the right to terminate part or all of the project for an early termination amount payable to Transurban. The early termination amount differs according to the circumstances, however, it is related to either the market value of the Transurban equity in the project, an amount sufficient to provide Transurban investors the returns projected on project commencement, or an amount equivalent to the expenses incurred by Transurban to the date of termination. **While the State has accepted the risk of absolute project prevention due to changes in law, Transurban investors have accepted the risk that, in certain circumstances, the compensation that will be received from the State may be less than the market value of their investment.**

*Failure to complete the project by the expected completion date*

**3.3.137** The project arrangements provide that if Transurban fails to complete the project by the expected completion date, then the State and Transurban are required to agree to a revised completion program. If completion is not subsequently achieved by the extended completion date or Transurban does not diligently pursue a solution to the problems causing the delay, then the State may terminate the Concession Deed. However, prior to termination, Transurban's financiers are to be provided with an opportunity to organise completion of the project. In these circumstances, **Transurban and its financiers have accepted the risk of project non-completion, with the project reverting to the State with no compensation payable to Transurban or its financiers.**



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*Requirement by the Commonwealth Government to undertake an Environmental Impact Statement*

**3.3.138** If prior to the completion of Link's construction the Commonwealth Government requires an Environmental Impact Statement to be undertaken and this precludes the completion of the Link, the State must acquire the project and pay an early termination amount to Transurban equivalent to the expenses incurred to date on the project, including accrued interest on debt associated with the project. Where the State decides not to terminate the project or the construction phase has been completed, Transurban is required to be ultimately compensated for any additional costs reasonably incurred as a result of the requirements of the Environmental Impact Statement. Consequently, **the State has accepted the risk associated with any adverse impacts associated with the issue of a Environmental Impact Statement by the Commonwealth Government.**

*Uninsurable catastrophic events*

**3.3.139** Transurban is responsible for the maintenance of specified insurances in relation to the project and has undertaken to repair any part of the Link that is damaged. However, this obligation to reinstate the Link (or part of the Link) does not extend to circumstances where the damage is caused by uninsurable catastrophic events and where the reinstatement is likely to result in Transurban investor returns being lower than the forecast returns prior to the damage. Uninsurable catastrophic events include natural disasters and other events such as war which are not reasonably capable of adequate insurance in the commercial insurance market.

**3.3.140** **In the above uninsurable circumstances under which Transurban may not reinstate the Link, or part of the Link, the State can terminate the concession as it relates to the damaged part of the Link and attain that part of the Link at no cost.**

**3.3.141** In addition, in circumstances where insurance is not available on commercially reasonable terms and a catastrophic event occurs, Transurban may be entitled, under the contractual provisions which stipulate material adverse events, for redress as previously described in this Report.

**3.3.142** **In summary, the agreements relating to the project provide for various circumstances under which the arrangements may be terminated, including abandonment of the project by Transurban, certain project defaults by Transurban which cover such circumstances as failure to complete the project by expected completion dates, and the failure to re-instate the City Link following certain uninsurable catastrophic events. In all such circumstances, Transurban has accepted the risk that the City Link (or the relevant parts thereof) will revert to the State with no compensation payable to Transurban.**



**3.3.143** However, the State has accepted the risk of paying compensation to Transurban in certain circumstances where either State or Commonwealth laws or requirements absolutely prevent the completion or operation of the City Link, the collection of tolls, or an Environmental Impact Statement is issued by the Commonwealth Government which materially adversely impacts on the project.

**Design and construction phase of the Link, including associated State Works**

**3.3.144** In accordance with the project agreements, the State is required to provide to Transurban, under licensing and leasing arrangements, the necessary parcels of land for the construction of the project, and to secure the necessary planning scheme amendments to enable the project to proceed. In turn, Transurban is responsible for the design and construction of the Link and certain associated works, in accordance with the project scope and technical requirements established by the State. **The costs associated with the design and construction of the Link are to be financed by Transurban, while the State will finance the estimated cost of \$159 million for the associated State Works**, which mainly include:

- widening of the Tullamarine Freeway from Moreland Road to Bulla Road, and certain associated works;
- rail infrastructure modifications for the Upfield railway line;
- modifications to structures associated with the South Eastern Arterial;
- implementation of certain traffic management measures involving specific changes to the existing road network in the vicinity of the Link (known as *Agreed Traffic Management Measures*); and
- rectification of certain specified imperfections in existing structures that are to be incorporated as part of the link.

**3.3.145** The State may require Transurban to undertake variations to the specified works, so long as it meets the additional costs required for implementation of the proposed variations.

**3.3.146** Prior to the commencement of construction, Transurban is required to make available to the State all relevant project designs and to permit an Independent Reviewer, jointly appointed between the State and Transurban, to undertake a review of the documentation to ensure compliance with the established project scope and technical requirements. Transurban is then obliged to construct the Link and the associated State Works with good workmanship and materials, and in accordance with the established design and construction documentation. The Independent Reviewer will periodically review the works to determine if they are undertaken in accordance with the documentation and the established completion timeframes.

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*General risks associated with project design and construction*

**3.3.147** Based on the terms and conditions incorporated in the project agreements, Transurban is principally responsible for the following general risks:

- completion of the design and construction of the Link;
- cost and time overruns associated with the project; and
- obtaining all necessary approvals and permits from relevant government agencies prior to commencement of construction, and meeting any additional costs associated with the related delays.

**3.3.148** In cases where the project design or the construction of works do not comply with the project scope and technical requirements, and Transurban fails to adequately rectify such non-compliance, the State may seek a Court order requiring Transurban to comply with the requirements or to provide compensation to the State equivalent to the direct costs of rectification, as certified by the Independent Reviewer.

**3.3.149** In addition, as commented earlier in this Report, if Transurban fails to complete construction of the Link by the expected completion date, the State may terminate the Concession Deed if, based on an agreed revised completion program, reasonable efforts are not taken to achieve completion of all the sections of the Link.

*State Works*

**3.3.150** The arrangements relating to the design and construction of State Works are contained in the State Works Design and Construct Contract and the Co-ordination Deed (known as the State Works Agreement). The primary requirements under these arrangements include:

- a contractor engaged by Transurban to procure, on the behalf of Transurban, the design, construction and integration of the State Works with the other works under the Concession Deed;
- the State to finance the construction of the State Works;
- the State not to regard the Link as complete unless the State Works are also completed (except for the Agreed Traffic Measurement Measures which must be implemented as soon as practicable following completion of the relevant section of the Link);
- provision of an indemnity by Transurban to the State against any claim by the contractor against the State, if Transurban terminates the State Works Agreement or the Design and Construct Contract with the contractor;
- if the design or construction of the State Works does not comply with the State's requirements, and the contractor fails to adequately rectify the non-compliance, the State may seek a Court order requiring the contractor to comply with the requirements or receive compensation equivalent to the direct cost of rectification as certified by the Independent Reviewer;



- right of the State to request the contractor to carry out variations to the specifications of the State works provided that it meets the additional costs of the variation; and
- entitlement by Transurban to claim an extension to the Link's expected completion date, if the completion of the works under the Concession Deed is delayed due to the suspension of State Works resulting from the State's failure to make progress payments on time to the contractor.

**3.3.151** In summary, Transurban and its contractor have substantially accepted the risks associated with the design and construction of the State Works.

*Specified imperfections*

**3.3.152** Under the Concession Deed, certain specified imperfections in existing structures have been identified which are to be incorporated as part of the Link. The State has accepted responsibility for these imperfections and may, at its option, engage Transurban to rectify them. Certain of these specified imperfections have been designated as *test cases*, indicating that further investigations into these imperfections are required. In these cases, the State is required to appoint an independent expert to scope the required remediation works and if the expert determines that some of these imperfections are not defects or imperfections, then Transurban is required to release the State from any responsibility.

**3.3.153** For those specified imperfections where the State has elected not to require rectification, an indemnity has been provided to Transurban against any adverse impacts resulting from the specified imperfections.

*Agreed Traffic Management Measures*

**3.3.154** As part of the State Works to be undertaken in connection with the Link, Transurban is required to implement the following *Agreed Traffic Measurement Measures* prior to the completion of the relevant section of the Link:

- downgrading of Footscray Road to 2 lanes in each direction between Flinders Street and Dudley Street, Melbourne;
- downgrading of Boundary Road, North Melbourne, to one lane in each direction;
- closure of Batman Avenue, Melbourne, west of Morell Bridge;
- closure of Morell Bridge at Anderson Street, Melbourne; and
- downgrading of Alexandra Avenue between Anderson Street and Swan Street, Melbourne, to one lane in each direction and other parking-related improvements.

**3.3.155** Under the established arrangements, Transurban is to bear the adverse revenue risk for the non-completion of the works related to the implementation of these agreed traffic measures.



*Project land*

**3.3.156** As previously mentioned, the State is responsible for the acquisition of all land required for the project and the attainment of all related planning scheme amendments. **The anticipated cost to the State for the acquisition of this land is \$107 million and the State is liable for costs incurred by Transurban associated with all delays in making available any parcel of land by the agreed dates.**

**3.3.157** The State is initially required to issue a licence to Transurban providing a non-exclusive right of possession over the project land, and to grant powers of entry and occupation of other areas, sufficient for Transurban to perform its obligations under the Concession Deed. Prior to the date of completion of each section of the Link, Transurban will have no interest, right or title in the project land or related areas, other than its ability to use the land to construct the Link sections. However, once completion of a section has occurred to the State's satisfaction, a commercial lease will be entered into by the State and Transurban at an annual rental of \$100 a year.

**3.3.158** Under the project agreements, the State has made no representation or warranty as to the condition of the project land, associated areas or any structures thereon. However, the State has indemnified Transurban for costs incurred for compliance with clean-up notices issued by the Environment Protection Agency within these areas where the State, a Victorian Government agency or occupants of the polluted land, caused or permitted the pollution to occur prior to Transurban taking possession of the land or the State granting a licence for the use of the land. This indemnity does not apply if the existence of the pollution was known or should have been reasonably known by Transurban prior to entering into the arrangements.

**3.3.159** Based on the terms and conditions incorporated in the project agreements, Transurban is responsible for the cost and execution of the project design in a manner consistent with the project scope and technical requirements. In addition, Transurban must finance and implement the construction of the project in a suitable standard, in accordance with specified construction documentation. Consequently, the risks associated with the design and construction of the City Link are principally borne by Transurban.

**Collection of tolls**

**3.3.160** The construction and operation of the Link is to be ultimately financed from tolls collected from private motorists for the usage of the Link over the concession period. Under the established arrangements, Transurban is empowered to fix, charge and collect these tolls, in accordance with the parameters established in the *Melbourne City Link Act 1995* and the Concession Deed.



**3.3.161** Tolls will be collected by means of an electronic collection system which will detect vehicles travelling through toll zones at highway speeds. Vehicles using the Link will be equipped with transponders provided by Transurban, giving them a unique electronic identification, which will enable their passage to be recorded automatically as they pass under toll detection gantries along the route. Roadside equipment will then electronically transfer the transponder identification to the Link control site and the users' accounts, which will generally be prepaid, will be debited with the appropriate toll.

**3.3.162** Tolls are to be levied on motorists for usage of the following toll zones:

- Tullamarine Freeway, between Moreland Road and Brunswick Road;
- Western Link, Section 1, between Racecourse Road and Dynon Road;
- Western Link, Section 2, between Footscray Road and the West Gate Freeway;
- South Eastern Arterial, between Punt Road and Burnley Street;
- South Eastern Arterial, between Burnley Street and Toorak Road;
- Domain Tunnel; and
- Burnley Tunnel.

**3.3.163** The Deed provides that the commencing toll levels, in March 1995 dollars, to apply for usage of each toll zone will be as follows:

**TABLE 3.3B  
TOLL LEVELS AS AT MARCH 1995**

| <i>Toll zone locations</i>                                 | <i>Toll zone</i> | <i>Motor-cycles</i> | <i>Cars</i> | <i>Light commercial vehicles</i> | <i>Heavy commercial vehicles</i> |
|------------------------------------------------------------|------------------|---------------------|-------------|----------------------------------|----------------------------------|
|                                                            |                  | (\$)                | (\$)        | (\$)                             | (\$)                             |
| Tullamarine Freeway (a)                                    | 1                | 0.40                | 0.80        | 1.30                             | 1.50                             |
| Western Link, Section 1                                    | 2                | 0.40                | 0.80        | 1.30                             | 1.50                             |
| Western Link, Section 2                                    | 3                | 0.50                | 1.00        | 1.60                             | 1.90                             |
| Domain Tunnel (west-bound)                                 | 4                | 0.50                | 1.00        | 1.60                             | 1.90                             |
| Burnley Tunnel (east-bound)                                | 4/5              | 0.90                | 1.80        | 2.90                             | 3.40                             |
| SE Arterial, Burnley Street to Punt Road (both directions) | 5                | 0.40                | 0.80        | 1.30                             | 1.50                             |
| SE Arterial, north-west of Toorak Road                     | 6                | 0.40                | 0.80        | 1.30                             | 1.50                             |
| Toll cap - day (b)                                         |                  | 1.50                | 3.00        | 4.00                             | 4.00                             |
| Toll cap - night (b)                                       |                  | 1.50                | 3.00        | 3.00                             | 3.00                             |

(a) Between Moreland Road and Brunswick Road.

(b) Toll caps refer to the maximum charge on one trip in one direction.



**3.3.164** Any increases in the actual toll levels are to be determined by Transurban, subject to the provisions of the Concession Deed which limit the rate at which actual tolls can be raised. The established escalation mechanism is based on a series of rules which apply to the tolls actually charged and the maximum tolls that can be charged. Movements in the maximum tolls that can be charged are subject, inter alia, to the following rules:

- for the period from January 1995 to 15 years following the date of Link completion, the maximum tolls that can be charged will escalate at an annual rate equivalent to the greater of 4.5 per cent and the CPI; and
- for the period from 15 years following the date of Link completion to the end of the Concession Period, the maximum tolls that can be charged will escalate quarterly at CPI.

**3.3.165** Also under the rules, the actual tolls can never exceed the maximum tolls and cannot decrease in value.

**3.3.166** The established regime provides that motorists who travel the length of the Link, avoiding the city centre, will pay a maximum of \$3.00 for each journey in one direction (in March 1995 prices) while motorcyclists will pay a maximum of \$1.50 a journey and commercial vehicles will pay a maximum of \$4.00 during the day and \$3.00 at night.

**3.3.167** The allocation of the key revenue risks relating to the Melbourne City Link are discussed below.

*Traffic risk*

**3.3.168** Traffic risk represents one of the key risks impacting on the financial viability of the project. The financial projections underlying the operation of the Link and in particular the toll revenue projections are based on traffic estimates determined by Transurban. Under the established arrangements, Transurban will bear the risk of reductions in traffic volumes and associated toll revenue, brought about by various factors including:

- incorrect traffic flow projections;
- adverse economic conditions;
- changing travel patterns and habits; and
- increases in the prices of petrol.



**3.3.169** However, this risk is partly mitigated by State undertakings which are incorporated under the arrangements that the Link is intended to be part of Melbourne's freeway network and that associated freeways and principal traffic routes will be managed in a manner that affords the Link due status as a central part of the network. The State nevertheless remains entitled to construct new toll roads and public transport routes, and implement new transport policies, so long as the Link continues to be afforded due status as a central part of Melbourne's freeway network. In addition, a number of proposed major transport network changes have been identified in the Concession Deed which the State is entitled to implement, consistent with the abovementioned intentions between the parties. In the event that the State undertaking is breached, resulting in a material adverse effect, Transurban may be entitled, under the contractual provisions which stipulate material adverse events, for redress as previously described in this part of the Report.

*Tollway operations and technology risk*

**3.3.170** As mentioned earlier, Transurban is required to develop, provide and maintain an electronic toll collection system for the Link. The Concession Deed provides that details of the system must be submitted to the State for approval prior to the completion of construction of the first section of the Link. In addition, the system cannot be changed in any material way without the State's approval.

**3.3.171** The risks associated with the operation of this system, which are to be borne by Transurban, include:

- the costs of system development, operation, maintenance and upgrading;
- technical obsolescence;
- system effectiveness and efficiency;
- inadequate vehicle recognition rates; and
- inclement weather, causing the incurring of increased costs of operation.

*Duration of concession period and level of concession fees payable to the State*

**3.3.172** The Concession Deed is premised on the expectation that Transurban will operate the Link as a tollway for a period of approximately 34 years. However, as previously mentioned, this concession period may be lengthened or shortened in certain circumstances. In particular, the State has the right to terminate the Deed at either 25 years and 6 months, 27 years, 29 years, 31 years or 33 years after the date of Link completion, if Transurban investors achieve a real internal rate of return after tax on their investment greater than 17.5 per cent, and the initially contemplated project debt facilities have been fully repaid. **This provision acts to cap the extent of returns to be received by Transurban investors from the Link.**

**3.3.173** On the other hand, as previously discussed, the concession period may be extended, under the established contractual provisions, as a means of redressing certain stipulated material adverse events previously described in this Report.





**3.3.174** In consideration for the concession granted by the State, Transurban is required to pay the following fees to the State during the concession period:

- \$95.6 million a year for the first 25 years;
- \$45.2 million a year from year 26 to year 34; and
- \$1 million a year from year 35 until the end of the Concession period.

**3.3.175** During negotiations with Transurban, and prior to the completion of the Concession Deed, the State accepted an increase in the level of the concession fees due to a decision not to receive commercial rentals on project leases and the associated stamp duty.

**3.3.176** In addition, Transurban is required to pay the State additional concession fees where actual tolling revenues exceed financial projections agreed with the State. These additional fees are payable where the actual cumulative real returns after tax to Transurban investors for a period exceed the projected cumulative real returns after tax up to the end of that period. The proportion of incremental revenue to be paid to the State increases on a sliding scale, depending on the extent that actual revenue exceeds the agreed projections and the year of operations. Generally, the proportion of surplus revenue paid to the State increases as the concession period progresses. **The effect of these provisions is to ensure that the State benefits from any "superprofits" achieved by Transurban from the operation of the Link.**

**3.3.177** However, Transurban may, at its option, issue Concession Notes to the State in satisfaction of its obligations to pay the concession fees. These Notes are due and payable at the expiry of the concession period, however, may be presented earlier by the State if investors have received a real rate of return after tax equal to or greater than 10 per cent and the payment does not exceed 30 per cent of the distributable cashflow for the previous year. Under these circumstances, **a risk exists for the State as to the timing of receipt of the actual concession fees, in the event that the project experiences financial difficulties.**

*Non-agreed traffic management measures*

**3.3.178** As previously explained, under the arrangements, the State has agreed to the implementation of certain traffic management measures involving specific changes to the existing road network in the vicinity of the Link (known as *Agreed Traffic Management Measures*). Given that Transurban have based its traffic and revenue projections on the assumption that these measures will be implemented, if the State removes any of the agreed measures, Transurban is eligible for redress either directly or under the material adverse effects regime outlined in the contract.



**3.3.179** Certain other traffic management measures which might be implemented by the State in the vicinity of the Link (known as *Non-Agreed Traffic Management Measures* and *Compensable Enhancements*) are recognised under the arrangements as measures which might enhance tolling revenue generated by the Link. These non-agreed traffic measures include certain modifications to King Street, Spencer Street and William Street, the Sporting and Entertainment Precincts, the Southbank Precinct and Flemington Road. If the State chooses to implement any of these measures, then Transurban and the State must consult in good faith to determine the net additional revenue to be paid to the State in the form of additional concession fees.

**3.3.180** Also, under the Deed, the State in future may implement *compensable enhancements*. These are defined as circumstances or events that occur after the date of the Deed relating to the road transportation network and not including events otherwise specified in the Deed, which result in additional net revenue being derived by Transurban. Under the arrangements, half of the net additional revenue derived from the compensable enhancements shall be paid to the State.

**3.3.181** Jointly, the above provisions act to ensure that any benefits generated from unanticipated enhancements to the transport network are shared between the State and Transurban.

**3.3.182** Under the arrangements, the key risks associated with the collection of tolls have been effectively transferred to Transurban. These risks relate to the achievement of projected traffic volumes and the effective and efficient operation of the electronic toll collection system. However, the State has undertaken that certain traffic management measures will be implemented and that, once the City Link is established, future transport policies will regard it as a central part of Melbourne's transport network, acting to partially mitigate this risk.

**3.3.183** To protect the taxpayers' interests, provision has been made within the arrangements for the sharing of certain toll revenues between Transurban and the State, or the early termination of the arrangements, in certain circumstances where higher than projected profits are achieved by Transurban from the operation of the City Link. However, the State has agreed to allow Transurban to retain 50 per cent of the additional revenues derived from certain enhancements to the road transport network.

**Link operating phase (including repairs and maintenance)**

**3.3.184** The Concession Deed assigns the principal responsibility for the operation, maintenance and repair of the Link to Transurban and allows the company to sub-contract the performance of some or all of its obligations to an *operator*. However, this arrangement does not limit or affect Transurban's operational obligations or liability under the Deed. In particular, the major responsibilities of Transurban once the Link becomes operational include:

- ensuring a smooth and uninterrupted flow of traffic during normal operating conditions;
- undertaking routine maintenance including the repairs of potholes, cracks, concrete joints, drains, line marking, lighting and signage;



- carrying out periodic preventative maintenance to the plant and equipment;
- identifying and undertaking major repairs and replacements;
- minimising disruption to traffic in the event of incidents affecting the Link's safety by providing a rapid and effective response, and maintaining liaison procedures with emergency services;
- liaising with VicRoads in relation to VicRoads' maintenance of entrances to and exits from the Link; and
- implementing an effective marketing program for the Link.

*Commencement of Link operations*

**3.3.185** Following the completion of the construction of each section of the Link, Transurban is required to open and operate each section as soon as practicable. While public use of a section is permitted prior to its completion, no tolls may be charged until formal completion occurs.

**3.3.186** Once a section has been opened for public use, Transurban is required to keep that section open for continuous use during the concession period. However, closure of a section is permitted under certain circumstances, with minimal public interruption, including Link maintenance or if there is a material risk to the health or safety of members of the public.

**3.3.187** Insofar as the operation or maintenance of the Link is likely to interfere with the flow of traffic in the vicinity of the Link, Transurban is obligated to provide reasonable notice requesting the State to deal with the interference or specify the likely level, location and duration of such interference to the State.

**3.3.188** For the purposes of the *Transport Act* 1983 and the *Road Safety Act* 1986, the Link will be classified as a *highway* and, therefore, will be subject to all the relevant provisions relating to traffic and motor vehicles on highways.

*Maintenance and repair responsibilities*

**3.3.189** Transurban is required to maintain, repair and make good any damage to or defect in, the Link to maintain the standards of finish, quality and conditions set out or referred to in the project scope and technical requirements, the design documentation and the Link operation and maintenance manuals. These obligations do not apply if there is any damage to or defect in the Link as a consequence of any neglect, wilful or reckless act of the State, any of its nominees or contractors, or any Victorian government agency. The State has indemnified Transurban with respect to any loss, cost, expense or damage suffered as a result of such acts.



*Link inspection requirements*

**3.3.190** Transurban is required to inspect each section of the Link at least once a month to determine its condition. The State must then be provided with a detailed report setting out:

- any identified material damage to, or defect or disrepair in, a section;
- action proposed to remedy that material, damage, defect or disrepair and the estimated time the proposed remediation will require; and
- any serious accidents involving injury or damage of which it is aware which occur on a section.

**3.3.191** Transurban is also required to provide the State and VicRoads with a written 6 monthly report of all maintenance and repairs carried out on the Link during the previous 6 month period, together with details of the procedures and materials used.

*State's rights in risk situations*

**3.3.192** In the event that an *operating default* occurs, such as a default in the obligation of Transurban to operate the Link in accordance with the project scope, and the State considers in good faith that this default will result in or is likely to result in a material risk to the health and safety of Link users or other members of the public, or of material damage to the Link, then the State may operate, repair or maintain the relevant part of the Link in an endeavour to address the risk or mitigate its consequences. The State has no right to tolls levied during any period during which it exercises this right.

**3.3.193** The State must return responsibility to Transurban for the operation, repair and maintenance of the relevant part of the Link as soon as reasonably practicable and the State is required to be reimbursed for any costs incurred.

*Liability for rates*

**3.3.194** Under current conditions, there is no requirement for Transurban to pay local government, and water and sewerage rates and charges in relation to land associated with the project, excluding usage. Under the Deed, the State has indemnified Transurban in respect of any future liability for these rates and charges.

**3.3.195** **The key risks associated with the operation, maintenance and repair of the Link rest with Transurban. However, the State has a limited right to step in and remedy an *operating default* by Transurban where such an event is likely to result in a material risk to the health and safety of its users, or will result in damage to the City Link. In these circumstances, the State may operate, repair or undertake maintenance to address the risk or mitigate the consequences associated with the default, and the State must be reimbursed for any costs incurred.**



**Handover of the Link to the State on expiry of the concession**

**3.3.196** The Melbourne City Link project has a defined life that will end at the expiration of the concession period, estimated to be 34 years. At the end of this period, the rights of Transurban in respect of the Link will be surrendered to the State of Victoria for no consideration.

**3.3.197** Regardless of when the concession period expires, the Concession Deed requires Transurban to surrender all rights, title and interest in the Link and deliver to the State all plant and equipment required and used for the tolling, operation, maintenance and repair of the Link, in a state and condition which complies with the project scope and technical requirements. Transurban is also required to deliver to the State all associated manuals, maintenance records and engineering specifications. Furthermore, all plant and equipment delivered to the State must be free of any encumbrances.

**3.3.198** The project scope and technical requirements detail the conditions of handover of the Link to the State at the expiry of the concession period. In essence, the major components of the Link must be in a condition which reflect a remaining operational life equal to the following:

- *bridges and tunnels* - 80 years;
- *road pavement* - average of 20 years;
- *road surfacing* - average of 5 years;
- *major electrical and mechanical equipment* - a minimum of 20 years;
- *communications and control systems and equipment* - 10 years; and
- *renewable items* - not less than 50 per cent of their operational life.

**3.3.199** Under the Deed, Transurban and the State are required to carry out a joint inspection of new work undertaken for the Link one year prior to the completion of the concession period. Any structural faults identified during this process will be documented, ultimately resulting in a program of remedial works to be undertaken by Transurban for rectification within the remainder of the concession period. At the time of handover, a final inspection will be carried out by both parties and any remaining remedial works will be undertaken at the expense of Transurban.

**3.3.200** At the time of handover, Transurban is also required to secure the novation of necessary operating contracts and the licensing of integral intellectual property rights to the State, to enable the State or its nominee to operate the Link and the tolling system. If the concession period is terminated prior to completion of construction, the State may require novation of construction contracts and take possession of any plant and equipment used in construction.

**Financing of the project**

**3.3.201** As previously mentioned, the total financing requirement for the construction and operation of the Link by Transurban will be approximately \$1.8 billion, excluding the specified works which are to be financed directly by the State. Transurban's funding requirement for the construction and operation of the Link will be met from a combination of debt and equity financing. Specifically, during the construction phase, \$1.3 billion of debt financing will be required, with supplementation from equity injections totalling \$455 million. However, once completion of the construction of the Link has occurred, the level of equity will be increased to \$510 million.

**3.3.202** The project lenders consist of 4 Australian banks and other international banking institutions which, jointly, have committed financing for the Link at mostly fixed rates of interest. The lenders have, in turn, secured the debt facilities through *Deeds of Charge* provided by Transurban over its assets and obligations, and mortgages over project leases. The overall requirements in relation to these securities are mainly set out in the *Master Security Deed*.

*Key financing risks*

**3.3.203** Under the Concession Deed, **Transurban bears the financing risks flowing from any increases in construction costs and interest rates. The State has not provided indemnities to Transurban or its lenders against any additional costs incurred as a result of these circumstances.** In addition, the State does not have any obligations in relation to the repayment of the project debt, unless there is a fundamental change in State or Commonwealth laws or policies, which absolutely prevents the construction or operation of the project by Transurban. In these circumstances, the State is required to assume responsibility of the Link and the repayment of the outstanding project debt.

**3.3.204** The *Master Security Deed* between the State, Transurban and the lenders regulates the priority of securities held by the lenders and those of the State, and specifies each party's obligations in the event of default under the Concession Deed. Securities obtained by the State in relation to the project are contained in the *Original Deed of Charge*, under which Transurban has granted a charge over all its assets, other than certain deposits securing infrastructure borrowings, in favour of the State. This charge secures the performance of Transurban's obligations under the project documents and the payment to the State of any money owing under the documents.

**3.3.205** Also under the *Master Security Deed*, the parties have agreed that the order of priority between the State's security under the *Original Deed of Charge* and the securities provided to the lenders will be as follows:

- firstly, *priority amounts*, representing amounts owing to the State where an operating default has compelled the State to incur costs for the operation, maintenance and repair of the Link, or the management of traffic and interferences in the vicinity of the Link;
- secondly, secured project debt, representing amounts due to lenders resulting from a Transurban breach of financial documents;



- thirdly, amounts owing to the State other than *priority amounts*; and
- fourthly, the remaining secured debt relating to the project.

**3.3.206** The Deed restrains the State's ability to immediately terminate the Concession Deed under circumstances constituting *default events*, where project debt is outstanding. Under these circumstances, lenders are provided the opportunity to demonstrate that they are diligently pursuing the sale of Transurban and do so within 2 years, or are taking remedial action necessary to complete the construction of the Link or rectify the relevant default within a reasonable period of time. Where the lenders choose to sell the project and fail to do so, then the State may step in, gain ownership free of debt and operate the Link.

**3.3.207** Also under the Deed, lenders generally cannot apply any funds that have been set aside by Transurban for Link maintenance and repairs, or any insurance proceeds, toward debt repayment. However, the lenders may apply the insurance proceeds to repay project debt if the insurance proceeds from a catastrophic event exceed \$100 million and either the proceeds are not sufficient to fund the necessary repair and reinstatement works, or if the necessary works were to be implemented, then Transurban's debt servicing capacity would be substantially diminished. Under these circumstances, the lenders may progressively apply the insurance proceeds towards debt repayment in accordance with the repayment schedules and the State is in turn entitled to terminate the Concession Deed in relation to the relevant section of the Link and gain ownership of that section. **While the State, under the arrangements, is not obligated to finance any required re-instatement of the Link, due to its critical importance to the Melbourne road transport network the State will be compelled to finance the remaining works.**

*Taxation risk*

**3.3.208** As a condition to the project proceeding, Transurban was responsible for receiving satisfactory final and binding income taxation rulings in respect of the project. In March 1996, Transurban received positive rulings on all its submissions to the Australian Taxation Office (ATO), in particular, allowing the deductibility of interest on the borrowings and other property expenses such as depreciation and repairs. In accordance with the project documents, Transurban is responsible for the taxation risks relating to the Link.

**3.3.209** Under the established arrangements, the key financing risks associated with the delivery and operation of City Link have been effectively transferred to Transurban. The State has not absorbed these risks, given that no indemnities have been provided to Transurban or its lenders in relation to the repayment of the project debt or the level of toll revenue. However, the State has undertaken to assume responsibility for any outstanding project debt in the event that the Concession Deed is terminated as a result of any changes in State or Commonwealth laws or policies which absolutely prevent Transurban from delivering or operating the City Link.

**3.3.210** In a worst case scenario for the lenders, the possibility exists that the lenders may be confronted with a termination of the Concession Deed by the State and, if they



fail to diligently pursue the sale of Transurban or rectify the default, the State will be entitled to obtain ownership of the relevant part of the Link free of any debt.

## ACCOUNTING FOR THE MELBOURNE CITY LINK

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**3.3.211** Having considered the detailed arrangements established between the State, Transurban and its financiers in relation to the financing, delivery and operation of the Melbourne City Link, it is important to consider the appropriate accounting treatment of the project by the Melbourne City Link Authority and the State.

**3.3.212** Integral to any consideration of the accounting treatment of the project is the question of whether the associated arrangements, in substance, result in liabilities or an asset which should be recognised within the Balance Sheet of the Melbourne City Link Authority, and ultimately the whole-of-government. To answer this question, one must examine the definition of liabilities and assets and the extent to which these definitions, and the related recognition criteria, have been met in relation to the State's obligations and rights under the project arrangements.

**3.3.213** While authoritative guidance is not available within Australia in the form of professional Accounting Standards on the definition and criteria to be applied for the recognition of assets and liabilities within financial statements, Statement of Accounting Standards *SAC4 - Definition and recognition of the Elements of Financial Statements*, issued in March 1995 by the Australian Accounting Research Foundation, provides some persuasive guidance. If an Accounting Standard is subsequently issued by the Australian accounting bodies, the method of disclosure of this significant arrangement within the financial statements will need to be revisited.

### *Accounting for State obligations*

**3.3.214** SAC4 defines liabilities as "*... future sacrifices of economic benefits that the entity is presently obligated to make to other entities as a result of past transactions or other past events*". For liabilities to be recognised within financial statements, it must be probable that the future sacrifice of economic benefits will be required and the amount of the liabilities can be measured reliably.

**3.3.215** To determine whether the State's obligations under the Melbourne City Link arrangements constitute liabilities that should be recognised in the financial statements, it is important to consider the extent to which the key risks relating to the project have been shared between the parties and, therefore, the probability that future sacrifices of economic benefits will be required by the State.





**3.3.216** Under the established arrangements, the State has been granted a right to receive ownership of the Melbourne City Link in a fully maintained state at the end of the contract period. However, while the users of the City Link via toll payments will in substance be the financiers of the project, Transurban has ultimately accepted substantial obligations in relation to the delivery and operation of the project.

**3.3.217** The State has accepted certain obligations, mainly relating to the maintenance of the current overall operating environment for the project. In addition, the State has undertaken to implement certain traffic management measures involving specific changes to the existing road network in the vicinity of the Link (known as *Agreed Traffic Management Measures*) to enable the most efficient use of the overall road network and provide benefits to the local communities. The toll revenue estimates expected to be collected by Transurban are based on traffic flows after taking account of these measures. Furthermore, the Government **may** implement future traffic enhancement measures over the life of the project which could assist Transurban in enhancing the revenues of the project. However, any revenue generated by these additional traffic management measures will be shared between the State and Transurban.

**3.3.218** In audit opinion, these obligations are not sufficient to constitute, or support the recognition of, the financing of the project as a debt of the State. Significantly influencing this assessment is that, while the State may implement additional traffic enhancement measures to indirectly provide financial support to the project, it is not obligated to do so and therefore has not undertaken to "underwrite" the revenues of the project. On the other hand, if the State was obligated to implement additional traffic management measures to assist the project under specified circumstances, such an obligation would have constituted an indemnity or guarantee which would have resulted in the assumption by the State, in substance, of the significant obligations associated with the project.

**3.3.219** Nevertheless, given the obligations and commitments of the State under the arrangements, to facilitate full accountability to the Parliament and Victorian taxpayers, it is important that the nature and extent of these obligations and commitments are disclosed in the financial statements of the Melbourne City Link Authority and the Government's Statement of Financial Operations.

- 3.3.220** The key obligations of the State under the project arrangements include:
- provision to Transurban of the required parcels of land and the associated planning scheme amendments, by the agreed dates, to enable the project to be completed;
  - meeting any costs associated with the clean-up of certain land contamination;
  - funding of certain works associated with the project, at an estimated cost of \$159 million;
  - implementation of certain agreed traffic management measures;
  - future transport policies to ensure that the City Link continues to be a central part of Melbourne's transport network;
  - indemnification of Transurban against costs incurred from any damage to the City Link caused by the State, its agencies or contractors;



- exemption granted to Transurban for the payment of local government, and water and sewerage rates and charges relating to project land, excluding usage; and
- assumption of Transurban debt obligations if it is fundamentally prevented from completing or operating the project as envisaged, due to a change in State or Commonwealth laws or policies.

**3.3.221** In addition, the key risks assumed by the State include:

- provision of financial contributions to Transurban, under certain circumstances which fundamentally alter the operating environment for the project;
- assumption of project responsibility and a requirement to make early termination payments to Transurban, under certain circumstances substantially within the control of the State that cause the project arrangements to be terminated, including new laws which prevent the project from completion or operation as envisaged, and the issue of an Environmental Impact Statement by the Commonwealth Government in relation to the project;
- assumption of the City Link or part thereof in a damaged condition, under certain catastrophic and uninsurable events; and
- delays in the collection of concession fees from Transurban in the event that the project experiences financial difficulties.

*Accounting for the State's rights*

**3.3.222** The State has been granted certain rights under the arrangements, including the receipt of certain fees over the concession period and, at the end of that period, ownership of the Link in a fully maintained condition.

**3.3.223** In determining whether these rights should be recognised in the financial statements of the Melbourne City Link Authority and the State, again it is important to consider the extent to which the definition and recognition criteria provided in SAC4 have been met. SAC4 defines assets as "... *future economic benefits controlled by the entity as a result of past transactions or other past events*". For assets to be recognised within financial statements, it must be probable that the future economic benefits embodied in the assets will eventuate, and their value must be able to be measured reliably.

**3.3.224** While, under the established arrangements for the Link, the State has a right to gain ownership of the Link as some point in the future, and it is probable that it will receive ownership of that asset, the Link is not controlled by the State until the expiry of the Concession Deed, which is estimated to be 34 years following the completion of the Link. Therefore, the Link should not be recognised in the body of the financial statements of the State until such time as the State gains ownership of the project.



**3.3.225** Accordingly, similarly with the suggested disclosure of the State's liabilities and commitments under these arrangements, the rights of the State to receive certain fees over the concession period should be disclosed by the Melbourne City Link Authority and in the Government's Statement of Financial Operations. Nevertheless, the Crown land upon which the City Link is situated would continue to be disclosed as an asset of the State.

**□ RESPONSE** provided by Chief Executive, Melbourne City Link Authority

*I have noted your conclusions that address key issues concerning the handling of the tender process, risk allocation and the need for the project as follows:*

- *the processes adopted for the assessment and selection of the private sector consortium were fair and equitable, resulting in the engagement of the consortium best suited to deliver the project;*
- *substantial risks and exposures have been transferred to Transurban;*
- *obligations and risks borne by the State are not sufficient to constitute or support the recognition of, the financing of the project as a debt of the State;*
- *the State has not undertaken to "underwrite" the revenues of the project; and*
- *the economic assessments undertaken over the years on proposals for the Western and Southern Bypasses have been consistently supportive of the development. The City Link project will provide a strategic road transport link and integration of Melbourne's freeway system.*

*The Authority however wishes to address 3 matters raised in your report that it believes are not fairly reflected. Firstly, audit has concluded that "However, no evidence was produced to audit in the form of a detailed model, comparing project costings on the basis of private sector financing versus government borrowings." In this respect, the following points should be noted:*

- *Treasury and the Southern and Western Bypasses Co-ordination Team did undertake a base case cost of public sector delivery. This work showed that the relative costs of private and public sector delivery depended on a number of key assumptions and that, depending on the value of these assumptions private sector delivery could be competitive and indeed cheaper than public sector delivery. The work was not progressed beyond this point because it was not possible to finance this project as a public sector project.*
- *Government financing of the project was not a feasible option. Responsible management of the State finances and the debt position precluded this.*
- *The private sector brings significant economies to the design, construction and operation of the Link. In particular, construction costs are significantly reduced. Benefits from infrastructure bonds and depreciation allowance that the private sector can draw on are not available to the State.*
- *As audit has concluded, substantial risks and exposures have been transferred away from the State. This is one of the major advantages in the project being undertaken by the private sector. Risk does not always eventuate, but when it does, it can be very large, for example the cost overruns in the electricity industry.*

*Secondly, audit has reported that while Transurban bears traffic risk, this has been partly mitigated by certain traffic management measures and the status accorded to the Link as a central part of the network.*



□ **RESPONSE** provided by Chief Executive, Melbourne City Link Authority - continued

*In respect of the Agreed Traffic Management Measures, the State has accepted these measures because they enable the most efficient use of the road system and provide significant benefit to local communities. If the State were undertaking the City Link project, these measures would be implemented. The State regard of the Link as a central part of the network derives fundamentally from its strategic importance in linking 3 important roads to improve the economic functioning of the city.*

*Finally, audit has identified a number of obligations and commitments of the State in respect of the Link that it recommends should be disclosed in the financial statements of the Authority and the Government's Statement of Financial Operations. The Authority will comply with all its undertakings and report on these. Fees to the State from Transurban would also be disclosed.*

**LOCAL GOVERNMENT REFORMS**

**3.3.226** Local government provides significant services to the community and in Victoria outlays nearly \$3 billion in the provision of transport, communication, recreation, cultural, health, social, and other general and community services or amenities.

**3.3.227** The institution of local government was formally recognised in Victoria in 1979 when the *Constitution Act 1975* was amended to accord constitutional recognition to the existence of local councils with powers provided by the Parliament to ensure the peace, order and good government of relevant municipal districts.

**3.3.228** The *Local Government Act 1989* sets out the legislative and administrative powers of local government and the regulation of certain related activities, including council operations, rating arrangements, and financial management and accountability arrangements. Currently, the Minister for Planning and Local Government is responsible for local government matters and is assisted in this task by the Office of Local Government, a unit within the Department of Infrastructure.

**3.3.229** Prior to 1992, the broad structure and operation of Victorian local government entities had remained essentially unchanged since the turn of the century. However, over the past 30 years there have been at least 6 major reviews of local government which recognised the need for its restructuring in order to provide economic and social benefits to ratepayers, and the wider community, from a more efficient and effective local government network.

**3.3.230** Although a number of reforms to local government were incorporated in the *Local Government Act 1989* and in amendments to that Act prior to October 1992, the restructuring of councils did not occur.

**3.3.231** In November 1992, as part of the current Government's reform program, a decision was taken to review local government operations. Consequently, in August 1993, the Government created the Local Government Board to provide advice on measures needed to improve the efficiency and effectiveness of municipal councils.

**3.3.232** By the end of 1995, the Government had considered a number of reports submitted by the Local Government Board and, based on their recommendations,

implemented a substantial package of economic and administrative reforms, including a complete restructuring of municipal council boundaries.

**Council restructuring**

*Boundary adjustments*

**3.3.233** Included among the initial referrals by the then Minister for Local Government to the Local Government Board was a request for the review of existing council boundaries, except for the City of Melbourne and the Geelong region which were the subject of specific legislation to restructure boundaries. The Board was required to seek industry, ratepayer and public comment on any restructuring proposals and the final recommendations of the Board to the Minister were required to address all public concerns.

**3.3.234** Based on the recommendations of the Board, council boundaries were revised by the Government. By 20 January 1995, council boundaries had been completely redrawn resulting in a **reduction in the number of councils by 132 (60 per cent), from 210 to 78**. The impact of the restructuring of Victorian municipalities is summarised in Table 3.3C.

**TABLE 3.3C  
COMPARISON OF MUNICIPAL NUMBERS,  
OCTOBER 1992 TO JANUARY 1995**

| Region                   | Council numbers |           |            |
|--------------------------|-----------------|-----------|------------|
|                          | 1992            | 1995      | Reduction  |
| Inner Melbourne          | 18              | 8         | 10         |
| Middle/Outer Melbourne   | 39              | 23        | 16         |
| Geelong/Ballarat/Bendigo | 25              | 7         | 18         |
| South West               | 24              | 8         | 16         |
| North West               | 27              | 9         | 18         |
| North Central            | 16              | 5         | 11         |
| North East               | 37              | 12        | 25         |
| Gippsland                | 24              | 6         | 18         |
| <b>Total</b>             | <b>210</b>      | <b>78</b> | <b>132</b> |

Source: Office of Local Government.

**3.3.235** At the conclusion of the reformation process, Victoria has a leaner local government framework than any other Australian mainland State. This is illustrated in Table 3.3D.

**TABLE 3.3D**  
**MUNICIPALITIES ACROSS AUSTRALIAN**  
**MAINLAND STATES AS AT JUNE 1995**  
 (Number)

| <i>State</i> | <i>NSW</i> | <i>Qld</i> | <i>WA</i> | <i>SA</i> | <i>Vic.</i> |
|--------------|------------|------------|-----------|-----------|-------------|
| Councils     | 178        | 159        | 146       | 124       | <b>78</b>   |

Source: Office of Local Government.

**3.3.236** Once councils had been reconstituted, the Minister for Local Government appointed Commissioners to oversee the actual restructuring within the newly-created councils. The reasons given by the Minister for appointing Commissioners to head the new councils included :

- that exceptional skills were required to oversee council reconstructions; and
- the appointment of councillors as Commissioners might be perceived as conferring an unfair advantage in any subsequent council election.

*Councillors*

**3.3.237** In February 1995, the Minister for Local Government requested the Local Government Board to review and report on the role and function of councillors. The request arose because the role and functions of councillors needed redefining in light of the broad social and economic changes arising from developments within the industry and the Government reforms which necessitated an increased focus by such elected office bearers on policy and strategic issues rather than on routine administrative issues.

**3.3.238** The recommendations of the Board arising from the request for this review included :

- the role and functions of councillors should be prescribed by legislation;
- councillors should be responsible for determining council's policy goals, the appointment of the Chief Executive Officer, and monitoring financial and administrative performance;
- councillor numbers should be limited to between a minimum of 5 and a maximum of 12;
- the level of remuneration that should be paid to councillors;
- the extent of secretarial and communication support to be provided to councillors; and
- that professional development programs should be made available to councillors.

**3.3.239** Following a review of the Board's recommendations, new levels of remuneration for councillors were set in December 1995, ranging from \$5 000 to \$12 000 annually, which reflect the additional responsibilities applying in the restructured councils. Previously, a maximum allowance of \$3 000 had been paid. The allowance for mayors remained unchanged with levels set between \$5 000 and \$100 000.

**3.3.240** In relation to the Melbourne City Council, separate levels of remuneration have been set in recognition of its capital city status. The allowance payable to these councillors is \$18 000 a year while the Lord Mayor's allowance is fixed at \$100 000.



**3.3.241** At the date of preparation of this Report, guidelines for the reimbursement of out-of-pocket expenses were in the process of development. Other recommendations outlined by the Local Government Board concerning the role of councillors were still under consideration by the Government.

**3.3.242** In recent times, there has been significant community concern relating to the independence of directors as they execute their corporate governance obligations. Consequently, there has been much public debate concerning the need to strengthen existing disclosure obligations applicable to *Related Party Disclosures*, being the value of dealings between an entity and external organisations in which individual directors have a financial interest. In the 1994-95 financial year, following overtures by my Office, the Government required additional disclosure in relation to related party transactions for public bodies.

**3.3.243** Although, related party disclosures do not currently apply to Councils, audit has informally recommended to the Office of Local Government that such disclosure requirements also be adopted for this sector. The matter was under consideration at the time of preparation of this Report.

*Executive management*

**3.3.244** In conjunction with the reform process, major changes were made to the executive management culture within councils with the introduction of employment contracts and annual performance assessments for senior management.

**3.3.245** Prior to the reforms, introduced in December 1993, statutory offices existed for the positions of town clerk, city/municipal shire engineer, building inspector etc., with the occupants of those positions required to hold prescribed qualifications. A review of these employment arrangements, conducted by the Office of Local Government, concluded that occupational regulation was no longer relevant and that councils should have access to a wider pool of management skills for senior management than that provided for under the legislation. Therefore, as part of the reforms, statutory positions were abolished and each council was required to appoint a Chief Executive Officer (CEO) with appropriate management skills but not necessarily possessing local government qualifications.

**3.3.246** The CEO is now required to appoint senior management staff in accordance with the council's approved organisational structure and, in accordance with legislation, all senior management positions with remuneration packages in excess of \$60 000 are to be appointed on a contract basis for terms of between 1 and 5 years. An annual review of the CEO's performance is to be conducted by the councillors and of all senior staff by the CEO.

**3.3.247** These reforms are aimed at increasing the effectiveness of senior management, promoting organisational flexibility within councils, and ensuring the accountability of senior executives to councillors and ratepayers.



**3.3.248** It was disappointing to note that prior to the December 1993 proclamation of legislation regarding employment contracts, a number of former councils entered into contracts with existing senior managers on terms and conditions which were clearly at variance with the spirit of the reforms. In response to these actions, the Minister for Local Government directed that councils were not to enter into contracts of more than one year with senior staff and announced that the Office of Local Government was to conduct a review of all senior council staff appointments.

**3.3.249** The results of the review conducted by the Office of Local Government were contained in a report tabled in the Parliament by the Minister in May 1994 which referred to senior staff contracts at 11 former municipalities. The report highlighted :

- an absence of performance criteria within the staff contracts;
- the non-advertisement of senior positions, including that of CEO; and
- that most contracts had been entered into just prior to the commencement of the revised legislation.

**3.3.250** The review resulted in an amendment to the legislation that requires all vacant senior management positions to be advertised externally.

### **Compulsory Competitive Tendering**

**3.3.251** A key element of the Government's reform process for local government was the introduction of a Compulsory Competitive Tendering (CCT) regime.

**3.3.252** The aim of CCT, which was introduced in the 1994-95 financial year, is to require councils to market-test the delivery of a substantial proportion of their services, thereby ensuring that ratepayers obtain both high quality services and value-for-money. The legislative enactment of the Government's policy enables councils to retain considerable autonomy in determining the services to be tendered rather than having specific services nominated by legislation for tender, as occurs in other jurisdictions.

**3.3.253** The requirement that councils comply with the competitive tendering regime is also consistent with the National Competition policy, agreed to by the Commonwealth and State Governments in April 1995, which is aimed at encouraging increased efficiency in government agencies.

**3.3.254** **The essence of the Government's CCT policy is that from July 1996 the total value of operating and capital expenditure of a council that is subject to market-testing in any one year must reach the equivalent of 50 per cent of the total expenses of council as reported in that year's audited operating statement.** The achievement of this target is to occur using a phased implementation program which required the achievement of a 20 per cent target for the 1994-95 financial year and a target of 30 per cent for the 1995-96 financial year.

**3.3.255** The Government expects that substantial savings will be generated under the CCT regime that could be passed on to ratepayers in the form of improved services or rate reductions.





**3.3.256** Under the CCT arrangements, existing service providers within councils are encouraged to compete with external providers for service contracts. To ensure fairness and probity in council tendering practices, the Office of Local Government, in consultation with the industry, developed the *Victorian Local Government Code of Tendering* which was released in August 1995.

**3.3.257** Key elements of the Code of Tendering are :

- tendering practices should be timely and fair to all tenderers;
- councils should clearly separate the roles of service buyer and service provider;
- there is to be complete impartiality between in-house and external providers;
- in-house bids are to be based on full costings; and
- tender panels are to include an independent expert.

**3.3.258** A number of measures have been adopted by the Government to ensure council compliance with CCT requirements. These include :

- a legislative requirement that an audited Compulsory Competitive Tendering Statement be included in the published annual report of each council;
- the responsible Minister may report to the Parliament on the CCT arrangements, outlining details of any non-compliance with the requirements by councils; and
- spot checks on tendering practices by the Office of Local Government.

**3.3.259** In November 1995, the Office of Local Government released the results of a review conducted into the first year of operation of CCT in Victorian councils. The review was based on incomplete and unaudited information. The report highlighted that during the 1994-95 financial year, 94 per cent of councils satisfied the target requirement that expenditure equivalent to 20 per cent of reported expenses was subject to CCT. In addition, the report indicated that 93 per cent of councils actually exceeded the benchmark.

**3.3.260** However, an audit review of the 1994-95 published annual reports of councils revealed that only 58 councils had included a statement relating to CCT, of which 54 councils reported that they had achieved the 20 per cent target. It should be noted that confirming audit opinions were only issued in relation to 48 of the councils who incorporated the statement relating to CCT in their annual report.

**3.3.261** The Office of Local Government, in November 1995, also announced the results of a series of spot audits undertaken by that Office during 1995 which highlighted concerns relating to :

- deficiencies in costing in-house tender submissions;
- the adequacy of the time allowed for tender submissions;
- the need for tender security deposits; and
- the adequacy of the criteria developed for tender evaluation.

**3.3.262** The Office of Local Government when announcing the results of the spot audits indicated that compliance with the Code of Tendering should see the identified deficiencies reduced over time.

**Rate reductions**

**3.3.263** An immediate benefit from council restructuring has been the reduction in the cost of local government to the community. The Office of Local Government has estimated that, based on council budgets, **savings of \$323 million in operating expenditure will be achieved in the 1995-96 financial year** compared with outlays in the 1993-94 financial year. These savings are expected to be generated from economies of scale, elimination of duplication and increased efficiency. However, the savings do not include efficiency gains expected from other reforms, particularly the CCT initiative introduced by the Government.

**3.3.264** The majority of savings arising from council restructuring is expected by the Government to be returned to ratepayers in the form of rate reductions except for approximately \$60 million which will be applied to capital works. In addition, there has been significant estimated rate reductions for the 1995-96 financial year are shown in Table 3.3E.

**3.3.265** **Rate reductions in the order of 18 per cent were incorporated in rate notices forwarded to ratepayers in the last quarter of the 1995 calendar year.** To ensure that these reductions have been passed to, and result in permanent benefits to ratepayers, a system of ongoing monitoring of council budgets has been established within the Office of Local Government.

**TABLE 3.3E  
ESTIMATED RATE REDUCTIONS**

| Region                    | Rate revenues |              |            |           |
|---------------------------|---------------|--------------|------------|-----------|
|                           | 1993-94       | 1995-96      | Savings    | Change    |
|                           | (\$m)         | (\$m)        | (\$m)      | (%)       |
| Inner Melbourne           | 365           | 302          | 63         | 17        |
| Middle/Outer Melbourne    | 688           | 565          | 123        | 18        |
| Geelong/Ballarat/Bendigo  | 126           | 103          | 23         | 18        |
| South West                | 55            | 46           | 9          | 16        |
| North West                | 51            | 43           | 8          | 16        |
| North Central             | 29            | 25           | 4          | 14        |
| North East                | 89            | 73           | 16         | 18        |
| Gippsland                 | 89            | 72           | 17         | 19        |
| <b>Total for Victoria</b> | <b>1 492</b>  | <b>1 229</b> | <b>263</b> | <b>18</b> |

Source: Minister's Review - Local Government in 1995.

**3.3.266** As a result of council restructuring, **rating levels for Victorian ratepayers are now the lowest of any Australian mainland State whereas they were previously the second highest prior to the reform process.** Table 3.3F provides a comparison of estimated rating levels across all mainland States.

**TABLE 3.3F  
COMPARISON OF ESTIMATED COUNCIL RATING LEVELS  
PER CAPITA ACROSS AUSTRALIAN MAINLAND STATES,  
AT JUNE 1995**

| State                 | Qld | NSW | SA  | WA  | Victoria    |            |
|-----------------------|-----|-----|-----|-----|-------------|------------|
|                       |     |     |     |     | Post-reform | Pre-reform |
| Rates per capita (\$) | 358 | 317 | 293 | 271 | <b>269</b>  | <b>324</b> |

Source: Office of Local Government.

**Improvements in financial accountability**

**3.3.267** As part of the reform process, changes have been made to the *Local Government Act 1989* to enhance the financial accountability of local government by improving the annual reporting arrangements and adopting revised audit requirements.

**3.3.268** One of the changes has been the re-alignment of the financial year for councils from the period 1 October - 30 September to 1 July - 30 June. This change will enable more effective comparisons to be undertaken with the public and private sectors and the development of benchmarking programs to ensure best practice is achieved in service delivery.

**3.3.269** In addition, in 1995, the Parliament amended both the *Audit Act 1994* and the *Local Government Act 1989* to extend the mandate of my Office to include the audit of local government, commencing from July 1995. Under this revised arrangement, audit reporting relating to local government will now be annually provided to both ratepayers and the Parliament.

**3.3.270** The Minister for Local Government, when introducing the enabling legislation to the Parliament, indicated that the aim of bringing local government within my purview was to :

- ensure greater consistency in accounting treatments and disclosures across the State, thereby improving the usefulness of financial information provided by councils;
- make it easier for the Government and ratepayers to identify significant financial issues impacting on all councils; and
- enable the Government and the community to gain a snapshot of the health of local government.

**3.3.271** These enhancements should improve the quality of annual reporting by local government and the overall accountability of councils to their ratepayers and the Parliament.

**Performance measurement**

**3.3.272** The absence of a consistent basis for the measurement of the performance of council services and activities across Australia has been perceived by both Government and the industry as a key obstacle to improving the efficiency of local government operations. The adoption of benchmarking processes by councils was perceived by the responsible Minister and the industry as enabling councils to comprehensively measure performance against the best in the field and then develop appropriate strategies to achieve improvements in service delivery.

**3.3.273** In 1992, the Office of Local Government published the first edition of *Local Governments - Side by Side*, a comparative analysis of selected financial indicators covering all Victorian councils for the period 1988 to 1991. The purpose of the publication was to assist the former councils to improve their financial performance by highlighting their individual standing against other councils. A second edition of the publication was issued in December 1993 covering the financial period 1988 to 1992.

**3.3.274** While these publications assisted the former councils in assessing their financial performance relative to their State counterparts, they were restricted to Victoria and only had a financial focus.

**3.3.275** In March 1994, the Australian Local Government Ministers Conference selected the Victorian Office of Local Government to undertake a national pilot study to develop benchmarking methods. Considerable input to the study was provided by a number of Victorian councils. The second phase of the project was to develop *aids to benchmarking*.

**3.3.276** In October 1995, the project concluded with the release of the pilot report and a kit entitled *Benchmarking for Local Government: A Practical Guide* which was distributed to every council in Australia and New Zealand. The kit provided explanatory materials on the implementation of benchmarking by councils.

**3.3.277** The Office of Local Government, in association with the industry, is continuing its research in this area with future developments expected to include, among other things, the development of national benchmarking and performance indicators for specific services or functions.

**3.3.278** The support for performance measurement in local government through the development of benchmarking techniques should lead to more efficient and effective local government service delivery by enabling councils to compare their performance with best practice and introduce appropriate measures to improve service delivery, where necessary.

**Central agency oversight of reforms**

**3.3.279** The Office of Local Government is the administrative unit within the Department of Infrastructure which has policy responsibility for the operation of local government at a State level and assists councils in executing their responsibilities under the *Local Government Act 1989* and associated regulations.



**3.3.280** In recent times, a key role of the Office has been to monitor the implementation of the local government reforms. The Office undertakes the monitoring of the reforms through a variety of activities, including monthly reporting by councils on key issues, the issuing of circulars and documents on important matters, and regular contact with councils.

*Monitoring of rates*

**3.3.281** A major monitoring activity of the Office of Local Government has been to ensure that rate reductions generated from council restructuring are returned to ratepayers. This is mainly achieved through the monitoring and analysis of councils' financial and budget positions, and employment levels. In particular, the Office requests councils to submit details of their annual budgets and monitors their budget performance on a regular basis by requesting 6 monthly budget update reports. Any issues arising from the review of the information provided are identified and discussed with the councils. The timely completion of information requested from councils is required to ensure the effective monitoring of council operations by the Office of Local Government.

**3.3.282** However, at the time of the audit review in March 1996, the 6-monthly review of all council budgets for the period 1 July 1995 to 31 December 1995 had not been finalised due to delays in councils providing their reports to the Office of Local Government. **The timely completion of these reviews should ensure more effective monitoring of council operations.**

*Monitoring of CCT*

**3.3.283** As indicated previously, councils are required to include in their annual report an audited Compulsory Competitive Tendering statement. In addition, the annual report must highlight any non-achievement of CCT targets together with appropriate explanations.

**3.3.284** The Office of Local Government reviews monthly reports provided by councils and the audited Compulsory Competitive Tendering statement, with the results of the reviews forming the basis of a Ministerial report to the Parliament. As indicated previously, the Office also conducts a program of spot checks to ensure that CCT tendering processes are conducted in accordance with the Government's CCT requirements and policies.

*Accountability*

**3.3.285** The Office of Local Government also monitors compliance with the improved reporting requirements established by the Government and provides guidance on management practices to be adopted by councils in such areas as corporate planning, budgeting, rating arrangements and annual reporting. In addition, the Office maintains ongoing consultation with the Ministerial Standing Committee on Local Government Financial Management to ensure financial practices in councils represent best practice.

**3.3.286** **Monitoring of council activities by the Office of Local Government should ensure that high standards of management and accountability are maintained.**

*□ RESPONSE provided by Director, Office of Local Government*



*The Office of Local Government welcomes the audit report on the administration of the local government reforms. The audit confirms that the far-reaching reforms have, for the most part, been introduced effectively with real benefits to ratepayers and residents.*

*The November 1995 review on CCT results released by the Office of Local Government was based on the best available information (refer paragraph 3.3.258 of this Report).*

*Audit's comments in relation to audited CCT statements have been noted. The legislation clearly requires councils to include audited CCT statements in their annual reports and the Office of Local Government will be requesting councils to comply with the legislation. It is expected that the Auditor-General will be monitoring compliance with the legislation.*

*As referred to in paragraph 3.3.281, reviews have been completed by the Office of Local Government for all those councils which have submitted the required information. Four councils are yet to submit their 6 monthly budget reviews and these are being pursued with the councils involved.*

**FINANCIAL STANDING OF MUNICIPAL COUNCILS ON CREATION**

**3.3.287** Given the substantial restructuring of councils during 1994, the Office of Local Government encouraged the Commissioners of the newly created councils to undertake independent reviews of the financial standing of their councils as at the date of their creation.

**3.3.288** The benefits arising from the completion of these reviews, known as due diligence audits, were :

- the independent confirmation of the consolidated financial position of each new council as at the date of its creation;
- the identification of areas where efficiency gains could be achieved; and
- the provision of recommendations for improving financial management.

**3.3.289** The scope of each due diligence audit was formulated and approved by the Commissioners of the individual councils prior to the commencement of the reviews, and usually included :

*Consolidated financial position*

- *the establishment of the consolidated financial position of the new council as at the date of its creation;*
- *the establishment of the actual cash position of the new council as at the date of its creation;*



- *the determination of trust funds held as at the date of creation; and*
- *the identification and examination of reserve funds to ascertain the justification for their continued existence.*

*Inappropriate actions prior to creation*

- *the identification of any significant budget re-allocations or variations that had occurred in the former councils since the adoption of their budgets for the period prior to their abolition.*

*Exposures*

- *a review of entrepreneurial activities to identify exposures for the new council;*
- *the identification of exposures associated with contingent liabilities in relation to legal actions commenced or about to commence;*
- *the determination of accruals of interest, gratuities etc. for officers and employees;*
- *a review of employment conditions within the new council to identify any inconsistencies and industrial relations exposures;*
- *the identification and examination of exposures relating to leasing agreements, guarantees and forward commitments under contracts entered into by the former municipalities; and*
- *the quantification of accumulated annual, long service and sick leave for all council officers and employees as at the date of creation.*

*Potential efficiencies*

- *a review of the bank accounts, insurances, investment and loan portfolios to identify potential efficiency enhancements;*
- *a review of information technology arrangements to identify any exposures and the potential for savings through rationalisation; and*
- *the provision of suggestions on financial strategies for Commissioners to consider when preparing forward budgets.*

*Other*

- *reporting of any other matters considered relevant arising from the audit review, e.g. undeclared conflicts of interest by former councillors.*

**3.3.290** The due diligence audits also examined whether the practices, policies, procedures and delegations of the former councils were in accordance with the requirements of the *Local Government Act 1989* and other relevant Acts and Regulations.

**How many due diligence audits were conducted ?**

**3.3.291** As indicated previously, the restructuring of local government in Victoria resulted in the number of local councils being reduced from 210 to 78 by January 1995. Approximately 90 per cent of the new councils were subject to a due diligence audit as at the date of their creation, as shown in Table 3.3G.

**TABLE 3.3G  
DUE DILIGENCE AUDITS  
OF LOCAL COUNCILS**



| <i>Due diligence audits</i>          | <i>Numbers</i> |
|--------------------------------------|----------------|
| Conducted by the Auditor-General     | 47             |
| Conducted by private sector auditors | 24             |
| Not undertaken                       | 7              |

**3.3.292** Audit is aware that councils which held elections on 16 March 1996 had completed a further independent due diligence audit or commissioned an independent review within the 3 month period prior to the elections so that the elected councillors would have available to them current independent information concerning the financial position of their respective council and, in some instances, the exposures facing that council. These examinations were conducted by private sector auditors as my Office, being the external auditor of all councils from July 1995, could not provide the independent assurance required from such reviews due to a perceived conflict of interest arising from my exiting audit involvement.

**What were the findings of the initial due diligence audits?**

**3.3.293** The major findings of the due diligence audits conducted as at the creation of the new councils and reported to Commissioners are summarised as follows :

*Consolidated financial position*

- 6 of the new councils were assessed as being in a weak financial position as at the date of their creation reflecting the poor financial practices of the former councils;
- 58 councils held reserves, which were supported by the cash and investments, that were not subject to legislative restriction and could therefore be used for other council purposes;
- 13 per cent of councils had low cash holdings as at the date of their creation;
- Most former councils had not adequately monitored the activities of their controlled entities, such as committees of management; and
- There was a lack of focus on long-term financial planning in most former councils.

*Inappropriate action prior to creation*

- There were instances of former councils accelerating their expenditure, committing to major contracts or reviewing staff salaries in the 3 month period prior to the creation of the new councils which had the potential to disadvantage the new councils by imposing obligations on them that were onerous.





*Exposures*

- 2 former councils inappropriately invested significant funds;
- A number of former councils had been involved in entrepreneurial activities, such as shopping centres, leisure centres, industrial estates and an electricity co-generation scheme which had the potential to expose ratepayers to unwarranted financial burdens;
- A number of former councils operated gratuity schemes which enabled staff to accumulate benefits for retirement, including the payment of a proportion of accumulated sick leave entitlements;
- 32 former councils had provided guarantees to sporting clubs and commercial entities to support borrowings raised by those entities;
- Many councils provided council-owned or controlled assets, being land or buildings, to community groups on a long-term basis at peppercorn rentals. In several instances, such assets were used by the community groups for commercial purposes;
- It was common practice for councils to allow their staff to accumulate excessive annual leave and long service leave entitlements; and
- There were inconsistent employment conditions across councils, such as differences in hours of work, leave provisions and allowances, and over-award payments.

*Potential efficiencies*

- Individual councils held a large number of bank accounts that could be rationalised with savings achievable through the tendering of banking services and reductions in associated administrative costs;
- Investments were generally managed with a short-term focus;
- There was potential to rationalise loan portfolios to reduce the cost of borrowing;
- Information technology within the new councils needed to be rationalised and enhanced to provide current managers with timely information needed to ensure that the new councils were able to operate in an efficient and effective manner; and
- Opportunities existed to achieve savings by taking advantage of the economies of scale provided by council amalgamation, including asset rationalisation.

**3.3.294** The findings of each due diligence audit, together with recommendations aimed at enhancing the future management of the restructured councils, were provided to Commissioners who had responsibility for determining the nature and extent of the publication of these findings to their ratepayers.

**3.3.295** An audit survey has indicated that Commissioners have elected to publicise the findings of the due diligence audits in their local community using the local press and council meetings, which generated considerable community interest.

**3.3.296** Councils have put in place a program to respond to the recommendations contained in the due diligence audit reports and the Office of Local Government is monitoring councils' progress in dealing with these issues.



**PEPPERCORN RENTALS FOR COMMUNITY ASSETS**

**3.3.297** An issue that was consistently highlighted during the due diligence audit process was the lease of council assets to various organisations or persons for a variety of purposes for nominal or peppercorn rentals.

**3.3.298** In instances where the use of a council asset was for community or not-for-profit activities, the lease was usually agreed to by council for an extended period on the basis of satisfying a community service obligation, such as the provision of sporting, recreational or cultural services or facilities.

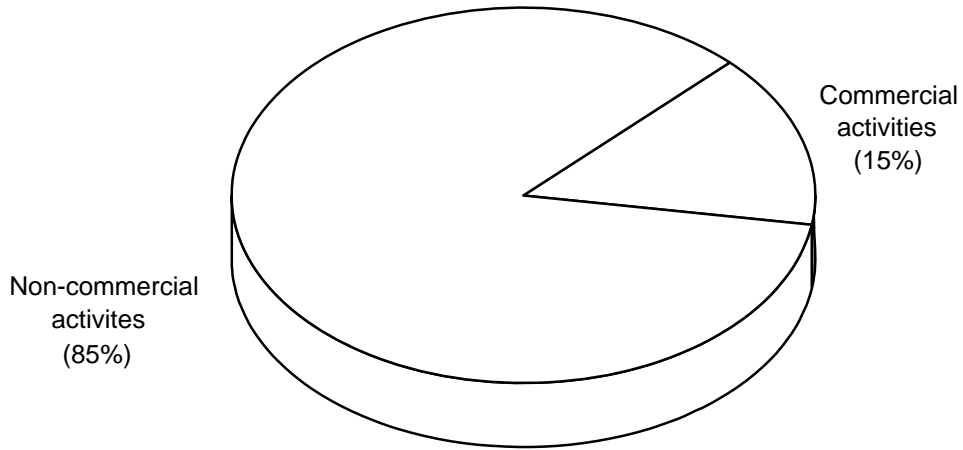
**3.3.299** In circumstances where non-commercial rentals apply, the council is in fact providing an implicit subsidy to the relevant organisation or persons equivalent to the difference between the commercial rental that could be charged and the peppercorn rental actually charged.

**3.3.300** Given the long-term nature of many of these leases and the low return to councils achieved as a consequence of the peppercorn rentals, it is important that the lease agreements include provision for periodic re-assessment to cater for situations where the value of the asset has increased over time or where the use of the asset by the occupant has changed to a commercial or profit making purpose.

**3.3.301** Based on the findings of the due diligence audit process, audit subsequently surveyed 15 councils to identify progress made on the implementation of the recommendations to review the ongoing appropriateness of peppercorn rentals.

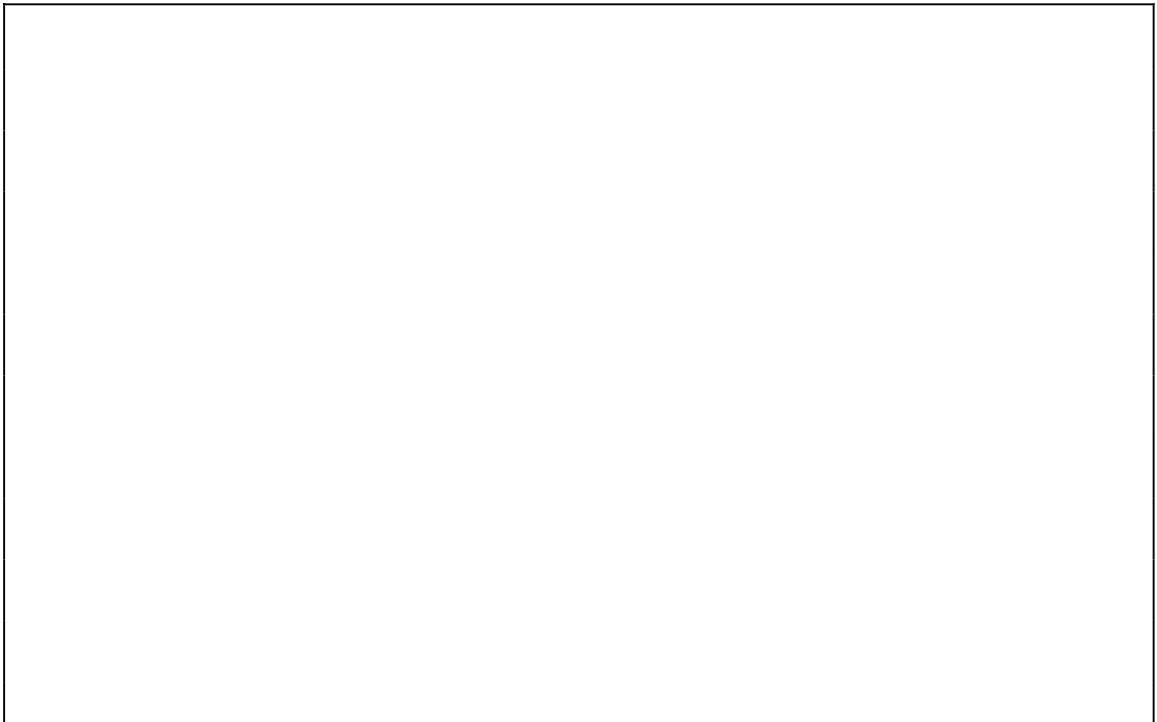
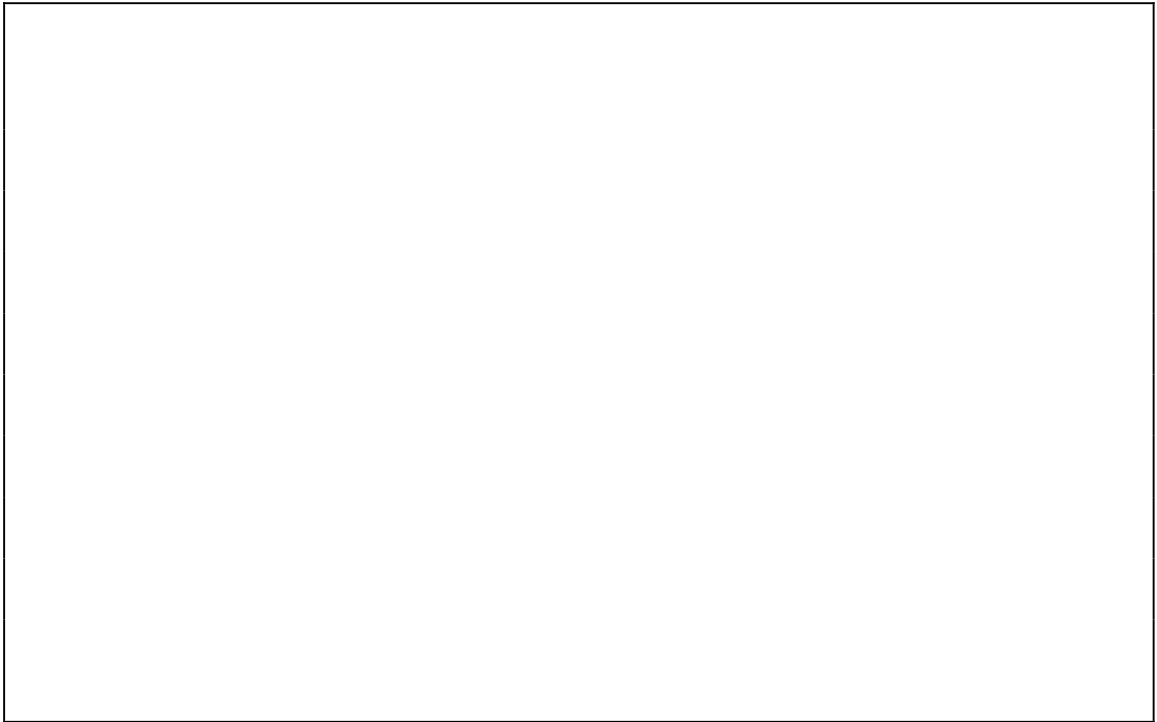
**3.3.302** As indicated in Chart 3.3H, peppercorn or non-commercial rentals applied to council-owned assets which were leased and utilised for commercial ventures, in 15 per cent of the councils surveyed by audit.

**CHART 3.3H  
SURVEYED COUNCILS WITH PROPERTIES UTILISED  
FOR COMMERCIAL PURPOSES THAT ARE  
SUBJECT TO PEPPERCORN RENTALS**



**3.3.303** An analysis of the survey responses indicated that:

- the majority of councils had at least one asset that was leased for a peppercorn rental and was currently used by the occupant to provide gaming and licensed entertainment services;
- in the majority of instances, the rentals levied by the controlling council ranged from the nominal amount of \$1 to \$1 800 a year;
- inadequate records were maintained of council properties subject to lease;
- inconsistencies existed between councils as to the determination of the appropriate rentals to be charged for community facilities, such as recreation reserves; and
- there were instances where lease terms were for an indefinite period.



*Gaming facilities operating on council land and paying a peppercorn rental.*



**3.3.304** The survey results confirm that a number of leases had not been effectively managed by the former councils resulting in a loss of revenue to ratepayers which could have been utilised for the provision of wider community services.

**3.3.305** However, the councils surveyed indicated that they were currently reviewing all rental arrangements with the aim of developing a register of relevant agreements. Furthermore, the councils indicated that agreements will be reviewed in the near future on an individual basis to ensure that appropriate rentals are charged relative to the use of the asset.

**3.3.306** To ensure that the ratepayers' interests are protected, it is important that councils regularly review all leasing arrangements. In addition, in order to ensure the effective management of assets, councils should be aware of the extent of implicit subsidies provided to organisations or persons in instances where commercial lease rentals are not charged.

*□ RESPONSE provided by Director, Office of Local Government*

*Audit's findings in relation to its survey on peppercorn rentals for community assets have been noted and will be drawn to the attention of all councils.*

## DEBT LEVELS WITHIN MUNICIPAL COUNCILS

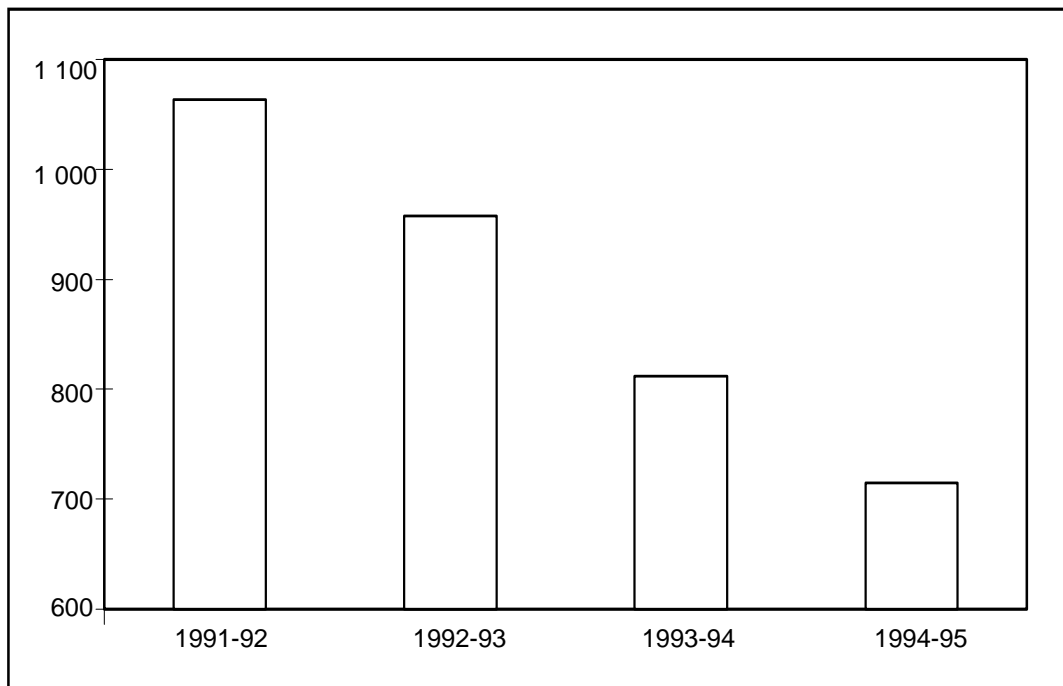
### Borrowings

**3.3.307** Powers conferred on local councils under the *Local Government Act 1989* include the capacity to borrow. In the past, a significant level of capital expenditure was financed from borrowings.

**3.3.308** Surveys of Victorian local government finances, which included the long-term indebtedness of councils as at 30 June 1992, indicated that debt levels were around \$1 billion with associated debt servicing costs of \$148 million. Furthermore, the ratio of council debt servicing outlays to rate revenues was, on average, 16 per cent with 38 per cent of councils spending 50 per cent or more of their rate revenue on debt servicing costs and administrative expenditure.

**3.3.309** However, since the 1991-92 financial year, there has been a substantial reduction in the level of debt held by councils, as illustrated in Chart 3.3I.

**CHART 3.3I**  
**COUNCIL DEBT LEVELS,**  
**1992 TO 1995**  
 (\$million)



Source: *Local Government Finance, Victoria, 1991-92 to 1993-94*, Australian Bureau of Statistics.  
*Council Debt Levels, 1994-95*, Office of Local Government.

**3.3.310** The above chart highlights that **debt levels of councils have decreased by \$330 million since the 1991-92 financial year, representing a 31 per cent reduction over a 3 year period.**

**3.3.311** The major reasons for this reduction were:

- the application of funds derived from asset sales, reductions in financial assets and cash surpluses arising from reforms during the 1994-95 financial year; and
- an increased focus by councils on debt management issues following:
  - the annual publication of council budgets, including debt levels, borrowing and redemption proposals;
  - the disclosure of debt-related indicators and other ratios in the financial statements of councils; and
  - the publication of global comparative data relating to debt servicing costs and associated ratios for all councils.



**3.3.312** In addition, during the 1994-95 financial year, new procedures were established by the Department of Treasury and Finance to improve the borrowing practices of councils, including:

- The abolition of councils' automatic right to new borrowings of \$1 million. Previously, under the established arrangement, councils could raise new borrowings of up to \$1 million regardless of need which, over time, encouraged some councils to borrow funds to create unnecessary cash reserves;
- The development of prudential guidelines for the evaluation of new borrowing proposals by councils; and
- The appointment of the Municipal Association of Victoria as the co-ordinator of council borrowing requests and to supervise the loan allocation process subject to overall control and reporting to the Department of Treasury and Finance.

**3.3.313** The revised arrangements for new borrowings should assist councils to ensure that borrowings are raised in accordance with their actual financing needs and their capacity to service the debts incurred. In addition, **the reductions in debt levels and associated debt servicing costs will improve the financial viability of councils, thereby creating additional opportunities for the allocation of resources to new services or reductions in the rates payable by ratepayers.**

**Unfunded superannuation liabilities**

**3.3.314** Unfunded superannuation liabilities in local government arise in relation to council employees who are members of the Local Authorities Superannuation Fund's Defined Benefits Scheme. The Scheme also provides benefits to other public sector employees, however, local government employees are the major members of the Scheme.

**3.3.315** Under the Fund's enabling legislation, a full actuarial investigation into the financial position of the Scheme is required to be completed every 3 years with the latest investigation completed as at 30 June 1995. Following this investigation, **the Scheme has disclosed an unfunded liability in respect of council employees at 30 June 1995 of \$187 million, a reduction of \$90 million since June 1992.**

**3.3.316** The major reasons for the decrease in the Scheme's unfunded liability over the 3 year period include:

- the Government's reform of public sector superannuation arrangements, including the closure of the Scheme to new members as from 1 January 1994; and
- the exit of several thousand council members from the Scheme due to local government restructuring.

**3.3.317** The Fund's actuary reported at the completion of the latest investigation that, depending on the Fund's future financial performance, a continuation of employer contributions at current rates should ensure that the Scheme is fully-funded by the year 2012.





**URBAN LAND AUTHORITY PROPERTY DEALINGS**

**3.3.318** The Urban Land Authority was established in March 1980 as the successor of the former Urban Land Council which had been in existence since 1975. The legislative objectives of the Authority, as set out in the *Urban Land Authority Act 1979*, are to:

- provide developed and development allotments as directed by the Minister;
- facilitate the disposal of surplus land held by the Crown and public bodies; and
- assist in the implementation of State urban planning policies and major State projects at the direction of the Minister through the acquisition, development and sale of land.

**3.3.319** As part of the reform program implemented by the Government, the Authority in April 1994 was declared a "re-organising body" under the *State Owned Enterprises Act 1992*, with a view to its corporatisation and the refocus of its activities to concentrate more on revitalising the urban areas within Victoria, with particular emphasis on central Melbourne. At the same time, a new Board was appointed by the Government to oversee the re-organisation of the Authority.

**3.3.320** Upon its appointment, the new Board initiated a comprehensive review of the activities undertaken by the Authority. As part of the review, a 3 year Corporate Business Plan was developed which refocused the Authority's activities towards the redevelopment and revitalisation of Melbourne, with less emphasis on residential development on the urban fringe of Melbourne, in line with Government expectations. In particular, the Authority determined that its strategic objectives over this period would be to:

- stimulate economic development activity in the urban land market;
- supply and maintain levels of housing affordability;
- act as a vehicle for the achievement of planning and housing policy objectives;
- provide good quality urban environments; and
- operate in a business-like manner as a complement to the private sector.

**3.3.321** To facilitate the achievement of these objectives and the related strategies, the Authority was restructured with a *new team-based* focus integrating the project management, marketing and administration functions.

**Assessment of Authority's performance**

**3.3.322** As part of its 3 year Corporate Business Plan, the Authority introduced for the 1994-95 financial year a series of benchmarks against which its performance could be measured. Table 3.3J provides a summary of the Authority's actual performance for 1993-94 and its performance in the 1994-95 financial year against the newly established benchmarks.



**TABLE 3.3J**  
**AUTHORITY'S FINANCIAL PERFORMANCE AGAINST BENCHMARKS**

| <i>Benchmarks</i>                                | <i>1994-95 (Forecast)</i> | <i>1994-95 Actual</i> | <i>1993-94 Actual</i> |
|--------------------------------------------------|---------------------------|-----------------------|-----------------------|
| Earnings before interest and income (EBIT)/Sales | 16%                       | 18.8%                 | 18.7%                 |
| EBIT/Total assets                                | 6%                        | 6.4%                  | 6.7%                  |
| Net profit after tax/equity                      | 1%                        | 3.5%                  | 5%                    |
| Sales volume                                     | \$82m                     | \$76.4m               | \$76.5m               |
| Overhead /Sales                                  | 13%                       | 12.8%                 | 14.3%                 |
| Borrowings                                       | -                         | -                     | -                     |
| Value added per employee (a)                     | \$385 000                 | \$369 000             | \$312 000             |

(a) Represents average sales revenue per employee.

**3.3.323** The table shows that, while the Authority did not achieve its established sales volume benchmark during the 1994-95 financial year, the majority of the other benchmarks were exceeded. However, an audit analysis of the financial performance of the Authority found that despite an 8 per cent increase in its revenue between the 1992-93 and 1994-95 financial years, the net profit of the Authority had decreased over the past 3 years. Table 3.3K illustrates this position.

**TABLE 3.3K**  
**FINANCIAL PERFORMANCE OF THE AUTHORITY,**  
**1992-93 TO 1994-95**  
**(\$'000)**

| <i>Item</i>                                                           | <i>1992-93</i> | <i>1993-94</i> | <i>1994-95</i> |
|-----------------------------------------------------------------------|----------------|----------------|----------------|
| <i>Revenue -</i>                                                      |                |                |                |
| Sales of Authority land                                               | 71 075         | 76 512         | 76 407         |
| Other Income                                                          | 3 232          | 2 072          | 3 589          |
| <b>Total</b>                                                          | <b>74 307</b>  | <b>78 584</b>  | <b>79 996</b>  |
| <i>Expenditure -</i>                                                  |                |                |                |
| Cost of Land Sales                                                    | 41 233         | 48 517         | 47 592         |
| Operating Expenses                                                    | 16 634         | 15 724         | 17 939         |
| <b>Total</b>                                                          | <b>57 867</b>  | <b>64 241</b>  | <b>65 531</b>  |
| <i>Operating Profit before abnormal items and income tax expenses</i> | 16 440         | 14 343         | 14 465         |
| Less/(add):                                                           |                |                |                |
| Abnormal items                                                        | (2 741)        | -              | 10 575         |
| State Equivalent Tax                                                  | -              | 4 743          | (2 931)        |
| <b>Net profit</b>                                                     | <b>19 181</b>  | <b>9 600</b>   | <b>6 821</b>   |



**3.3.324** The main factors which have influenced the Authority's operating results over the past 3 years were:

- The depressed real estate market in recent years which adversely impacted on the value of certain of the Authority's undeveloped land holdings, resulting in a \$10.5 million write-down in the value of these holdings during the 1994-95 financial year;
- The requirement by the Government for the Authority to pay State Equivalent Taxation on earnings from the 1993-94 financial year;
- The cessation of the Homestart Scheme, which assisted first home buyers and low income earners while at the same time generating building activity, and the depressed residential market over the past few years contributing to a 33 per cent decrease in the number of property lots sold by the Authority between the 1992-93 and the 1994-95 financial years. Despite this decrease, the average selling price per lot has increased by 36 per cent, from \$41 397 to \$56 426. However, this upward movement in the sale price of lots generally reflected the higher value associated with the development of property in the inner and middle suburbs of Melbourne; and
- The requirement for the Authority to pay a backlog of land tax on certain Crown land in the 1994-95 financial year.

*□ RESPONSE provided by Executive Chairman, Urban Land Authority*

*This point references the adverse impact of property devaluations on the ULA's financial results during the 1994-95 financial period. The property "devaluation" brought to account in 1994-95 was a direct result of the conservative accounting policies adopted by the ULA. These policies require ULA to reflect property values at the "lower of cost or realisable value" in the accounts. As a consequence, should any ULA property valuation fall below its book value, ULA must record that fall in value in that year. On the converse, any appreciation in property values are "ignored" in the accounts until that gain is realised.*

*The ULA believes the inference that a devaluation recorded as a result of an accounting policy is not a true indicator of ULA "performance". Management believes any "performance" review should make reference to the potential "revaluation" of assets not reflected in the accounting statements. Had the net movements in land values been considered the ULA would have reported an increase in its land valuations.*

**Developments undertaken by the Authority**

**3.3.325** The Authority achieves its objectives mainly by undertaking residential developments and urban redevelopments, and participating in joint ventures. All projects undertaken by the Authority are approved by the responsible Minister as required by the *Urban Authority Act 1979*.

**3.3.326** At 30 June 1995, the Authority's land holdings were valued at \$121 million, with a further \$36 million committed for property acquisitions for the purpose of future redevelopments.

*Residential developments*

**3.3.327** Residential developments undertaken by the Authority in recent years have been predominantly in the outer metropolitan growth areas of Melbourne. A summary of the residential properties developed by the Authority and sold over the past 3 years is shown in Table 3.3L.

**TABLE 3.3L**  
**RESIDENTIAL PROPERTIES RELEASED FOR SALE AND**  
**SOLD, 1992-93 TO 1994-95**  
(number)

| <i>Item</i>                                | <i>1992-93</i> | <i>1993-94</i> | <i>1994-95</i> |
|--------------------------------------------|----------------|----------------|----------------|
| Stock available for sale at 1 July         | 832            | 848            | 451            |
| Released for sale                          | 1 955          | 1 145          | 1 432          |
| Sold                                       | (1 939)        | (1 542)        | (1 276)        |
| <b>Stock available for sale at 30 June</b> | <b>848</b>     | <b>451</b>     | <b>607</b>     |

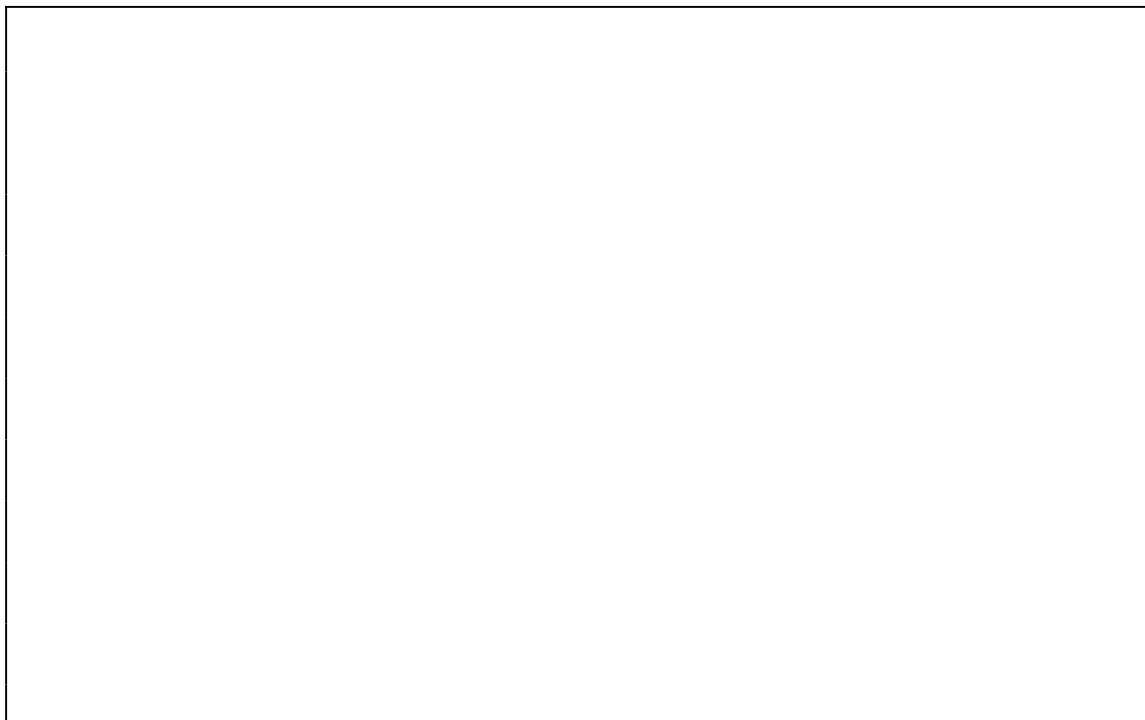
**3.3.328** Comments follow on 2 major residential estates developed by the Authority.

*Roxburgh Park*

**3.3.329** Roxburgh Park is situated at Somerton, north of Melbourne and is the Authority's largest development. The estate, which covers 566 hectares, is expected to provide homes for 26 000 people by the year 2003 and was purchased between May 1987 and January 1993 at a cost of around \$26 million. The development of the estate commenced in November 1991, with the first allotments released for sale in May 1992. The Authority's vision for the estate is to provide a fully-integrated residential development incorporating community facilities such as neighbourhood community centres, and primary and secondary schools.

**3.3.330** Between May 1992 and December 1995, the Authority had sold 1 413 lots which generated revenue of \$58.3 million, after incurring associated costs of \$45.7 million. Accordingly, the development of this estate has returned a gross profit to the Authority of around \$12.6 million up to December 1995.

**3.3.331** At 30 June 1995, the Authority revalued the land relating to the Roxburgh Estate, resulting in a decrease in its value by around \$5.7 million due to the down-turn in the property market since the acquisition of the estate.



*Roxburgh Park Estate situated at Somerton.*

*Goonawarra Estate*

**3.3.332** The development of the Goonawarra Estate, situated at Sunbury, north-west of Melbourne, was initially commenced in 1978 by the former Housing Commission of Victoria. In April 1983, the estate was vested with the Authority for its development, with the first priority to re-design the estate in a way that would improve the number of lots that could be developed.

**3.3.333** In June 1992, the Minister approved the Authority's purchase of the vested land, covering 205.6 hectares. The purchase price of \$8.7 million was based on the lower of 2 valuations: one provided by the Valuer-General and the other by a private sector valuer.

**3.3.334** Between July 1992 and December 1995, the Authority developed 172 lots and sold 94 of these lots, generating revenue of \$3.1 million after incurring associated costs of \$2.1 million. In relation to the 78 lots that were not sold, the Authority incurred costs of \$2.3 million.

**3.3.335** In May 1995, the Authority placed the estate covering 185 hectares for sale through public tender. However, the sale did not proceed due to concerns raised by prospective purchasers regarding the impact on the Goonawarra Estate of the Authority's proposed Jackson's Hill redevelopment project also located in Sunbury. At the date of preparation of this Report, the Authority was undertaking a review of future development options for the estate.

**3.3.336** At 30 June 1995, the Authority revalued the land relating to the Goonawarra Estate resulting in a decrease in its valuation by around \$3.4 million.

*Urban re-development*



**3.3.337** The redevelopment of surplus and under-utilised government land has been an integral part of the Authority's operations. The Range Estate, Williamstown, was the major redevelopment project undertaken by the Authority in the 1994-95 financial year. However, there are a number of other areas currently approved for redevelopment, such as Jackson's Hill at Sunbury and the Bundoora/Mont Park Precinct, north of Melbourne.

*The Range*

**3.3.338** In 1987, the Authority purchased the former rifle range at Williamstown, west of Melbourne, comprising an area of around 110 hectares from the Commonwealth Government for \$11.7 million. The Authority proposed to develop 60 hectares of the property for housing and related commercial and community activities, while the remaining 50 hectares was to be reserved for the protection of the surrounding environmentally sensitive area.

**3.3.339** Following the Authority's acquisition of the estate, it was listed as a contaminated site by the Environment Protection Authority. Although the Authority endeavoured to obtain compensation from the Commonwealth Government to finance the contamination clean-up, it was not successful. **The total cost incurred by the Authority to 31 December 1995 for the de-contamination of the site was \$3.7 million, with a further \$640 000 in costs expected to be incurred with the release of future stages of the estate.**

**3.3.340** Following consideration of various proposals, in November 1989, the Authority approved the development of the estate. The development which commenced in January 1990 is earmarked for completion in 1997, with allotments progressively released for sale from May 1991.

**3.3.341** The development of the Range has been one of the most successful projects undertaken by the Authority, with keen demand for the developed lots. Between May 1991 and December 1995, the Authority sold 510 lots, generating revenue of \$48 million with associated costs of \$33.3 million, resulting in a gross profit of \$14.7 million.



*The Range Estate at Williamstown.*

*Joint ventures*

**3.3.342** Since 1991, joint ventures have increasingly played an important part in the Authority's development program. In particular, the Authority has sought joint ventures to acquire the necessary skills and expertise to effectively redevelop strategic sites. A summary of the joint venture developments undertaken by the Authority over the past 3 years is shown in Table 3.3M.

**TABLE 3.3M  
JOINT VENTURES UNDERTAKEN BY THE AUTHORITY**

| <i>Estate</i>            | <i>Location</i> | <i>Description</i>                                                                                                                                        | <i>Proposed dwellings/ lots</i> | <i>Dwellings/ lots sold</i> | <i>Authority's share of profit/(loss) as at 31/12/95</i> | <i>Status</i>               |
|--------------------------|-----------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------|-----------------------------|----------------------------------------------------------|-----------------------------|
| The Mews                 | East Melbourne  | Residential development comprising refurbished historic school buildings and new apartments.                                                              | 46                              | 46                          | \$108 000                                                | Completed                   |
| St Vincent's Terrace     | South Melbourne | Construction of terrace houses on the grounds surrounding former school buildings.                                                                        | 19                              | 19                          | \$443 000                                                | Completed                   |
| Yarraberg Estate (Lot 4) | Richmond        | Residential apartments on a former TAFE site overlooking the Yarra River.                                                                                 | 29                              | 29                          | \$235 000                                                | Completed                   |
| Hillcrest Park           | Meadow Heights  | Mixed residential lots ranging from terraces to conventional 4 bedroom homes, developed on a former government-owned site.                                | 43                              | 43                          | \$478 000                                                | Completed                   |
| The Range (Lot 25)       | Williamstown    | Development comprises 2 and 3 storey terrace houses on the former Williamstown Rifle Range.                                                               | 19                              | 19                          | \$660 000                                                | Completed                   |
| McKean Street            | North Fitzroy   | Comprising terrace and warehouse apartments on a former Public Transport Corporation bus depot.                                                           | 13                              | 13                          | \$424 000                                                | Completed                   |
| Lynbrook Estate          | Lyndhurst       | Residential development with an emphasis on energy efficient housing and traditional neighbourhood design with high quality presentation and landscaping. | 600                             | 44                          | (\$284 000)                                              | Currently under development |

**3.3.343** As shown in Table 3.3M, the Authority has completed 6 joint venture projects which have resulted in the construction of 169 dwellings, with each project generating profits. Under each of the arrangements, the Authority contributed the land and the joint venture partner developed and sold the units to the public, with both parties entitled to a share of the profits. The Authority envisages seeking joint venture partners for an additional 5 projects in the 1995-96 financial year.

**3.3.344** Comments on 2 joint venture developments follow.



*The Mews*

**3.3.345** The Mews redevelopment in East Melbourne, which was approved by the Minister in June 1992, was the Authority's first joint venture arrangement. A condition of the Minister's approval was that the developer, inter alia, had to satisfy the Authority of its financial viability and arrange suitable finance for the project on terms acceptable to both parties to the agreement.

**3.3.346** However, the developer was subsequently unable to arrange finance, on terms and conditions acceptable to the Authority, to meet the obligations under the agreement and, in April 1993, a decision was made by the Authority to enter into a subsidiary agreement with the developer's financier, under which the financier was provided by the Authority with:

- an unconditional guarantee for an \$8.6 million loan facility raised by the developer; and
- a first mortgage over the development sites.

**3.3.347** The Authority's overall contribution to the project was the land, which had been valued by the Valuer-General at 30 June 1992 at \$1.5 million, together with \$600 000 in related property costs and the provision of a guarantee to the developer's financier of \$8.6 million.

**3.3.348** In the Auditor-General's May 1994 *Report on Ministerial Portfolios*, the following concerns were raised on this joint venture arrangement:

- the Authority substantially accepted responsibility for the financial risks of the project without revision of the profit sharing arrangement; and
- the Authority anticipated a net return of only around \$100 000 on the venture.

**3.3.349** **The Mews project was completed in the 1994-95 financial year with the Authority receiving a net return of around \$108 000.**

*□ RESPONSE provided by Executive Chairman, Urban Land Authority*

*Reference here is made to an unconditional guarantee for a loan facility to the builder. The inference in this report is that the ULA provided a financial guarantee to the builder. The ULA would clarify that this guarantee was structured such that it was only exercisable on default by the builder. This structure was agreed on the basis that the facility was to guarantee the completion of construction and not a guarantee for the builder.*

*Lynbrook Estate*

**3.3.350** In December 1993, the Authority selected a consortium as a joint venture partner for the purpose of developing the Lynbrook Estate located at Lyndhurst, south-east of Melbourne. Subsequently, the Authority entered into a joint venture agreement with the consortium in June 1994, with an entitlement for a half share in the project. A condition of the agreement was that the consortium would make an up-front payment to the Authority equivalent to half the value of the land as its equity share in the project.





**3.3.351** The Valuer-General valued the land in January 1994 at \$3 million. However, the consortium did not accept this valuation, and following negotiations, an agreement was reached between the parties under which the consortium was required to contribute \$1.25 million to the Authority plus a bonus of up to \$500 000 if actual sales exceeded projections. The agreement also specified that the Authority was to retain title to the land and be responsible for the management of the project, while both parties to the agreement were to share equally all costs and profits.

**3.3.352** In October 1995, a member of the private sector consortium agreed to relinquish all of its interest as a party to the joint venture, including its appointment as marketing consultant for the project. The Authority agreed to pay a sum of \$150 000 to that member in satisfaction of all expenses and marketing services provided, and agreed to undertake the marketing role for the project.

**3.3.353** The development of the estate commenced in June 1994 and is due for completion in June 1999. Allotments were first released for sale in December 1994, however, up to December 1995, only 44 lots were sold resulting in a deficit of \$284 000 for the joint venture.

**3.3.354** Due to the disappointing level of sales, the budget for the project was reviewed in December 1995 which resulted in a revision of the 1995-96 forecast sales to only 83 lots with an operating deficit of \$215 000. The deficit incurred in the 1994-95 financial year of \$284 000, together with the projected loss of \$215 000 in the 1995-96 financial year, means that this venture is performing well below expectations as compared with the original forecast.

*□ RESPONSE provided by Executive Chairman, Urban Land Authority*

*The summary estate performance indicates an operating deficiency which may be interpreted to suggest that produced lots are being disposed of at a loss. A project of this magnitude has a requirement for substantial "start-up" and "positioning" expenditure. The ULA elected to expense these costs according to its conservative accounting policies rather than have them capitalised. It is still anticipated that all "start-up" costs will be recovered against future sales.*

**Duplication of services**

**3.3.355** The work undertaken by the Authority in some areas such as residential development, urban redevelopment and sale of real estate, is similar in nature to that performed by other government agencies, such as:

- Docklands Authority, which is co-ordinating the development of the docklands area;
- Department of Infrastructure, through its division of Office of Major Projects, which is involved in the residential development and redevelopment of under-utilised government land;



- Department of Education, which is responsible for the disposal of surplus school sites; and
- The Property Group of the Department of Treasury and Finance, which is involved in facilitating the disposal of surplus government assets, including real estate.

**3.3.356** The duplication of services provided by the Authority and the above entities suggests that scope may exist for some rationalisation, with potential for cost savings and more effective use of available expertise.

*□ RESPONSE provided by Executive Chairman, Urban Land Authority*

*This comment is noted and should be useful input to machinery of government changes likely to be considered and through possible rationalisation as a consequence of the establishment of the Department of Infrastructure.*

## REFORM OF VICTORIAN PORTS

**3.3.357** Commercial ports in Victoria are located at Melbourne, Geelong, Portland and Hastings. The port at Melbourne is the most significant port in Victoria and is the nation's largest container port, handling around one-third of the value of Australia's international trade. The other Victorian ports handle significant volumes of bulk products including grains, petroleum and industrial chemicals.

**3.3.358** Separate port authorities have operated for each port except for Hastings, which has been managed by the Port of Melbourne Authority. All Victorian port authorities have provided to exporters and importers a range of port services including channel dredging, harbour control, lease of berths and land for stevedoring, and pilot services. In addition, the port authorities were allocated responsibility for 14 associated ports, utilised mainly for recreational and commercial fishing activities.

**3.3.359** While significant productivity improvements have been made by Victorian ports over the past 5 years, they have not matched the gains achieved internationally. In 1994, the Bureau of Industry Economics found that port charges levied by the Port of Melbourne Authority were high by world standards. Other independent studies commissioned by the Department of Treasury and Finance also indicated that Victorian ports had high cost structures and poor commercial practices.

**3.3.360** Port authority asset holdings at 30 June 1995 totalled \$770 million, with such authorities generating operating profits before abnormal items during the 1994-95 financial year of \$56 million and providing \$20 million to the State in the form of dividends and tax equivalent payments.

**3.3.361** Following extensive consultation with industry, unions and other interested parties, the Government in January 1995 announced its port reform policy. The objective of the reforms was to improve the efficiency and effectiveness of port services in Victoria, thereby enhancing the competitiveness of Victoria and providing an improved return to taxpayers for their investment.



**3.3.362** The key components of the port reform program which was initiated through the *Port Services Act* 1995 involved:

- creation of the Melbourne Port Corporation (MPC), acting as a commercial landlord for the port at Melbourne, with lessees of land and berths being the predominate providers of port infrastructure and services;
- establishment of a separate subsidiary of the MPC, known as Melbourne Port Services Pty Ltd, to provide on a contestable market basis certain port services previously provided by the Port of Melbourne Authority;
- creation of the Victorian Channels Authority (VCA), to manage the channels at the ports at Melbourne, Geelong, Portland and Hastings, to perform the harbour control function within Port Phillip Bay and the ports at Melbourne and Geelong, and to ensure the provision of navigational aids;
- establishment of a port asset divestment program, under the oversight of the reform unit within the Department of Treasury and Finance, comprising:
  - an asset sales program including onshore assets at Geelong and Portland, and sale of the World Trade Centre, which was previously managed by the Port of Melbourne Authority; and
  - a program to transfer certain associated port assets mainly to municipal councils.
- economic regulation of specific port services by the Victorian Regulator-General.

**3.3.363** Since the establishment of the port reform program, the Government has completed the sale of the port-related assets under the management of the Port of Portland Authority and, at the date of preparation of this Report, had commenced action to sell the World Trade Centre and the port-related assets under the management of the Port of Geelong Authority.

**Port of Portland sale**

**3.3.364** The port at Portland is a deep water port servicing western Victoria and south-eastern Australia. The Port of Portland Authority (the Authority) was established in 1949 to regulate and manage the port. The infrastructure of the port mainly includes onshore assets comprising 5 common user berths, one dedicated smelter berth, and channel assets and navigational aids. The port is connected to key regional areas through an extensive network of road and rail services.

**3.3.365** Shipping traffic of the port consists of bulk cargoes including woodchips, grains, alumina ingots, live sheep, petroleum and other chemicals.

**3.3.366** At 30 June 1995, the Authority's asset holdings as disclosed in its balance sheet were valued at \$51 million, with liabilities of \$28 million including borrowings valued at \$26 million.

**3.3.367** When the Government announced its intention to sell the port's onshore assets, it decided that the residual assets consisting of channels and navigational aids would come under the control of the VCA, while the associated ports were to be transferred to municipal councils in the area.

*Sale process*



**3.3.368** The Government determined that in the sale of regional port facilities, sole or predominant users of the berths were to be offered the first right of refusal to purchase these facilities. Any dedicated port facilities not sold in this manner were to be included in a whole-of-port sale offer. Consistent with this decision, in September 1995, Portland Smelter Services Pty Ltd was offered the opportunity to purchase the Authority's dedicated smelter berth.

**3.3.369** Following a decline of the offer by the company, public advertisements were placed nationally and internationally in the print media in early November 1995, inviting expressions of interest for the acquisition of onshore assets on a whole-of-port basis. The Department of Treasury and Finance had previously appointed consultants to act as their advisors, and an independent accounting firm to monitor the tender process and ensure all interested parties were accorded fair treatment and evaluated fairly against the established selection criteria.

**3.3.370** An Information Memorandum was provided to a number of potential bidders who had previously lodged expressions of interest in the acquisition of the Authority's onshore assets. The Information Memorandum stipulated, inter alia, that the successful bidder would be required to reduce port usage charges by 20 per cent in real terms over a 4 year period to ensure that the benefits of privatisation are passed on to port users. In early December 1995, the Department received 8 indicative bids and, following their evaluation, 6 bidders were short-listed and were invited to submit firm bids.

**3.3.371** In December 1995, the Department's advisors valued the port's operating assets in a range of \$23 million to \$31 million, based on the net present value of future cash flows determined using a number of assumptions regarding cost structures, port trade and the anticipated reduction in port charges of 20 per cent.

**3.3.372** In February 1996, following the conduct of due diligence inquiries, the short listed bidders lodged firm bids. Following the evaluation of these bids, in mid-February 1996, the Government announced the sale of the port-related assets under the control of the Port of Portland Authority for \$30 million to a consortium comprising Infratil Australia Limited and Ascot Investments Pty Ltd, effective from 6 March 1996.



*Sale terms*

**3.3.373** Key features of the sale arrangements included:

- the sale of the assets and the business operations of the Authority, excluding operations relating to channel dredging and maintenance, navigational aids and shipping movements, and investments, borrowings, deferred debtors and cash held by the Authority;
- assumption by the consortium of all existing leases and licences;
- requirement for the consortium to enter into a long-term lease with VCA to maintain and manage shipping channels; and
- employment of all existing employees on conditions no less favourable than previous conditions of employment, the honouring of staff entitlements prior to sale, and compliance with all other conditions of a Memorandum of Understanding entered into between the Government and the maritime unions.

*Sale result*

**3.3.374** The sale price of \$30 million was near the upper end of the valuation range previously provided by the Government's advisors. An audit analysis to determine whether a book profit or loss has resulted from the sale of the port assets will be undertaken when the Authority produces its financial statements for the year ended 30 June 1996.

**3.3.375** The sale proceeds were applied by the Government to extinguish the Authority's borrowings of \$26 million. The residual proceeds of \$4 million together with surplus cash realised from debtors of approximately \$1 million are to be held by the Authority to meet costs associated with the sale, the disposal of the residual assets, and liabilities relating to unfunded superannuation.

**3.3.376** The future obligations of the State under the sale arrangement mainly relate to:

- a requirement of the State to comply with any environmental and de-contamination notices issued by the Environmental Protection Authority arising from a port environmental survey conducted prior to the sale; and
- any liability arising from legal action against the Authority for WorkCare claims related to asbestos, and claims arising from the construction of the main port breakwater.

**3.3.377** It is my intention to comment further on the outcome of this sale in the Report to the Parliament on the Government's Statement of Financial Operations in October 1996.

*□ NO RESPONSE provided to the matters raised.*



**SCHEDULE A  
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS**

| <i>Report</i> | <i>Subject</i> | <i>Status at date of preparation of this Report</i> |
|---------------|----------------|-----------------------------------------------------|
|---------------|----------------|-----------------------------------------------------|

|                                             |
|---------------------------------------------|
| <b>MATTERS RESOLVED OR ACTION COMMENCED</b> |
|---------------------------------------------|

**PUBLIC TRANSPORT CORPORATION**

|                                                                                                                 |                                                          |                                                                                                                                                                                                                                                                                                                                                                                                                          |
|-----------------------------------------------------------------------------------------------------------------|----------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p><i>Second Report, 1985-86, pp. 166, 178. Ministerial Portfolios, May 1989, p. 256. May 1990, p. 304.</i></p> | <p>Excessive accumulation of employee leave credits.</p> | <p>At the end of March 1996, more than 1 700 employees had annual leave entitlements of more than 60 days. The Corporation has recently formulated a policy which, subject to operational constraints, requires that employees reduce their excess leave entitlements by 30 per cent by December 1996.</p> <p>Reductions of 4 per cent of excess leave entitlements were achieved between March 1995 and March 1996.</p> |
|-----------------------------------------------------------------------------------------------------------------|----------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

|                                                         |                                                                                                                                                                                                                                |                                                                                                                                                    |
|---------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------|
| <p><i>Ministerial Portfolios, May 1989, p. 238.</i></p> | <p>Internal management reporting and oversight by central agencies of PTC and Roads Corporation financial operations are based on cash data whereas year-end external reporting is based on accrual accounting principles.</p> | <p>Internal management reporting and oversight by central agencies is now undertaken using accrual accounting principles as well as cash data.</p> |
|---------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------|

|                                                            |                                                                                                                                                                                                                                                                                                                                                                                                           |                                                                                                                                                                                                                                                                                                        |
|------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p><i>Ministerial Portfolios, May 1994, pp. 365-75</i></p> | <p>Membership numbers and subsidy costs associated with the Multi-Purpose Taxi Program have expanded substantially, due largely to the absence of clear objectives and the use of loosely-framed eligibility criteria. The Program's operational characteristics render it susceptible to fraudulent activity, with a heavy reliance placed on the honesty and integrity of taxi drivers and members.</p> | <p>Consultants have been appointed for the purpose of writing the specifications for the re-engineering of an operating system for multi-purpose taxis, to eliminate fraud by forgery of vouchers, or misuse of membership cards, and to reduce paperwork through the introduction of smart cards.</p> |
|------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

**URBAN LAND AUTHORITY**

|                                                         |                                                                                                                                                                                                                                                                                                                                    |                                                                                                    |
|---------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------|
| <p><i>Ministerial Portfolios, May 1994, p. 333.</i></p> | <p>To ensure that a joint venture known as <i>The Mews</i> proceeded, the Urban Land Authority substantially accepted responsibility for the financial risks of the project. The overall financial result for the Authority from participation in the project was anticipated to be a marginal net return of around \$100 000.</p> | <p>For further comments on this matter, refer to paragraphs 3.3.345 to 3.3.349 of this Report.</p> |
|---------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------|

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**SCHEDULE A**  
**STATUS OF MATTERS RAISED IN PREVIOUS REPORTS - continued**

| <i>Report</i>                                    | <i>Subject</i>                                                                                                                                                                       | <i>Status at date of preparation of this Report</i>                         |
|--------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------|
| <b>NO ACTION TAKEN</b>                           |                                                                                                                                                                                      |                                                                             |
| <b>PUBLIC TRANSPORT CORPORATION</b>              |                                                                                                                                                                                      |                                                                             |
| <i>Ministerial Portfolios, May 1989, p. 236.</i> | The adequacy and quality of disclosure within the financial reports of the transport authorities is inadequate because financing costs related to centralised debt are not included. | Position unchanged. Finance costs are reported centrally by the Government. |

**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS**

| <i>Entity</i>                                        | <i>Financial year ended</i>        | <i>Reporting to Parliament</i>                       | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|------------------------------------------------------|------------------------------------|------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS</b>                              |                                    |                                                      |                                              |                                        |
| Department of Transport                              | 30 June 1995                       | 31 Oct. <i>Financial Management Act 1994, s.45.</i>  | 30 Oct. 1995                                 | 31 Oct. 1995                           |
| <b>PLANNING AND LOCAL GOVERNMENT</b>                 |                                    |                                                      |                                              |                                        |
| Architects Registration Board of Victoria            | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994, s.46.</i> | 29 Sept. 1995                                | 29 Sept. 1995                          |
| Building Control Commission                          | 30 June 1995                       | " "                                                  | 21 Sept. 1995                                | 22 Sept. 1995                          |
| City of Melbourne Superannuation Fund                | 30 June 1995                       | " "                                                  | 25 Oct. 1995                                 | 30 Oct. 1995 (a)                       |
| Docklands Authority                                  | 30 June 1995                       | " "                                                  | 18 Aug. 1995                                 | 18 Aug. 1995                           |
| Historic Buildings Council                           | 30 June 1995                       | " "                                                  | 21 Sept. 1995                                | 21 Sept. 1995                          |
| Loddon-Campaspe Regional Planning Authority          | 30 Sept. 1995                      | 31 Dec. <i>Financial Management Act 1994, s.46.</i>  | 28 Dec. 1995                                 | 28 Dec. 1995                           |
| Melbourne City Link Authority                        | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994, s.46.</i> | 6 Sept. 1995                                 | 8 Sept. 1995                           |
| Plumbers, Gasfitters and Drainers Registration Board | 30 June 1995                       | " "                                                  | 14 Sept. 1995                                | 19 Sept. 1995                          |
| Upper Yarra Valley and Dandenong Ranges Authority    | Period 1 Oct. 1994 to 30 June 1995 | " "                                                  | 21 Nov. 1995                                 | 1 Dec. 1995 (b)                        |

**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                     | <i>Financial year ended</i>        | <i>Reporting to Parliament</i>                        | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|---------------------------------------------------|------------------------------------|-------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS - continued</b>               |                                    |                                                       |                                              |                                        |
| <b>PLANNING AND LOCAL GOVERNMENT</b>              |                                    |                                                       |                                              |                                        |
| Upper Yarra Valley and Dandenong Ranges Authority | Period 1 Oct. 1994 to 30 June 1995 | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 21 Nov. 1995                                 | 1 Dec. 1995 (b)                        |
| Urban Land Authority                              | 30 June 1995                       | " "                                                   | 19 Sept. 1995                                | 19 Sept. 1995                          |
| <b>ROADS AND PORTS</b>                            |                                    |                                                       |                                              |                                        |
| Marine Board of Victoria                          | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 6 Oct. 1995                                  | 10 Oct. 1995                           |
| Port of Geelong Authority                         | 30 June 1995                       | " "                                                   | 30 Aug. 1995                                 | 22 Sept. 1995 (c)                      |
| Port of Melbourne Authority                       | 30 June 1995                       | " "                                                   | 28 Sept. 1995                                | 29 Sept. 1995                          |
| Port of Portland Authority                        | 30 June 1995                       | " "                                                   | 1 Sept. 1995                                 | 1 Sept. 1995                           |
| Roads Corporation                                 | 30 June 1995                       | " "                                                   | 26 Sept. 1995                                | 26 Sept. 1995                          |
| <b>TRANSPORT</b>                                  |                                    |                                                       |                                              |                                        |
| Public Transport Corporation                      | 30 June 1995                       |                                                       | 29 Aug. 1995                                 | 6 Sept. 1995                           |

(a) Ceased operations on 31 October 1995.

(b) Ceased operations on 30 June 1995.

(c) Qualified audit report issued.



# Part 3.4

## Justice

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### KEY FINDINGS

#### **Sheriff's Office - Uncollected fines**

- Cash collections as a proportion of uncollected fines and costs, declined from 31.5 per cent in 1990-91 to 15.7 per cent in 1994-95.  
*Paras 3.4.12 to 3.4.13*
- Despite productivity measures and amendments to legislation the amount of uncollected fines continued to rise.  
*Paras 3.4.18 to 3.4.19*
- Over the period 1986-87 to 1994-95 total outstanding fines and costs has grown 9 times from \$41.3 million to \$366.6 million.  
*Para. 3.4.18*
- At 30 June 1995, of the \$366.6 million in outstanding fines and costs, a total of \$289.1 million was payable to the State. Of this amount \$85.1 million has been written-off as bad debts and the collection of \$116.9 million is regarded as doubtful.  
*Paras 3.4.21 to 3.4.22*
- Of the total outstanding fines payable to the State, 75 per cent has been outstanding for more than 1 year.  
*Para. 3.4.23*
- In the 6 year period 1 January 1990 to 31 December 1995, a total of 2.2 million warrants had been lodged with the Sheriff's Office of which 1.3 million remains unexecuted.  
*Para. 3.4.24*



**KEY FINDINGS - continued**

**Sheriff's Office - Uncollected fines - continued**

- Bad and doubtful debts provided in respect of debt payable to the state over the last 5 years have grown from \$80.4 million in 1990-91 to \$202 million in 1994-95.  
*Paras 3.4.31 to 3.4.33*
- The Government and the Department of Justice have recently introduced a number of further initiatives to improve the enforcement and collection of fines.  
*Paras 3.4.34 to 3.4.62*
- At 15 March 1996, time-to-pay arrangements totalled \$28.4 million of which \$19.1 million was in arrears.  
*Paras 3.4.64 to 3.4.66*

**Police leave records**

- Approximately 80 per cent of the Office of Chief Commissioner of Police (OCCP) operational budget (\$786 million) and liabilities (\$190 million) is related to employee entitlements.  
*Para. 3.4.75*
- A qualified audit opinion was issued on the 1994-95 financial statements of OCCP, due to discrepancies between manual leave cards, personnel records and the data in the new computerised personnel system.  
*Paras 3.4.82 to 3.4.84*
- OCCP has initiated action to ensure that leave balances are more accurately reflected in the personnel system.  
*Paras 3.4.86 to 3.4.90*



**3.4.1** The Attorney-General, the Minister for Corrections, the Minister for Fair Trading, the Minister for Police and Emergency Services and the Minister for Women's Affairs, have responsibility for operations within the Justice sector. These Ministers have collective responsibility for the Department of Justice.

**3.4.2** Details of the specific ministerial responsibilities for public bodies within the Justice sector are listed in Table 3.4A. These public bodies, together with the Department of Justice, were subject to audit by the Auditor-General during the 1994-95 financial year.

**TABLE 3.4A  
MINISTERIAL RESPONSIBILITIES FOR PUBLIC BODIES WITHIN THE JUSTICE SECTOR**

| <i>Ministerial portfolio</i>         | <i>Entities subject to audit</i>                                                                                                                                                                                                                                                                                                                                                                     |
|--------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Attorney-General</b>              | Estate Agents Guarantee Fund (a)<br>Guardianship and Administration Board<br>Legal Aid Commission of Victoria<br>Legal Aid Commission Staff Superannuation Fund<br>Office of the Director of Public Prosecutions<br>Office of the Public Advocate<br>Solicitors Guarantee Fund<br>State Electoral Office<br>Victorian Financial Institutions Commission<br>Victorian Institute of Forensic Pathology |
| <b>Corrections (b)</b>               | Victorian Prison Industries Commission                                                                                                                                                                                                                                                                                                                                                               |
| <b>Fair Trading (b)(c)</b>           | -                                                                                                                                                                                                                                                                                                                                                                                                    |
| <b>Police and Emergency Services</b> | Country Fire Authority<br>Metropolitan Fire Brigades Board<br>Office of the Chief Commissioner of Police                                                                                                                                                                                                                                                                                             |
| <b>Women's Affairs (b)</b>           | -                                                                                                                                                                                                                                                                                                                                                                                                    |

(a) Previously known as Estate Agent Board.

(b) Minister has responsibility for certain functions of the Department of Justice.

(c) Includes responsibility for Residential Tenancy Fund.

**3.4.3** Comment on matters of significance arising from the audit of entities within the Justice sector is provided below.





**SHERIFF'S OFFICE - UNCOLLECTED FINES**

**ENFORCEMENT MANAGEMENT UNIT**

**Background**

*Objectives of the Enforcement Management Unit*

**3.4.4** The Enforcement Management Unit (EMU) is a unit within the Department of Justice (the Department) and comprises the Sheriff's Office and the Penalties Enforcement by Registration of Infringement Notice (PERIN) Court. The EMU was established in March 1994 to streamline arrangements between the Sheriff's Office and the PERIN Court by developing an integrated process for fines management and enforcement.

**3.4.5** The overall objectives of the EMU are to:

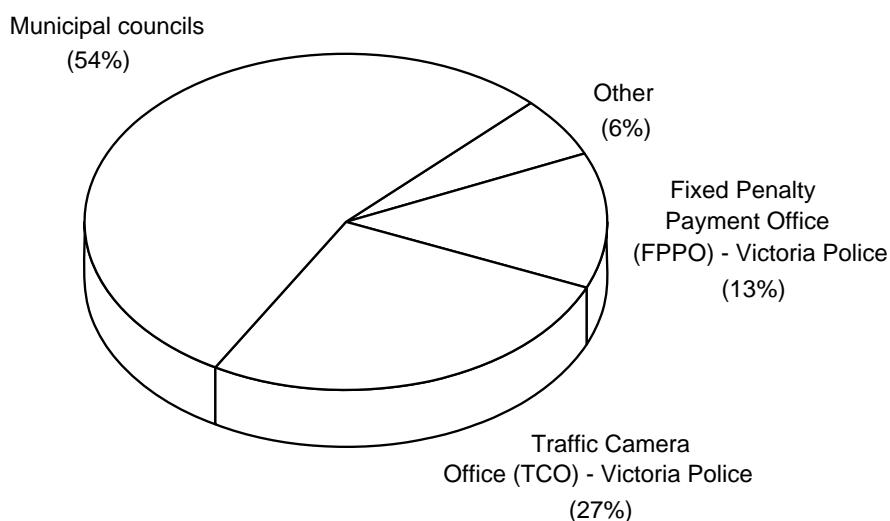
- execute civil and criminal warrants in a timely, effective and fair manner;
- co-operate and liaise with the courts and other law enforcement and associated bodies to ensure that the standard of operations and performance is of the highest level;
- increase the level of fines collected by developing information technology solutions in conjunction with revised business systems and best practice processes of debt management; and
- reduce the amount of outstanding fines.

*Role and responsibilities of the Enforcement Management Unit*

**3.4.6** The EMU is responsible for the administration and enforcement of all unpaid fines and criminal warrants issued to the Sheriff's Office by the PERIN Court and the Magistrates (Open) Court.

**3.4.7** Of the warrants issued by the PERIN and Open Courts, approximately 96 per cent and 35 per cent respectively, relate to traffic-related offences. Warrants issued by the PERIN Court during 1994-95 represented 87 per cent of total warrants issued to the Sheriff's Office. The major clients of the PERIN Court are illustrated in Table 3.4B:

**TABLE 3.4B  
MAJOR CLIENTS OF THE PERIN COURT,  
AT 30 JUNE 1995**



**3.4.8** The EMU is also responsible for the execution of all civil warrants issued by the Supreme, County and Magistrates' Courts and interstate, Commonwealth and international jurisdictions.

**3.4.9** Currently, the EMU has a field force of 160 officers and manages approximately 680 000 criminal and civil orders and warrants each year.

**Level of uncollected fines - current status**

**3.4.10** Statistics maintained by the Department show that of the total number of fines imposed through infringement notices:

- **83 per cent were settled** within the stipulated periods allowed before the matter was referred to court;
- of the matters referred to court, **a further 5 per cent are finalised at the court stage;**
- of the remaining 12 per cent of cases:
  - **4 per cent of the fines are finalised by the Sheriff's Office** by way of either payment, imprisonment or revocation; and
  - **8 per cent remain unpaid.**

**3.4.11** The cumulative impact of the 8 per cent of fines unpaid represents \$366.6 million in total outstanding fines and costs, and is set out in Table 3.4C. In summary, of the total outstanding fines and costs, \$289.1 million relates to uncollected revenue payable to the State, of which \$85.1 million (29.4 per cent) is regarded as uncollectable and a further \$116.9 million (40.5 per cent) is regarded as doubtful.

**TABLE 3.4C**  
**UNCOLLECTED FINES AND COSTS,**  
**AT 30 JUNE 1995**  
(\$million)

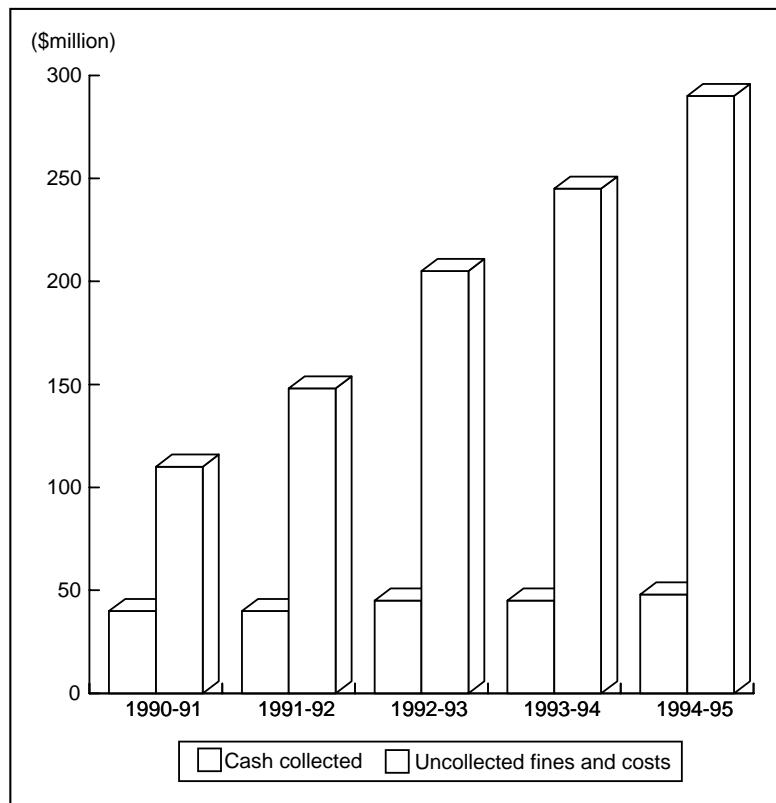
| <i>Description</i>                                     | <i>Payable<br/>to the<br/>State</i> | <i>Payable<br/>to local<br/>government</i> | <i>Total</i> |
|--------------------------------------------------------|-------------------------------------|--------------------------------------------|--------------|
| Court Orders                                           | 33.9                                | (a)                                        | 33.9         |
| Sheriff - warrants                                     | 159.6                               | 77.5                                       | 237.1        |
| Total uncollected fines                                | 193.5                               | 77.5                                       | 271.0        |
| Execution costs (b)                                    | 95.6                                | n/a                                        | 95.6         |
| <b>Total uncollected fines<br/>and execution costs</b> | <b>289.1</b>                        | <b>77.5</b>                                | <b>366.6</b> |
| Provision for doubtful<br>debts                        | (116.9)                             | (50.0)                                     | (166.9)      |
| Bad debt write-off (c)                                 | (85.1)                              | n/a                                        | (85.1)       |
| <b>Balance</b>                                         | <b>87.1</b>                         | <b>27.5</b>                                | <b>114.6</b> |

- (a) This information is not readily available from departmental records.
- (b) Execution costs are attached to all warrants executed by the Sheriff.
- (c) Bad debts were written-off for the first time in 1994-95 with the introduction of accrual accounting.

**3.4.12** Table 3.4D indicates that in the 5 year period 1990-91 to 1994-95, the level of uncollected fines and costs payable to the State (before the write-off of bad debts) has grown from \$117.1 million to \$289.1 million, whereas annual cash collections made by the Sheriff's Office in the same period have increased from \$36.5 million to \$45.5 million. **Cash collections, as a proportion of uncollected fines and costs, have declined from 31.5 per cent in 1990-91 to 15.7 per cent in 1994-95.**

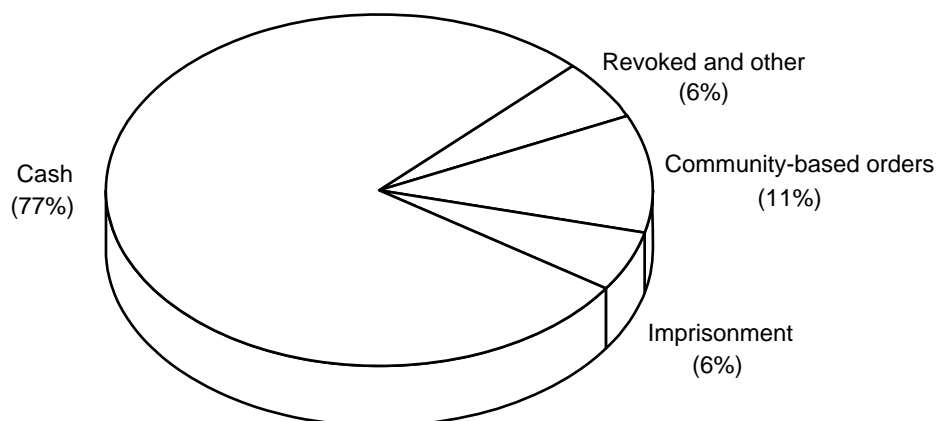
**3.4.13** The percentage decrease in cash collections has been affected by a one-off increase in warrant execution costs in October 1990 from \$11.60 to \$50.00, and an annual CPI increase to the costs applicable to all unpaid fines.

**TABLE 3.4D  
CASH COLLECTIONS AND UNCOLLECTED FINES AND COSTS**



**3.4.14** Settlement of the uncollected fines and costs can be made in the form of cash or by a number of non-cash options, e.g. imprisonment and community-based orders. Table 3.4E illustrates that, **of the total fines settled in 1994-95, 77 per cent and 23 per cent are settled for cash and non-cash, respectively.**

**TABLE 3.4E  
FINES SETTLED BY CASH AND NON-CASH,  
YEAR ENDED 30 JUNE 1995**





**□ RESPONSE** provided by Secretary, Department of Justice

*The trend of the collection figures is acknowledged and has clearly required corrective action. This action commenced part way through 1994-95 with the result that the actual level of cash collections increased from \$42.4 million in 1993-94 to \$45.5 million in 1994-95. In 1995-96, cash collection is expected to amount to some \$51 million, with further increases in subsequent years.*

**Reason for this review**

*Previous report findings made by the Auditor-General*

**3.4.15** Since the establishment of the PERIN Court in 1986-87, audit has commented in several Reports to the Parliament on the level of uncollected fines and costs. In these Reports, audit concluded that several factors had contributed to the substantial increase in the amount of uncollected fines. These were:

- lack of reliability of the database used by the Sheriff's Office to identify the whereabouts of offenders;
- inadequacies in the enforcement options available to the Sheriff such as the power of seizure of personal property and the suspension of motor vehicle registration; and
- the excessive timelag of at least 112 days between the date an offence is committed and the date a warrant is available for execution contributed to the difficulties in locating offenders.

**3.4.16** In response to the Auditor-General's *Report on Ministerial Portfolios* in May 1994, the Department acknowledged the issues raised by audit and the need to substantially improve the situation. In addition, the Department stated that the Government also recognised the importance of the issues raised and that they were being dealt with as a matter of priority through a number of additional initiatives which were in the process of implementation.

*Reform process*

**3.4.17** The Government and the Department have introduced a number of initiatives to reform the enforcement and collection of fines within the EMU. These initiatives include:

- Amendments to legislation providing the Sheriff with the power to seize personal property or business assets of defaulters who refuse to pay;
- Capital funding to enable the development of an integrated computer system and the amalgamation and re-engineering of the administrative processes of the EMU, the Traffic Camera Office and the Fixed Penalty Payments Office business units, into one location;



- Recurrent funding to improve the efficiency of the EMU's operations through a range of productivity improvement initiatives; and
- Introduction by the EMU of a number of in-house productivity improvement initiatives/pilot programs aimed at reducing the level of uncollected fines. These include:
  - address validation/data matching;
  - targeting of debtors; and
  - time to pay arrangements.

*Why the review?*

**3.4.18** Since audit first made comment in 1986-87, outstanding fines have grown 9 times from \$41.3 million to \$366.6 million prior to providing for bad and doubtful debts in 1994-95.

**3.4.19** Despite the in-house productivity initiatives undertaken by the Department and amendments made to legislation in recent years, there has been a continued growth in the level of uncollected fines payable to the State as shown in Table 3.4D. In addition, as indicated in Table 3.4C, **the Department has written-off \$85.1 million in bad debts and provided a further \$116.9 million in doubtful debts in 1994-95.** The main factors which have contributed to this unfavourable situation are:

- inefficient and non-integrated computer systems which failed to produce effective management information systems and reporting facilities; and
- limitations in the powers of the Sheriff in the enforcement and collection of uncollected fines.

**3.4.20** The Government has responded to the needs of the Department by providing additional funding.

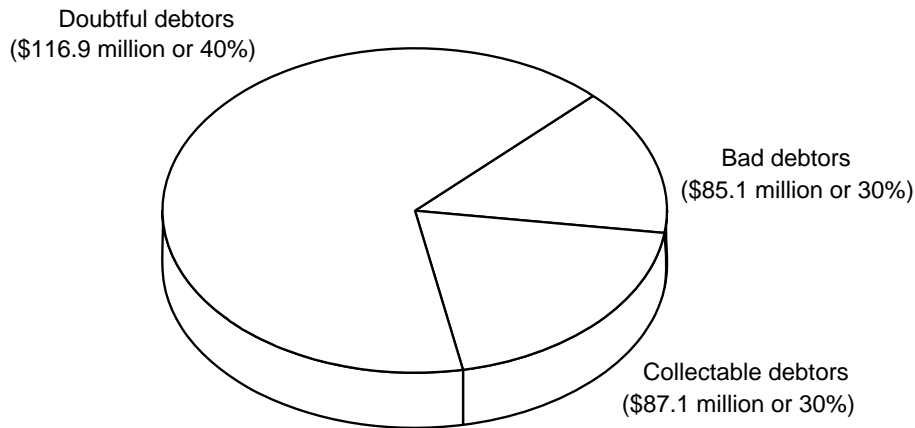
**DOUBTFUL AND UNCOLLECTABLE FINES**

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**3.4.21** As reported in paragraph 3.4.11 of this Report the Department had, at 30 June 1995, a total of \$366.6 million in uncollected government and non-government fines and costs. Of these fines and costs, \$289.1 (79 per cent) are payable to the State.

**3.4.22** Table 3.4F illustrates that of the \$289.1 million of uncollected fines payable to the State, **the Department has written-off \$85.1 million as uncollectable and the collection of \$116.9 million is considered doubtful. This means that only \$87.1 million (30 per cent) of outstanding fines and costs is regarded as collectable.**

**TABLE 3.4F**  
**UNCOLLECTED FINES AND COSTS PAYABLE TO THE STATE,**  
**AT 30 JUNE 1995**  
**(Total uncollected fines and costs: \$289.1 million)**



**Age analysis of uncollected fines**

**3.4.23** Under the current fine enforcement process, the timelag between the date a penalty is imposed and the date a warrant is issued to the Sheriff's Office, through the PERIN and the Open Courts, is a minimum of 112 days and 37 days, respectively. Table 3.4G illustrates that **of the \$193.5 million of uncollected fines payable to the State (excluding warrant execution costs), 75 per cent is more than 1 year old.**

**TABLE 3.4G**  
**AGE ANALYSIS OF UNCOLLECTED**  
**FINES AS AT 30 JUNE 1995**

| <i>Ageing of uncollected fines</i> | <i>Uncollected fines</i> | <i>Total</i>  |
|------------------------------------|--------------------------|---------------|
| (years)                            | (\$m)                    | (%)           |
| 0 - 1                              | 47.4                     | 24.5          |
| 1+ - 2                             | 35.4                     | 18.3          |
| 2+ - 3                             | 30.9                     | 16.0          |
| 3+                                 | 79.8                     | 41.0          |
| <b>Total</b>                       | <b>193.5</b>             | <b>100.00</b> |

**3.4.24** Statistics maintained by the Department show that for the 6 year period 1 January 1990 to 31 December 1995, a total of 2.2 million warrants had been lodged with the Sheriff's Office from the PERIN and Open Courts with **a total of 1.3 million (59 per cent) of warrants remaining unexecuted at 31 December 1995.**

**3.4.25** All warrants, including those written-off as bad debts for accounting purposes are followed-up if a new address is identified for a defaulter. However, no costing exercise has been performed by the EMU to determine the total costs involved in following-up an outstanding debt and assessing the cost-effectiveness of pursuing a defaulter.

**3.4.26 The EMU should:**

- perform a critical analysis of its age debtors report on a regular basis to assess the collectibility of any outstanding fine; and
- undertake a review to determine the total costs involved with the follow-up of fine defaulters to establish the cost-effectiveness of actively pursuing a debt.

**□ RESPONSE** provided by Secretary, Department of Justice

*The necessary "due process" associated with the execution of warrants means that at any time there will always be a substantial number unexecuted, particularly those warrants arising from the PERIN system.*

*However, we acknowledge that better debt management processes are required including an assessment of debt age and debt write-off. These corrective actions include the use of new legislative powers, new integrated computer systems, increased recurrent funding and other actions as outlined in paragraph 3.4.17 above. In addition, there will be an emphasis on recovery of newer debt.*

**Bad debt write-off**

**3.4.27** The introduction of accrual accounting in 1994-95 has necessitated a more critical assessment of the Department's outstanding debtors to be undertaken so that the value attributed to this item in its financial statements is a fair presentation of the debts which may be collected.

**3.4.28** Recognising this need, the Department, with the assistance of an external consultant, developed criteria to enable a consistent approach to be applied to the write-off of bad debts. The criteria, which was applied to all uncollected fines owing to the State and warrant execution costs relating to non-government fines, requires all filed warrants held by the Sheriff for greater than 12 months to be written-off. A filed warrant is one where the defendant had left his/her address and the Sheriff had been unable to find a new address in the ensuing 12 months. The criteria does not apply to non-government fines (e.g. municipal council parking fines).

**3.4.29** It should be noted that the write-off of uncollected fines is for accounting purposes only, as all warrants remain enforceable by law. Therefore, as stated above, if a new address is subsequently identified after the write-off of the debt, the Sheriff will enforce the warrant.

**3.4.30** The application of this criteria to uncollected fines and costs payable to the State has **resulted in a bad debt write-off of \$85.1 million in 1994-95, with a further write-off anticipated in 1995-96 of \$15 million, bringing the bad debt write-off to \$100 million in the last 2 years.**

**Provision for doubtful debts**

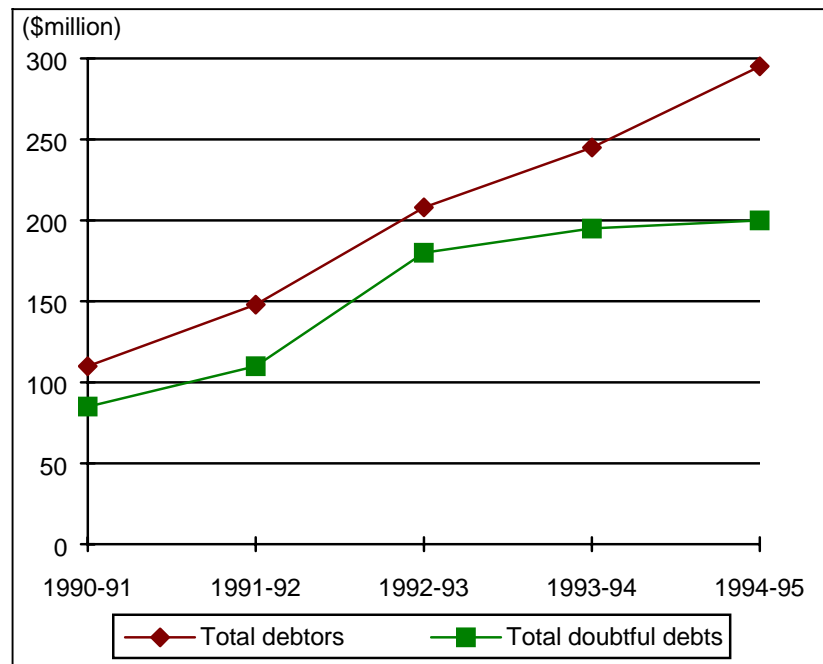
**3.4.31** The provision for doubtful debts is also made for accounting purposes so that the net amount of debtors shown in the Department's financial statements fairly reflects the amount expected to be collected.

**3.4.32** The provision for doubtful debts in respect of outstanding fines and costs is based on collection patterns which are reviewed annually and adjusted for any legislative changes or departmental initiatives.

**3.4.33** As indicated in Table 3.4H, doubtful debts provided in respect of debt payable to the State (prior to the bad debt write-off of \$85.1 million) over the last 5 years:

- have grown from \$80.4 million in 1990-91 to \$202 million in 1994-95; and
- as a proportion of debtors has remained high at approximately 70 per cent.

**TABLE 3.4H  
DEBTORS AND DOUBTFUL DEBTORS**



□ **RESPONSE** by Secretary, Department of Justice

*Given the nature of these debts an extremely high proportion would be categorised as doubtful by a normal commercial or government trading enterprise. This is particularly so because there have already been attempts to collect the debt by other agencies prior to referral to the EMU.*

*Furthermore, over 50 per cent of the warrants on the database lack a current address and over 40 per cent of the uncollected fines are more than 3 years old. It is also inevitable that the pool of doubtful debt will continue to grow as the debt pool ages.*

*We have already written-off substantial unrecoverable sums in 1994-95. We will continue this practice. However, and more significantly, we are improving our debt recovery processes as previously outlined in paragraph 3.4.17.*

## REFORMS

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### Legislative amendments

#### *Amendments in 1994*

**3.4.34** The *Magistrates Court (Amendment) Act* 1994, which was proclaimed on 24 October 1994, provided the Sheriff's Office with new powers relating to the enforcement and collection of unpaid fines. The relevant amendments to the Act, which can be applied retrospectively, are as follows:

- the Sheriff can now seize personal property or business assets of defaulters; and
- directors of bodies corporate can now be jointly and severally liable for the payment of the fine imposed on the body corporate.

**3.4.35** Statistics maintained by the Department showed that for the period March 1995 to March 1996, a total of \$221 000 was received from the sale of seized property relating to corporate and individual warrants valued at \$1.2 million. In addition, a further \$226 000 was received in respect of these warrants by defaulters paying their outstanding fines in full or entering into a time to pay arrangement.

**3.4.36** However, given the lack of information maintained by the Department, audit was unable to fully assess the impact of these legislative amendments on the level of outstanding fines and costs or the extent of fines paid by offenders during the stipulated periods allowed.

#### *Proposed amendments*

**3.4.37** The EMU has recognised that there is a need for further legislative change to address:

- inconsistencies in legislation relating to the PERIN and the Open Courts; and
- inadequate and insufficient enforcement powers given to the Sheriff.

**3.4.38** A proposal was recently prepared by the EMU listing all issues requiring legislative change to facilitate the more efficient and effective operation of the unit. Audit has been advised that no legislative amendments are likely to be presented to Parliament in the near future, mainly due to other government priorities.

**3.4.39** The Department has since taken action to review the current and proposed legislative framework, including accessing of public databases, as part of a project to integrate and amalgamate the systems and administrative processes of the Traffic Camera Office (TCO), Fixed Penalty Payment Office (FPPO) and the EMU. This is discussed in detail in paragraphs 3.4.43 to 3.4.47.

**3.4.40** **Given that it will be late 1997 before this project is completed, audit recommends that those legislative changes which are not dependant on the outcome of the project but could assist the EMU in reducing or preventing the increase in the level of uncollected fines and costs should be given immediate consideration.**



*□ RESPONSE provided by Secretary, Department of Justice*

*It is not correct that no legislative amendments are likely to be presented to Parliament in the near future. Any proposals for legislative change put forward by the EMU will be considered and will proceed if assessed as improving the recovery system.*

**Funding of reforms**

**3.4.41** In July 1994, the EMU via the Department of Justice presented a proposal for additional funding to the Department of Treasury and Finance (DOTF) to enable the development and introduction of various reforms and initiatives relating to the enforcement and collection of fines. This proposal was not approved. The Department was later advised by DOTF that a detailed and comprehensive business proposal would be required if further funding was to be considered.

**3.4.42** The EMU, in conjunction with an external consultant, developed business proposals for additional capital and recurrent funding which it presented to the DOTF in September 1995. The proposal was approved in December 1995 almost 18 months since the original request. **The delay in obtaining the required funding has possibly been a contributing factor to the increase in the level of total outstanding debt in that period.**

*Capital funding - Integration and amalgamation of the TCO/FPPO/EMU*

**3.4.43** As referred to paragraph 3.4.39, there are 3 main business units which provide fine collection services within Government, namely, the TCO and FPPO business units within Victoria Police, and the EMU business unit within the Department of Justice.

**3.4.44** These business units are functioning separately despite the common administrative processes and business elements of their operations. Specifically, each unit operates on different computer systems, with different payment methods, different client service capabilities and at different locations. The Department has recognised that this has contributed to a lack of a global management approach to the fines portfolio.

**3.4.45** The EMU obtained capital funding of \$7 million of which \$2 million will be expended in 1995-96 and \$5 million in 1996-97 to bring together the operations of the 3 business units by the:

- development of an integrated computer system;
- amalgamation and re-engineering of the administrative processes to one location;
- outsourcing of the operation and management of the amalgamated administrative processes; and
- joint development of products and services such as the integrated computer system, which will be marketed nationally and internationally.



**3.4.46** The project, undertaken jointly by the Department and Victoria Police, is known as the TCO/EMU business project. A Project Director was appointed in December 1995 who, in conjunction with the Department's Project Executive Committee, is responsible for the overall management of the project outlined above, including the tender process.

**3.4.47** At the date of preparation of this Report, the tender process has commenced. Evaluation of the tender submissions will facilitate the decision as to either outsource or retain in-house all appropriate functions of the TCO, FPPO and the EMU. The target date for finalising all contractual arrangements is 30 September 1996 and it is anticipated that the project will be completed by 1997.

*Recurrent funding*

**3.4.48** In addition to the capital funding, the Department also requested \$4.7 million in annual recurrent funding to improve the efficiency of the EMU's operations and increase revenue generation through a range of productivity improvement initiatives.

**3.4.49** The DOTF has approved an appropriation of \$1.6 million a year to commence in 1996-97. In addition to the annual appropriation, the Department and DOTF have agreed to enter into a Revenue Retention agreement to commence on 1 July 1996 for a maximum period of 2 years, as a supplement to the annual recurrent funding provided to the Department.

**3.4.50** The amount of revenue to be retained by the Department will be based on the amount of filing fees collected in 1996-97. A filing fee, currently \$30.50, is charged to non-government agencies when such agencies lodge an infringement at the PERIN Court.

**3.4.51** The Department's business proposal to the DOTF stated that the additional recurrent funding will be used for the following purposes:

- encouraging earlier payment of fines by increasing payment options;
- promoting awareness of the Sheriff's powers through a community education program to encourage payment of fines;
- utilising consumer databases (e.g. electronic white pages) to improve accuracy of addresses of fine defaulters;
- outsourcing warrant execution and fines collection where it is considered to be more efficient;
- reviewing legislation impacting on the enforcement of fine collection and making appropriate amendments;
- restructuring the administrative and field operations of the EMU to provide additional efficiencies; and
- increasing and improving reporting to clients including results and achievements.

*Anticipated benefits to be derived from the additional funding*

**3.4.52** The Department's business proposal also outlines the anticipated benefits which include:

- recurrent savings of \$500 000 effective from 1997-98;
- an increase in cash collections by \$2.25 million a year effective from 1997-98 through the ability of the integrated system to electronically search a range of government and public databases resulting in improved data quality;
- a further increase in cash collections of \$4.5 million in 1995-96 resulting from data quality reviews, better targeting of particular classes of defaulters and the effective management of time to pay arrangements;
- protection of 1994-95 cash collection levels of about \$150 million a year (including EMU, \$45.4 million; TCO, \$52.7 million; and FPPO, \$48.9 million);
- substantial improvements in service delivery to the community;
- maximising the opportunities for commercial benefits to the State by the development and exploitation of intellectual property produced or enhanced through the project; and
- reducing the pool of outstanding fines.

**3.4.53** The EMU's business proposal for funding included cash collection projections of \$52 million in 1995-96 and \$60 million in 1996-97. However, as a result of delays in obtaining funding, the projections were subsequently revised to \$45.4 million in 1995-96 and \$46.8 million in 1996-97.

*Conclusion*

**3.4.54** **The development of an integrated computer system and the re-engineering and amalgamation of the common administrative processes of the EMU, TCO and FPPO is crucial to the improved effectiveness of the EMU's operations and overall objective of reducing the substantial level of uncollected fines and costs. It is, therefore, imperative that the implementation plan, when developed, be closely monitored to ensure that any unnecessary delays are avoided.**

*□ RESPONSE by Secretary, Department of Justice*

*By its very nature the collection of these debts has always been much more difficult than normal commercial debt. However, the Department has recognised the need to further improve collection performance and has acted through the initiatives outlined in paragraph 3.4.17. We believe that these initiatives will generate significant improvements over coming years.*



## In-house productivity improvement initiatives

### *Address validation*

**3.4.55** At 30 June 1995, there were 1.3 million warrants on the Sheriff's Office database known as "Recovery Enforcement and Execution in Victoria by Employees of the Sheriff" (REEVES), of which 54 per cent had been filed "left address".

**3.4.56** In August 1995, the Department undertook a data quality review project which involved:

- contracting of private sector consultants to provide data matching and address verification techniques to the EMU's "filed" warrant base; and
- a direct debtor contact campaign in respect of matched warrants.

**3.4.57** The objectives of this project included the determination of the match rate that can be generated by using Vic Roads registration database and establishing the potential level of revenue from the filed warrants.

**3.4.58** The contractor matched records from REEVES with VicRoads registration database to confirm addresses or provide a revised address. Consumer databases, such as Telecom's White Pages, the Electoral Roll and Australia Post were also used to provide phone numbers or confirm the revised addresses.

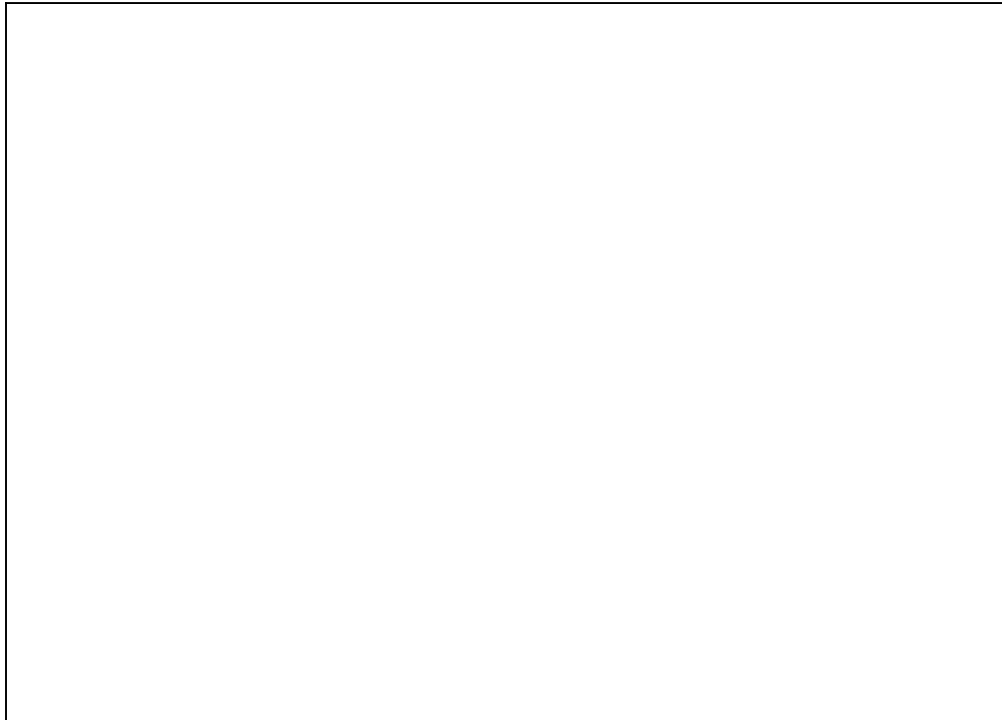
**3.4.59** The matching process between REEVES and VicRoads involved a total of 322 000 filed warrants. It resulted in a revised address being established for 12 per cent of those warrants with a value of \$6.4 million.

**3.4.60** The direct debtor contact campaign, in respect of those warrants where a new address had been identified, is being undertaken by a newly established debt recovery section utilising commercial debt collection software. At 15 March 1996, a total of \$2.6 million (including \$1 million in time to pay arrangements) or 40.6 per cent of the \$6.4 million debt had been actioned and/or finalised.

### *Targeting of defaulters*

**3.4.61** The Sheriff's Office field operations are divided into 3 regions within Victoria: Eastern, Central and Western. Each of the regions include 3 divisions comprising a metropolitan area and 2 country areas. In achieving the determined revenue targets set for each region and the EMU overall, different methods of warrant execution are adopted. These include:

- *Country Blitz and Saturation Execution* - A country town or postcode is identified for action, infringement details are mailed out then field execution is conducted saturating the targeted areas for a short period of time;
- *Time to Pay Defaulters* - When an defendant defaults on a time to pay arrangement and fails to respond to mail and phone calls, the warrant is directed to the field for execution;
- *Road Blocks* - Field staff participate with Victoria Police to check for outstanding warrants by reference to vehicle registration and driver's licence details;



*Special operations activities on parking fine evaders held within the City of Stonnington by the Sherriff's Office and the Victorian Police.*

- *Publicity Campaigns* - Use of media advertising to motivate fine defaulters to initiate action that will result in finalisation of their fines; and
- *Client Special Activities* - Warrants for infringements that originated within a client's (municipal council) boundaries are identified and targeted. To date, the special operations have been performed with the following municipal councils:
  - Melbourne;
  - Bendigo;
  - Wodonga;
  - Shepparton;
  - Stonnington.

**3.4.62** These client special activities have resulted in additional cash collections of \$1.1 million and a further \$790 000 in time to pay arrangements over the past 12 months.

.....

### *Amnesty provided to fine defaulters*

**3.4.63** During the period 14 September 1994 to 24 October 1994, the Sheriff's Office introduced an amnesty in the enforcement of warrants. This amnesty provided fine defaulters with the opportunity to finalise their outstanding warrants prior to changes in legislation which allowed the seizure of property coming into effect. The Sheriff did not execute any warrants during the amnesty period with the effect that the impact on cash collections during that period was minimal.

### *Time to pay arrangements*

**3.4.64** An outcome of the amnesty referred to above was an increase in the value of warrants subject to time to pay (TTP) arrangements from \$3 million at October 1994 to \$15 million at December 1994.

**3.4.65** Given the substantial growth in TTPs, the EMU recognised the need for a monitoring process to be implemented to follow-up on defaulters of these arrangements. However, this process was not implemented until September 1995 when TTPs had totalled \$25 million. **At 15 March 1996, TTP arrangements totalled \$28.4 million representing 31 565 debtors of which \$19.1 million (67 per cent) was in arrears.**

**3.4.66** The Debt Recovery Section is also pursuing fine defaulters for whom a new address was identified through the Data Quality Review project (refer to paragraphs 3.4.55 to 3.4.60). Where these fine defaulters enter into TTP arrangements, the arrangements are recorded on commercial debt recovery software. The use of this software has, through the use of its automated diary and report writer facilities, provided prompt follow-up and a reduction of defaulters in arrears. Such a facility, however, is not currently available on the Sheriff's computer system (REEVES), therefore, targeting and prompt follow-up of defaulters on TTP arrangements is not possible.

### *Gippsland Project*

**3.4.67** The Magistrates (Open) Court orders and its database (Courtlink) currently operates separately to the PERIN Court and the Sheriff's Office. The EMU, however, has recognised the potential to increase revenue and reduce costs through the development of procedures to allow:

- the sharing of databases;
- court staff to process payments and handle general execution inquiries; and
- Sheriff's Office field staff to spend more time in the field executing warrants.

**3.4.68** During the period April to December 1995, the EMU in conjunction with Magistrate Courts in the Gippsland region undertook a pilot program which involved the processes outlined above. The EMU is currently in the process of analysing the results of the pilot program and, if favourable, anticipates it will provide an appropriate operational alternative for the future.

Conclusion

**3.4.69** The productivity improvement initiatives detailed above indicate that improvements in the method of warrant execution are being actively pursued and the EMU has already benefited through an increased level of collections and actioned and/or finalised warrants. The EMU is to be commended for such initiatives but particular attention will need to be devoted to the monitoring and prompt follow-up of the defaulters on time to pay arrangements as delays would adversely affect the effectiveness of these arrangements.

Access to databases

**3.4.70** As stated at the introduction of this section of the Report, the EMU was established to improve the effectiveness of fine collection. To achieve this objective a number of strategies have been adopted, one of which is improving the accuracy of contact addresses, which require access to other government databases.

**3.4.71** To date, VicRoads (licence and registration databases) is the principle database used to locate fine defaulters, but, of the warrants matched and issued to the field for execution, approximately 60 per cent are returned unexecuted. The EMU is of the view that by searching and matching the PERIN Court and Sheriff's Office (REEVES) databases against other government databases more accurate addresses can be obtained.

**3.4.72** Due to privacy considerations in the *Privacy Act* 1988 the EMU is unclear as to the extent of its power to interrogate databases of public utilities such as the former SEC, Gas and Fuel, water boards and Telstra, to validate the addresses of fine defaulters as shown on the Sheriff's Office database (REEVES).

**3.4.73** Legal advice is being sought by the EMU from the Victorian Government Solicitor (VGS) as part of the project to integrate and amalgamate the systems and common business elements of the TCO, FPPO and the EMU. Specifically, the VGS will be requested to provide legal advice:

- to ensure proper account is taken of privacy issues likely to arise from the planned operation of the services partnership;
- on legislative issues including:
  - the likely effectiveness of the current and planned legislative framework under which the TCO and EMU operate;
  - how legislation would need to be changed in order for the TCO and EMU to achieve their objectives through the services partnership with the prime contractor; and
  - what legislative changes would be required to optimise access to databases to improve debt recovery rates by the EMU.

**3.4.74** Failure to gain access to other public databases will inhibit the effectiveness of the new integrated computer system, therefore, it is imperative that timely action be taken to ensure this issue is resolved.

## POLICE LEAVE RECORDS

### Background

**3.4.75** The Office of Chief Commissioner of Police (OCCP) employs 12 300 staff consisting of 10 500 police officers and 1 800 civilians. Approximately 80 per cent of the OCCP's operational budget (\$786 million) and liabilities (\$190 million) is related to employee entitlements.

**3.4.76** Over the past few years, the OCCP has moved from a multiplicity of personnel systems to a fully integrated, on-line personnel/payroll system (HR system). The system, which was fully implemented in 1994-95, provides for the management of:

- personal details of all staff;
- training and development;
- recruitment and placement;
- leave management; and
- payroll.

**3.4.77** The OCCP has a decentralised structure with 90 budget and district centres. Under this structure, the head of each centre has operational and administrative responsibility, including responsibility for leave management. Each centre has its own personnel officer responsible for the processing of leave data and the continuous updating of the HR system.

### Employee entitlements

**3.4.78** The OCCP's 1993-94 financial statements were prepared on a cash basis with the liability for employee entitlements appended by way of supplementary information. OCCP utilised the HR system in calculating the liability for annual leave but adopted a manual approach to calculate the long service leave liability as it found the relevant data in the HR system to be totally unreliable.

**3.4.79** Audit testing of the annual leave liability revealed that the manual records for annual leave could not be reconciled to the HR system in 50 per cent of cases. Factors that contributed to this situation were:

- system irregularities which had distorted the conversion of balances brought forward;
- delays in the recording of leave on the HR system by budget and district staff; and
- incorrect recording of leave transactions on the HR system due to initial training not focusing on accrual accounting implications.

**3.4.80** In view of those deficiencies audit advised the OCCP that, with the change to accrual accounting due in 1994-95, corrective action was required.

**3.4.81** In response, the OCCP undertook a validation exercise which required all HR system leave data to be updated. All staff and centre heads were, by March 1995, required to provide certification that the leave data was correct.

### *Audit qualification*



**3.4.82** The 1994-95 financial statements were, for the first time, prepared on a full accrual basis. The quantum of annual and long service leave entitlements, therefore, had a material impact on both the operating result reported in the Operating Statement and leave liabilities reported in the Balance Sheet.

**3.4.83** Audit testing of a sample of annual and long service leave records again revealed significant discrepancies between manual leave cards, personnel records and the data in the HR system. Discrepancies were found in:

- 69 per cent of annual leave records sampled; and
- 29 per cent of long service leave records.

**3.4.84** Consequently, a qualified audit opinion was issued on the 1994-95 financial statements as audit could not adequately verify the liability for employee entitlements of \$189.9 million. Management also could not provide an assurance as to the accuracy of the OCCP's employee entitlements liability with the Chief Commissioner of Police qualifying his certification to the 1994-95 financial statements stating that he was unable "*to verify the liability for employee entitlements*".

*Causes of discrepancies*

**3.4.85** Audit testing identified a number of causes of the discrepancies, some of which were similar to the previous year. The main causes identified by audit were:

- the validation process was not completed within the OCCP timeframe of March 1995, with some centres not completing the process until after 30 June 1995;
- a one-for-one check of adjustments to the HR system was not performed with the result that incorrect conversion and input errors could not be detected;
- although the system automatically updates leave entitlements, in many cases the personnel officers in the centres used an over-ride facility resulting in duplication of entitlements for the 6 month period to June 1995;
- a failure by centre heads to accurately validate the *reasonableness* of employees' entitlements;
- a lack of adequate training, particularly at the district centres, of key personnel responsible for maintaining the HR system; and
- an effective quality assurance program was not undertaken by the central personnel department so that corrective action could be taken on a timely basis.

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*Actions initiated by the OCCP*

**3.4.86** As a consequence of the qualification to the 1994-95 financial statements, the OCCP has recently incorporated responsibility for leave recording into the individual performance plans of each personnel officer and centre head in order to reinforce personal responsibility for system data.

**3.4.87** In addition, the OCCP established a project team whose brief was to ensure that each officer's leave balance was accurately reflected in the HR system. This project involves the following procedures:

- establishing and implementing standards for leave recording and processing for all district/budget centres;
- further training of all personnel staff;
- certification by all centre heads of the accuracy of the data for all staff after completion of a one-for-one check from the manual records to the HR system;
- HR system enhanced to enable each staff member to verify their leave balances by the inclusion of this data on their fortnightly pay slip; and
- ongoing quality assurance assessment by the central personnel department, including exception reporting, random sampling and analysis.

**3.4.88** The initial quality assurance assessment, undertaken by the personnel department in November 1995, highlighted continuing significant error rates in some centres, despite the data being certified as complete and accurate. Analysis indicated human errors, rather than system errors, as the major cause for data inaccuracy, suggesting that the certification process by centre heads was ineffective and that further effort and training will need to be placed on processing issues.

**3.4.89** A one-for-one check of HR system data to manual records was undertaken for all employees in February 1996. The centre heads then provided written certification that the records for all staff members were correct.

**3.4.90** Outside consultants were employed in March 1996 to assist with the quality assurance program, thereby strengthening the program and providing OCCP with independent advice as to the integrity of the data on the system. In addition, the OCCP's internal audit department has commenced a detailed analysis of the HR system and its surrounding control environment with a view to:

- documenting the system including controls and risks;
- analysing sufficiency of controls; and
- recommending actions to rectify any shortcomings.

**Conclusion**

**3.4.91** Significant costs have been incurred to date in attempting to establish reliable employee entitlements records in the OCCP. The outcome of the various measures referred to above will be reviewed by audit when conducting the audit of the 1995-96 financial statements of the OCCP. Hopefully, the various corrective measures will produce information that is complete, accurate and reliable, thereby obviating the need for a further qualification of the financial statements of the OCCP.

*□ RESPONSE provided by Acting Chief Commissioner, Victoria Police*

*I am concerned that the Report remains negative in its approach to the matters of leave management and reporting in Victoria Police. While the contextual comments are reasonably accurate, little emphasis has been placed on the considerable advances made by Victoria Police in the last 3 years, the ongoing program of improvement initiatives in place or the current independent sampling processes occurring, which will, in fact, test the validity of your comments. Indeed, Victoria Police cannot provide a definite response to comments outlined in the Report until after the external contractors complete their audit.*



SCHEDULE A  
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS

| Report | Subject | Status at date of preparation of this Report |
|--------|---------|----------------------------------------------|
|--------|---------|----------------------------------------------|

|                                             |
|---------------------------------------------|
| <b>MATTERS RESOLVED OR ACTION COMMENCED</b> |
|---------------------------------------------|

**DEPARTMENT OF JUSTICE**

**Crimes Compensation Tribunal**

|                                                             |                                                                                                                                                                                                                                            |                                                                                                                                                                                                                                                                                                                                                                                                                    |
|-------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p><i>Ministerial Portfolios, May 1995, p. 148.</i></p>     | <p>A business plan should be developed to reflect the mission, strategic and operational goals of the Crimes Compensation Tribunal. Performance indicators and targets should also be developed to monitor the Tribunal's performance.</p> | <p>The administrative business plan of the Magistrates' Court includes the Tribunal in its scope. In addition, performance indicators specific to the Tribunal will be included in the 1996-97 business plan of the Magistrates' Court, which is currently being prepared.</p>                                                                                                                                     |
| <p><i>Ministerial Portfolios, May 1995, p. 149.</i></p>     | <p>The <i>Crimes Compensation Tribunal - Magistrates' Handbook</i> needs to be revised and updated annually.</p>                                                                                                                           | <p>A <i>Crimes Compensation Tribunal Handbook</i> was published in November 1995, however, there is no provision for the Handbook to be updated annually. This Handbook has replaced the <i>Magistrates' Handbook</i>.</p>                                                                                                                                                                                         |
| <p><i>Ministerial Portfolios, May 1995, pp. 149-50.</i></p> | <p>All data extracted from the Tribunal's information system should be complete, accurate and analysed to assist in decision-making and the provision of forward projections.</p>                                                          | <p>Enhancements to the Tribunal's information computer system currently being undertaken will enable the introduction of a computerised award system and the collection of more complete and accurate data. These enhancements, training of staff and the development of a user manual will be completed in May 1996. Procedural checks and balances were also introduced to improve financial accountability.</p> |
| <p><i>Ministerial Portfolios, May 1995, pp. 150-52.</i></p> | <p>Broadening the definition of "victim" and "injury" has led to an increase in the type and number of claims made.</p>                                                                                                                    | <p>A working party is working on issues raised and will make recommendations in its final report to the Attorney-General.</p>                                                                                                                                                                                                                                                                                      |
| <p><i>Ministerial Portfolios, May 1995, pp. 153-4.</i></p>  | <p>Appropriateness of the one year time limit should be considered and guidelines be included in the <i>Magistrates' Handbook</i> for granting time extensions.</p>                                                                        | <p>A paper prepared in 1995, entitled <i>Time Limits and You</i> has been included in the <i>Crimes Compensation Tribunal Handbook</i>. This paper examines the 2 most frequently considered time limits imposed by the <i>Crimes Injuries Compensation Act 1983</i> and is to be used as a guide.</p>                                                                                                             |
| <p><i>Ministerial Portfolios, May 1995, p. 154.</i></p>     | <p>The minimum compensation amount payable to a victim has not been reviewed for over 10 years. Given the substantial associated costs with awards involving minor injuries, this should be reviewed for appropriateness.</p>              | <p>The abovementioned working party has this matter under consideration.</p>                                                                                                                                                                                                                                                                                                                                       |
| <p><i>Ministerial Portfolios, May 1995, pp. 155-57.</i></p> | <p>Consideration needs to be given to the development of a formal scale of fees for legal, medical and psychological services.</p>                                                                                                         | <p>The Tribunal has developed an informal (advisory) scale which is included in the <i>Crimes Compensation Tribunal Handbook</i>. The abovementioned working party will consider and report on the matters raised by audit.</p>                                                                                                                                                                                    |

**SCHEDULE A**  
**STATUS OF MATTERS RAISED IN PREVIOUS REPORTS - continued**

| Report | Subject | Status at date of preparation of this Report |
|--------|---------|----------------------------------------------|
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**MATTERS RESOLVED OR ACTION COMMENCED - continued**

**DEPARTMENT OF JUSTICE - continued**

**Crimes Compensation Tribunal - continued**

|                                                         |                                                                                                                                                                                               |                                                                                                                                                                                                                                                                                                                                                                                                                                              |
|---------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p><i>Ministerial Portfolios, May 1995, p. 157.</i></p> | <p>Given the substantial amounts of compensation likely to be paid, the Government should consider whether the Tribunal should be assisted by legal counsel where it is deemed necessary.</p> | <p>Legal counsel has been used to assist in the hearing of a small number of claims. The appropriateness for the use of legal counsel is a decision for the Supervising Magistrate. From 1 January 1996, the Victorian Government Solicitor's Office can be called upon to defend the Tribunal's decision in any appeal to the Administrative Appeals Tribunal. The abovementioned working party will address this matter in its report.</p> |
|---------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

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|------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------|
| <p><i>Ministerial Portfolios, May 1995, pp. 157-8.</i></p> | <p>Consideration should be given to performing a review to determine whether work-related claims should also be dealt with under the Criminal Injuries Compensation Act.</p> | <p>Recommendations are awaited from the abovementioned working party on this matter.</p> |
|------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------|

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|-------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------|
| <p><i>Ministerial Portfolios, May 1995, pp. 158-59.</i></p> | <p>No checks are made to determine whether recipients have received, or are entitled to receive, awards from other compensating bodies.</p> | <p>Random checks will be instituted, and the procedure for such checks to prevent double dipping is currently being finalised.</p> |
|-------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------|

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| <p><i>Ministerial Portfolios, May 1995, p. 159.</i></p> | <p>The Tribunal and the Director of Public Prosecutions (DPP) has not developed procedures to recover moneys from convicted offenders. Therefore, the potential for the Consolidated Fund to recover moneys from these offenders has not been realised.</p> | <p>The DPP has complete discretion to determine whether proceedings against a convicted offender are instituted. However, the working party is currently considering alternative methods of seeking an order of the court to direct an offender to refund the Tribunal part or all of the compensation paid or payable to a victim.</p> |
|---------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

**SOLICITORS' GUARANTEE FUND**

|                                                         |                                                                                                                                                                                                                      |                                                                                                                                                                                                                                                                                                                                                                                                                |
|---------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p><i>Ministerial Portfolios, May 1995, p. 162.</i></p> | <p>The Attorney-General has recently released a discussion paper canvassing the transfer of the Solicitors' Guarantee Fund to the Legal Practices Board. A working party is currently considering this proposal.</p> | <p>The Attorney-General, in December 1995, released Draft Proposals for a bill to improve the regulation of legal practice and repeal the <i>Legal Profession Practice Act 1958</i> and amend the <i>Partnership Act 1958</i>. These proposals were published for the purpose of obtaining public comment and detail the proposed transfer of the Solicitors' Guarantee Fund to the Legal Practices Board.</p> |
|---------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

SCHEDULE A  
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS - *continued*

| <i>Report</i>                                                  | <i>Subject</i>                                                                                                                                                                          | <i>Status at date of preparation of this Report</i>                                                                                                                                                                                                                                                                                                                    |
|----------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>MATTERS RESOLVED OR ACTION COMMENCED - <i>continued</i></b> |                                                                                                                                                                                         |                                                                                                                                                                                                                                                                                                                                                                        |
| <b>SOLICITORS' GUARANTEE FUND - <i>continued</i></b>           |                                                                                                                                                                                         |                                                                                                                                                                                                                                                                                                                                                                        |
| <i>Ministerial Portfolios, May 1995, p. 162.</i>               | The Fund's financial position revealed a significant deterioration in the period June 1989 to June 1994 from net assets of \$21.2 million to a net liability of \$9.2 million.          | The 1994-95 annual report of the Fund discloses a further deterioration of its financial position to a net liability of \$32.2 million. This was caused by increased claims expenses against the Fund from \$16.6 million in 1993-94 to \$31.4 million in 1994-95.                                                                                                     |
| <i>Ministerial Portfolios, May 1995, p. 164.</i>               | The Fund needs to ensure that appropriate systems and methodologies are developed and implemented in order that the Fund's financial position can be properly determined in the future. | Parliament passed an amendment to the <i>Legal Profession Practice Act 1958</i> whereby the Attorney-General can now require practising solicitors to pay a fee not exceeding \$1 500 to the Fund. In addition, this amendment also restricted the claims to be made against the Fund to only those in connection with direct mortgage practices.                      |
|                                                                | The consultants appointed by the Department of Justice recommended the inclusion of claims incurred, but not reported, in the provision for claims.                                     | The Fund appointed an actuary in 1995 to review the outstanding claims liability to ascertain its true financial position and set down a methodology for the recording of the provision for claims in the financial statements. The actuary developed a methodology for the calculation of claims incurred but not reported for inclusion in the provision for claims. |
|                                                                |                                                                                                                                                                                         | This was not included as part of the provision for claims in the Fund's 1994-95 financial statements. Consequently, a qualified audit opinion was issued on the Fund's 1994-95 financial statements on the basis that provision for claims was understated by \$14 million.                                                                                            |

**SCHEDULE B  
COMPLETED/INCOMPLETE AUDITS**

| <i>Entity</i>                                     | <i>Financial<br/>year<br/>ended</i> | <i>Reporting to Parliament</i>                              | <i>Financial<br/>statements<br/>signed by<br/>entity</i> | <i>Auditor-<br/>General's<br/>report<br/>signed</i> |
|---------------------------------------------------|-------------------------------------|-------------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------------|
| <b>COMPLETED AUDITS</b>                           |                                     |                                                             |                                                          |                                                     |
| Department of Justice                             | 30 June<br>1995                     | 31 Oct. <i>Financial<br/>Management Act 1994,</i><br>s.45.  | 23 Oct.<br>1995                                          | 30 Oct.<br>1995                                     |
| <b>ATTORNEY-GENERAL</b>                           |                                     |                                                             |                                                          |                                                     |
| Estate Agents Board                               | 31 Jan.<br>1995                     | 30 Sept. <i>Financial<br/>Management Act 1994,</i><br>s.46. | 14 Sept.<br>1995                                         | 27 Sept.<br>1995                                    |
| Estate Agents Guarantee<br>Fund                   | 30 June<br>1995                     | " "                                                         | 2 Oct.<br>1995                                           | 2 Oct.<br>1995                                      |
| Guardianship and<br>Administration Board          | 30 June<br>1995                     | " "                                                         | 4 Oct.<br>1995                                           | 9 Oct.<br>1995                                      |
| Legal Aid Commission of<br>Victoria               | 30 June<br>1995                     | " "                                                         | 27 Sept.<br>1995                                         | 29 Sept.<br>1995                                    |
| Legal Aid Commission Staff<br>Superannuation Fund | 30 June<br>1995                     | 30 Sept. <i>Legal Aid<br/>Commission Act 1978,</i><br>s.42. | 27 Sept.<br>1995                                         | 29 Sept.<br>1995                                    |
| Office of the Director of<br>Public Prosecutions  | 30 June<br>1995                     | 30 Sept. <i>Financial<br/>Management Act 1994,</i><br>s.46. | 16 Oct.<br>1995                                          | 20 Oct.<br>1995                                     |
| Office of the Public Advocate                     | 30 June<br>1995                     | " "                                                         | 6 Oct.<br>1995                                           | 12 Oct.<br>1995                                     |
| Senior Master of the<br>Supreme Court (a)         | 31 Dec.<br>1994                     | <i>Supreme Court Act 1986</i>                               | 19 June<br>1995                                          | 29 June<br>1995                                     |
| Solicitors' Guarantee<br>Fund                     | 30 June<br>1995                     | 30 Sept. <i>Financial<br/>Management Act 1994,</i><br>s.46. | 31 Oct.<br>1995                                          | 31 Oct.<br>1995 (b)                                 |
| State Electoral Office                            | 30 June<br>1995                     | " "                                                         | 31 Oct.<br>1995                                          | 31 Oct.<br>1995                                     |
| Victorian Financial<br>Institutions Commission    | 30 June<br>1995                     | " "                                                         | 5 Sept.<br>1995                                          | 7 Sept.<br>1995                                     |
| Victorian Institute of Forensic<br>Pathology      | 30 June<br>1995                     | " "                                                         | 25 Sept.<br>1995                                         | 28 Sept.<br>1995                                    |
| <b>CORRECTIONS</b>                                |                                     |                                                             |                                                          |                                                     |
| Victorian Prison Industries<br>Commission         | 30 June<br>1995                     | 30 Sept. <i>Financial<br/>Management Act 1994,</i><br>s.46. | 29 Sept.<br>1995                                         | 29 Sept.<br>1995                                    |

**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                              | <i>Financial year ended</i> | <i>Reporting to Parliament</i>                       | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|--------------------------------------------|-----------------------------|------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS - continued</b>        |                             |                                                      |                                              |                                        |
| <b>POLICE AND EMERGENCY SERVICES</b>       |                             |                                                      |                                              |                                        |
| Country Fire Authority                     | 30 June 1995                | 30 Sept. <i>Financial Management Act 1994, s.46.</i> | 18 Sept. 1995                                | 21 Sept. 1995                          |
| Metropolitan Fire Brigades Board           | 30 June 1995                | " "                                                  | 27 Sept. 1995                                | 27 Sept. 1995                          |
| Office of the Chief Commissioner of Police | 30 June 1995                | " "                                                  | 30 Oct. 1995                                 | 30 Oct. 1995 (b)                       |
| <b>INCOMPLETED AUDITS</b>                  |                             |                                                      |                                              |                                        |
| Senior Master of the Supreme Court         | 31 Dec. 1995                | <i>Supreme Court Act 1986.</i>                       | Audit to commence shortly.                   |                                        |

- (a) Senior Master of the Supreme Court produces financial statements which are not a statutory requirement but are audited by arrangement.
- (b) Qualified audit report issued.

# Part 3.5

## Natural Resources and the Environment

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### KEY FINDINGS

#### Melbourne water industry reforms

- The community service function of parks and waterways has not been completely separated from the commercial business of supplying water, sewerage and drainage services as the Melbourne Water Corporation continues to provide \$14 million a year to fund the operations of Melbourne Parks and Waterways.  
*Paras 3.5.13 to 3.5.18*
- Based on the performance of the 3 retail water companies, it appears that City West Water is not as profitable as the other 2 retail water companies.  
*Paras 3.5.23 to 3.5.27*
- Despite the progress made by the Office of the Regulator-General, in satisfying its objective of customer service, its inability to assess operating performance, viability and water service pricing in the short-term has severely affected its effectiveness as the regulator of the water industry.  
*Paras 3.5.51 to 3.5.55*
- While strategies have been developed to undertake a reduction in the total debt of the Melbourne water industry to approximately \$3 billion by 30 June 1998, the level of debt will continue to significantly impact on the industry's ability to effectively utilise resources and provide services to customers at least cost.  
*Paras 3.5.70 to 3.5.72*



**KEY FINDINGS - continued**

**Melbourne water industry reforms - continued**

- The introduction of an additional sewerage charge, the movement to a user-pays system and the replacement of defective water meters, has resulted in an overall increase in the cost to the customer in the order of 4 per cent.  

*Paras 3.5.75 to 3.5.77*
- In the absence of appropriate asset management systems to accurately assess maintenance requirements, projected maintenance expenditure for the Melbourne Water Corporation and the retail water companies may be understated.  

*Paras 3.5.93 to 3.5.98*
- With returns on government equity of 18.2, 17.3 and 25.6 per cent for 1992-93, 1993-94 and 1994-95, respectively, and a planned return of 28 per cent for 1995-96, the State Government has extracted a very healthy return on its investment in the Melbourne metropolitan water industry, compared with other State governments such as the New South Wales Government, which in 1994-95 received a 6 per cent return from the Sydney Water Board.  

*Paras 3.5.101 to 3.5.102*
- The Melbourne Water Corporation and the retail water companies have written-off a combined total of \$54.6 million in assets over the last 2 years.  

*Paras 3.5.103 to 3.5.105*
- Based on forward projections provided by the Melbourne Water Corporation and the 3 retail water companies, the reform process will generate \$109 million in cost savings, 27 per cent less than that originally projected.  

*Para. 3.5.106*

**3.5.1** The Minister for Agriculture and Resources and the Minister for Conservation and Land Management, have responsibility for operations within the Natural Resources and Environment sector. These Ministers have collective responsibility for the Department of Natural Resources and the Environment.

**3.5.2** Details of the specific ministerial responsibilities for public bodies within the Natural Resources and Environment sector are listed in Table 3.5A. These public bodies, together with the former Departments of Agriculture, Energy and Minerals and Conservation and Natural Resources were subject to audit by the Auditor-General during the 1994-95 financial year.

**TABLE 3.5A  
MINISTERIAL RESPONSIBILITY FOR PUBLIC BODIES  
WITHIN THE NATURAL RESOURCES AND ENVIRONMENT SECTOR**

| <i>Ministerial portfolio</i>            | <i>Entities subject to audit</i>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                |
|-----------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Agriculture and Resources</b>        | City West Water Ltd<br>Daratech Pty Ltd<br>Gippsland and Southern Rural Water Authority (a)<br>Goulburn Murray Rural Water Authority<br>Grain Elevators Board (a)<br>Melbourne Market Authority<br>Melbourne Water Corporation<br>Melbourne Water Corporation Employees' Superannuation Fund<br>Murray Valley Citrus Marketing Board<br>Murray Valley Wine Grape Industry Development Committee<br>Non-metropolitan water authorities<br>Northern Victorian Fresh Tomato Industry Development Committee<br>Radius Computing Pty Ltd<br>Rural Water Corporation<br>South East Water Ltd<br>Southern Rural Water Corporation<br>Sunraysia Rural Water Authority<br>Veterinary Board of Victoria<br>Victorian Dairy Industry Authority<br>Victorian Dried Fruits Board<br>Victorian Institute of Marine Sciences<br>Victorian Institute of Marine Sciences Superannuation Fund (b)<br>Victorian Meat Authority<br>Victorian Plantations Corporation<br>Victorian Strawberry Industry Development Committee<br>Water Eco Science Pty Ltd<br>Water Training Centre<br>Wimmera Mallee Rural Water Authority<br>Yarra Valley Water Ltd |
| <b>Conservation and Land Management</b> | Alpine Resorts Commission<br>Bairnsdale Waste Management Group<br>Bundoora Park Committee of Management (c)<br>Environment Protection Authority<br>Eastern Regional Waste Management Group<br>Melbourne Parks and Waterways                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |





|                                                 |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           |
|-------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Conservation and Land Management - cont.</b> | Mount Macedon Memorial Cross Committee of Management (d)<br>Northern Regional Refuse Disposal Group<br>Olympic Park Committee of Management (e)<br>Penguin Reserve Committee of Management<br>Port Bellarine Committee of Management<br>Recycling and Resource Recovery Council<br>Royal Botanic Gardens Board<br>Shrine of Remembrance Trustees<br>South Eastern Regional Waste Management Group<br>State Swimming Centre Committee of Management<br>Surveyors Board<br>Victorian Conservation Trust<br>Waste Management Council<br>Western Regional Waste Management Group<br>Yarra Bend Park Trust<br>Zoological Board of Victoria<br>Zoological Board of Victoria Superannuation Fund |
|-------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

(a) Ceased operations on 31 December 1995.  
 (b) Ceased operations on 30 June 1990.  
 (c) Ceased operations on 18 January 1996.  
 (d) Ceased operations on 18 April 1995.  
 (e) Melbourne and Olympic Parks's Trust established on 5 October 1995, incorporating the former National Tennis Centre Trust and the Olympic Park Committee of Management.

**MELBOURNE WATER INDUSTRY REFORM**

**Background**

**3.5.3** Prior to 1 July 1994, the metropolitan water industry was operated by the Melbourne Water Corporation, a statutory corporation with responsibility for:

- water, sewerage and drainage systems for greater metropolitan Melbourne;
- management of Melbourne's open spaces and waterways; and
- the operation component of industrial waste management within Victoria.

**3.5.4** As the only provider of the above services, the Corporation operated as a monopoly and, as such, had been protected from competitive pressures. The State Government was of the view that this protected position had resulted in an organisation which was not receptive to change, unresponsive to customer needs, inefficient and operated with high debt levels and over-investment in its capital infrastructure.

**3.5.5** To address this situation the State Government set about reforming the metropolitan water industry in 1993. The outline of the Government's reform program was detailed in the former Office of State Owned Enterprise's policy document titled *Reforming Victoria's Water Industry: A Competitive Future, October 1993*.

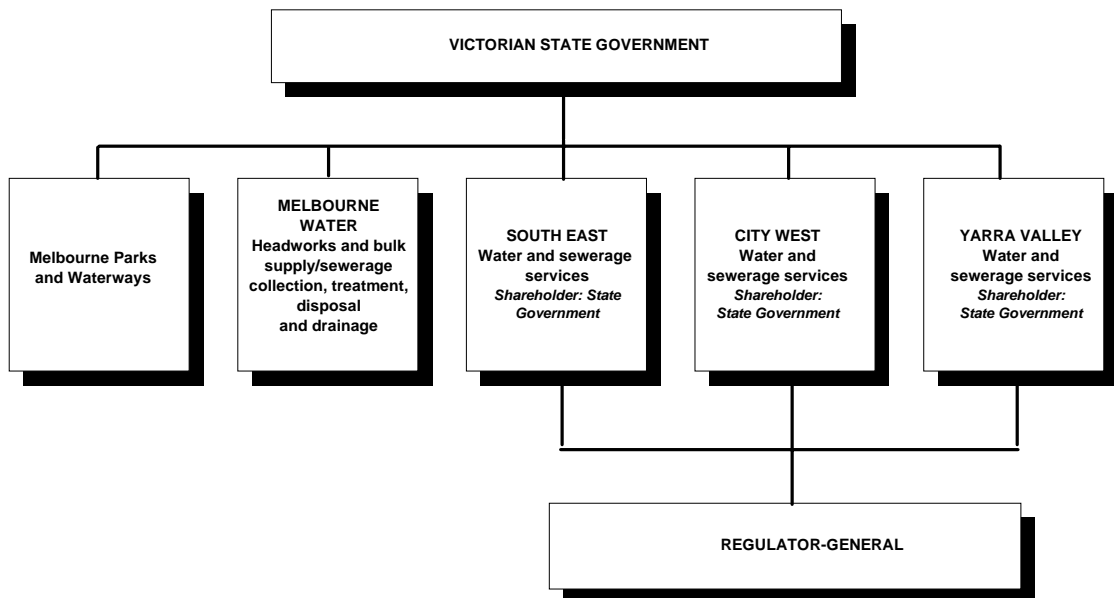
**3.5.6** A major component of the reform process involved legislative changes in the form of the *Melbourne Water Amendment Act 1994*, which provided for the corporatisation and break-up of Melbourne Water Corporation, and the *Water Industry Act 1994*, the licensing of 3 new retail water companies and the creation of Melbourne Parks and Waterways. The 3 new entities were:

- City West Water Limited;
- Yarra Valley Water Limited; and
- South East Water Limited.

**3.5.7** In the new structure, the Corporation's role was reduced to that of water and sewerage wholesaler and supplier of drainage services. Melbourne Parks and Waterways assumed responsibility for the management of Melbourne's parks and waterways and the 3 retail water companies were created to manage water and sewerage distribution services and some limited sewerage treatment services.

**3.5.8** An outline of the new structure is provided in Chart 3.5B.

**CHART 3.5B  
NEW STRUCTURE OF MELBOURNE WATER INDUSTRY**



**3.5.9** Reforms introduced into the water industry were designed to provide a number of benefits to the community, including:

- a reduction in operating expenditure;
- more efficient use of resources;
- better service to customers;
- a reduction in debt financing;



- more effective provision of public goods;
- a viable long-term water industry; and
- better management of Victoria's scarce natural water resources.

**3.5.10** In accordance with allocation statements approved by the Treasurer on 29 December 1994, the assets and liabilities detailed in Table 3.5C were transferred from the Corporation to the new water companies and Melbourne Parks and Waterways.

**TABLE 3.5C**  
**TRANSFER OF ASSETS, LIABILITIES AND EQUITY TO NEW WATER**  
**ENTITIES**  
 (\$m)

| <i>Entity</i>                 | <i>Total assets</i> | <i>Total liabilities</i> | <i>Total equity</i> |
|-------------------------------|---------------------|--------------------------|---------------------|
| Yarra Valley Water            | 1 055.2             | 660.6                    | 394.6               |
| South East Water              | 966.4               | 605.8                    | 360.6               |
| City West Water               | 512.1               | 329.2                    | 182.9               |
| Melbourne Parks and Waterways | 165.9               | 18.0                     | 147.9               |

**3.5.11** In undertaking this review of the Melbourne metropolitan water industry, audit was aware of the fact that the water reform process was still taking place. Although the legislative framework, operational structure and management teams had been established, strategies and targets in relation to many other aspects of the reform process such as pricing, financial viability, debt management and asset management were still evolving.

**3.5.12** In respect of these later aspects, audit has not attempted to form a judgement on whether objectives established to date have been achieved, but rather to identify potential problems and risks that may need to be addressed.

**Separation of responsibility for provision of public goods**

**3.5.13** Pursuant to the *Water Industry Act* 1994, Melbourne Parks and Waterways (MPW) was established as an independent statutory body on 1 July 1994. From this date, MPW assumed responsibility for managing and controlling open space, parks and waterways within the Melbourne metropolitan area for the purposes of conservation, recreation, leisure, tourism and navigation.

**3.5.14** The Government's objective in establishing MPW was to separate the community service function of parks and waterways management (public goods) from the Corporation's commercial business, which involved supplying water and sewerage services (private goods) to the public.

**3.5.15** Separation of commercial and community activities was designed to eliminate problems associated with conflicting responsibilities and objectives, allowing both organisations to clearly focus on their respective core functions and to deliver services and outcomes in a more effective manner.

**3.5.16** Although the separation of commercial and community services is substantially complete, the Corporation still retains responsibility for the provision of



some community services (\$2.5 million), such as drainage rate exemptions for non-rateable properties.

**3.5.17** The Corporation also continues to pay approximately \$14 million a year to the Consolidated Fund to fund services provided by MPW.

**3.5.18** **In audit opinion, consideration should be given to completely separating these community responsibilities from the Corporation.**

**Focus on core business**

**3.5.19** In addition to separating the provision of public and private goods, the disaggregation of the Corporation was also designed to separate its retail and wholesale businesses. This was achieved by establishing and issuing licences for the provision of metropolitan water supply and sewerage services to 3 new water companies.

**3.5.20** The Corporation retained responsibility for:

- water collection, storage and the wholesale function of delivery;
- treatment and disposal of sewerage; and
- drainage services.

**3.5.21** The newly created retail water companies assumed responsibility for the distribution of water and sewerage services, which are purchased from the Corporation on commercial terms.

**3.5.22** The break-up of the Corporation's operating structure was designed to enable each of the retail water companies and the Corporation to focus on their respective core business, by restricting each entity to a select number of key commercial objectives.

**Introduced competition**

**3.5.23** As a monopoly institution, the Corporation was seen as being protected from competitive pressures. Although the introduction of competition was likely to generate operating efficiencies, the nature of the business with its fixed supply infrastructure did not allow for the provision of alternative service suppliers.

**3.5.24** In the absence of direct competition, the Government decided that efficiencies could be generated through the creation of 3 regionally-based distribution businesses which would not compete for each others customers but compete by comparison. The retail water companies would compete with one another on the basis of service and business performance, allowing customers to compare their performance, quality and service with those in neighbouring regions.



**3.5.25** In order for there to be effective competition, the Government established the retail water companies based principally on catchment areas. Although the concept of competition by comparison is sound, its practical application was always likely to create some difficulties. The concept is largely dependent on establishing 3 comparable organisations. However, the companies had a number of significant differences, which included:

- in terms of the value of assets and liabilities, City West Water is effectively half the size of the other 2 companies;
- City West Water's distribution network, which covers a greater proportion of inner city Melbourne, is the oldest of the 3 companies;
- 70 per cent of City West Water's water and sewerage revenue was paid to the Corporation in 1994-95 (for the purchase bulk of water and sewerage services), compared with 44 per cent and 50 per cent for South East Water and Yarra Valley Water, respectively; and
- City West Water's projected annual revenue of less than \$300 million is significantly less than South East Water which generates in excess of \$400 million and Yarra Valley Water which generates in excess of \$440 million.

□ *RESPONSE provided by Secretary, Department of Treasury and Finance*

*The different value of the asset base of each business does not prevent comparison of performance. The Water Reform Unit (WRU) has developed a series of ratio measures which complement analysis undertaken by the Monitoring Unit of Privatisations and Industry Reform Division.*

*Differences in the age of assets does not prevent comparison across retail companies but can be taken into account when analysing results.*

**3.5.26** The factors outlined above have contributed to the lower profitability of City West Water in comparison with the other 2 companies both on total operating result and in terms of the return on assets employed, i.e. earnings before interest and tax over total assets. City West's operating result after tax for 1994-95 was a loss of \$5 million compared with South East Water (\$32 million profit) and Yarra Valley Water (\$42 million profit). These results were arrived at after allowing for \$14.1 million, \$11.3 million and \$4.5 million respectively

**3.5.27** On the basis of return on assets employed, the results were: City West (3.0 per cent), South East Water (12.5 per cent) and Yarra Valley Water (13.1 per cent).

□ *RESPONSE provided by Secretary, Department of Treasury and Finance*

*City West Water's loss after tax was a direct result of a decision to write-off \$14.1 million in assets and other abnormal items. This write-off is outside the core operations of the business and was a prudent decision by an independent Board based on an inherited position at disaggregation.*

**Corporatisation**



**3.5.28** Another component of the reform process involved the corporatisation of the 3 retail water companies. Corporatisation refers to the process of replicating or introducing commercial and market disciplines into public sector organisations while still retaining full government ownership. Benefits to the community from corporatisation are perceived as:

- improved operations through the establishment of specific performance targets and creation of boards of directors with appropriate commercial expertise;
- a movement to market-driven corporate strategies;
- changed attitudes to the way in which the organisation operates;
- greater independence from government allowing more control by management over business activities; and
- enhanced accountability through the provision of improved information on operations.

**3.5.29** It is difficult to assess the benefits of corporatisation at this early stage of the reform process, however, in audit opinion once provision of the Corporation's community services were separated from its commercial products, corporatisation of the retail water companies represented a logical progression.

**Operating licences**

**3.5.30** In order to ensure that the retail water companies provide appropriate services to the public, the terms and conditions of their provision are defined and outlined in a licence agreement between each company and the Government.

**3.5.31** Establishing acceptable standards of practice under each operating licence provided customers with information on their entitlements and established a benchmark by which each company's performance could be measured.

**3.5.32** The principal conditions of the licences cover provision of services, performance standards, oversighting of pricing, customer service guarantee, customer liaison and penalty provisions.

**Performance monitoring**

**3.5.33** A major objective of the disaggregation of the Melbourne metropolitan water industry was to achieve operational efficiencies and improve service to customers. In order to facilitate improved performance of the water industry, 3 separate mechanisms were established.

*Privatisations and Industry Reform Division*

**3.5.34** The first of the performance monitoring functions was to be undertaken by the Privatisations and Industry Reform Division of the Department of Treasury and Finance. Discussions held with the Division's staff indicated that its role was to establish a comprehensive and consistent monitoring regime for all Government Business Enterprises.

**3.5.35** Performance measures and indicators were to be established in order to provide criteria by which the performance of Government Business Enterprises could be assessed. The competitiveness of these entities was then to be measured by



comparison, through benchmarking of service activities, trend analysis and segment analysis on an activity basis, using established performance indicators. Performance indicators have been developed and used to measure the performance of the 3 retail water companies. **However, as the information is considered to be commercially sensitive, assessments of the comparative performance of the companies is not publically available. As a result, customers cannot assess the overall performance of retail companies as envisaged by the model of competition by comparison.**

*National Performance Monitoring*

**3.5.36** Another mechanism by which the performance of the water industry is assessed involves the Trading Enterprises Steering Committee on National Performance Monitoring of Government Trading Enterprises (GTEs), which was established in 1991. The objective of the Committee was to develop a set of indicators to allow the performance of GTEs to be monitored, with the results published annually. The Committee's first report, released in April 1995, assessed financial performance, pricing, shareholder's returns, assets, debt, productivity and service quality, of a number of GTEs including the Corporation.

**3.5.37** Information contained in the Committee's report has been used in the audit analysis of pricing and viability of the water industry.

*Role of the Regulator-General's Office*

**3.5.38** An important element of the Government water industry reform process was to move the Melbourne metropolitan retail (but not the wholesale) water industry away from self-regulation to a system in which the efficiency and effectiveness of the 3 retail water companies within that segment of the industry are publicly monitored.

**3.5.39** In order to establish an independent monitoring function, responsibility for ensuring compliance with licence provisions was assigned to the Office of the Regulator-General (the Office). The major role of the Office, which was established on 1 July 1994, is to promote competition and look after the interests of customers. In relation to the Melbourne metropolitan water industry, the Office has the following specific objectives:

- ensure the maintenance of an efficient and economic water industry;
- protect the interests of customers with respect to water industry charges and terms and conditions of water industry services;
- protect the interests of customers with respect to the reliability and quality of water industry services; and
- facilitate the maintenance of a financially viable water industry.

**3.5.40** Audit review of the Office's role disclosed the following.



*Monitoring of financial performance*

**3.5.41** The Office has commenced the process of developing industry benchmarks, performance indicators and targets, which will enable it to assess the efficiency and quality of services provided by the retail water companies, monitor compliance with licence conditions, compare the performance of the companies and provide essential information required for execution of an economically and technically sound pricing review process.

**3.5.42** Discussions with the Office indicated that monitoring of company performance has been developed in consultation with the industry and the Office's Customer Consultative Committee. The first report on the retail water industry performance, covering calendar year 1995, will be published in May 1996. Similar reports will be published annually. A primary objective in publishing this information is to inform and empower customers thereby stimulating competition by comparison between these monopoly businesses. The Office is extending this program, in consultation with the companies and customer representatives, to cover some additional technical performance indicators which will be incorporated into later reports.

**3.5.43** **The development of appropriate industry benchmarks, performance indicators and targets for the Melbourne metropolitan water industry is a complex exercise. Given these complexities, the Office has engaged the services of consultants with international water industry expertise to assist in their development. Until these indicators and benchmarks are established, effective independent monitoring and regulation of the industry will not be complete.** However, audit is of the opinion that the Office has commenced a process that will enable assessment of the performance of the metropolitan water industry to be undertaken.

*Protecting customer interests and promoting services*

**3.5.44** In recognition of its objectives to "protect the interests of customers with respect to terms and conditions of water industry services", the Office has developed an industry standard customer contract and customer charter. These documents are designed to define the terms and conditions under which the water industry operates and promote the reliability and quality of services provided to customers. These documents were completed in December 1995.

**3.5.45** The contract and charter contain extensive information regarding customer service performance indicators and incorporates such measurables as the supply of water and sewerage services, interruptions to those services, charging and methods of billing, restriction or disconnection of services and responsibilities for maintenance services.

**3.5.46** The Office also provided assistance to the 3 retail water companies to enable them to produce an abridged version of the charter for distribution to all customers.





- 3.5.47** A number of other initiatives undertaken by the Office include:
- development of a customer service performance indicator schedule, which is required to be completed on a quarterly basis by each company; and
  - planned publication of the results from the Office's analysis of customer service indicators, with the first report due for release in May 1996.

**3.5.48** **The Office and the retail companies should be commended for the development and implementation of the standard customer contract and charter.**

*Financial viability of the retail water companies*

**3.5.49** Another key objective of the Office in carrying out its function and exercising its powers under the *Water Industry Act 1994*, is to "facilitate the maintenance of a financially viable water industry". For example, when it comes to set prices in the industry it would have regard to the effect its decisions may have on the financial viability of the water industry. However, as noted below, responsibility for pricing issues remains with the Government until at least July 1998.

**3.5.50** **Discussions with management of the Office indicated that in the absence of government policy that allows licensing of the Corporation, the Office has no power to obtain information for the complete industry. Consequently, the Office has undertaken only general planning work for a water industry pricing review.**

*Pricing review*

**3.5.51** In order to protect the interests of customers in relation to water industry charges, and also to facilitate the maintenance of a financially viable water industry, the Office has responsibility for the review of water and sewerage tariffs.

**3.5.52** In this context, the powers of the Office to regulate pricing are set out in the *Office of the Regulator-General Act 1994*. The Act empowers the Office to prescribe price levels having regard to:

- cost of making, producing or supplying of the goods or services;
- return on assets;
- interstate and international benchmarks for prices, costs and return on assets in comparable industries;
- financial implications of the determination; and
- any other factors considered relevant.

**3.5.53** The Office was advised by the Treasurer and the Minister for Natural Resources in November 1995 that water pricing will remain under the control of the Government until at least 1 July 1998 and that the Office would not conduct a review of water industry pricing in 1997. Audit was advised by the Office that experience in the United Kingdom showed that a comprehensive, economically independent pricing review and technically sound pricing review would take around 3 years to complete. If a review was not commenced until after 1998, this could result in it not being completed until 2001.



**3.5.54** Although the interests of customers are largely protected through the Government's cap on water and sewerage rates and charges until 1 January 1997, delaying the Office's first independent price review may leave customers vulnerable to price movements until such time as the review is completed. In addition, until the Office undertakes a pricing review it is unable to determine the financial viability of the Melbourne metropolitan water industry.

**3.5.55** Despite the progress made by the Office in satisfying its objective of customer service, its inability to assess operating performance, viability and water service pricing in the short-term could possibly inhibit its effectiveness as the regulator of the water industry.

□ *RESPONSE provided by Secretary, Department of Treasury and Finance*

*ORG's power to regulate prices are contained in the Office of the Regulator-General Act 1994. These powers must be triggered by Orders in Council being made under section 3(2) of that Act. Those orders have not been made.*

*The Government, through current amendments to the Water Industry Act, has decided to maintain control over pricing until at least 1998. The WRU has been asked by the Government to undertake a review of the pricing and regulatory framework in order to develop a set of pricing guidelines which can be passed to ORG in due course. This will ensure there is no period when pricing conditions are unclear.*

*No evidence or arguments are advanced as to why a delay in ORG's first review, while the Government continues to exercise its control over prices in the interim, "may leave customers vulnerable to price movements".*

*Independent monitoring of the Corporation*

**3.5.56** Although the Corporation is deemed to be part of the regulated water industry for the purposes of Part 3 of the *Office of the Regulator-General Act 1994*, it is not required to operate under a licence and is therefore outside the regulatory framework of the Office.

**3.5.57** The Government is responsible for determining the price of bulk water and sewerage services supplied to the retail water companies, which is built into the retail price charged to customers. As the Office has no control over the Corporation's pricing policy or even access to all necessary information, its ability to effectively regulate retail prices could be impaired.

**3.5.58** In order to improve the Office's control over pricing policy the Government should consider the introduction of a licence, monitored by the Regulator-General, to cover the provision of the Corporation's services.

*Return on assets*

**3.5.59** The percentage return generated on assets employed is a good indicator of how efficient an organisation manages its assets. This ratio compares earnings before interest and income tax with the value of total assets.

**3.5.60** At present, the Corporation and the retail water companies are recording their fixed assets at cost. Therefore, any return on asset calculations for the industry reflect the return on the historical cost of the assets employed.



**3.5.61** In comparison, the Sydney Water Board and a number of overseas water utilities use replacement cost to value their assets. Consequently, the return on assets employed is much lower than for the Melbourne metropolitan water industry.

**3.5.62** **If the performance of the Corporation and the retail water companies is to be effectively benchmarked against comparable interstate and overseas water utilities, valuing fixed assets based on the current cost of their replacement may be more appropriate.**

□ *RESPONSE provided by Secretary, Department of Treasury and Finance*

*For national performance monitoring purposes the four water businesses provide information according to the National Government Trading Enterprises guidelines. This incorporates a form of current value of assets. For accounting purposes, the retail companies report under Australian Securities Commission requirements. The DTF will review whether these separate reporting requirements can be more closely aligned.*

## Debt management

**3.5.63** Traditionally, the Corporation has relied heavily on debt financing to fund its capital needs. The following statistics provide some indication of the level of reliance placed on debt financing:

- in 1993-94, 39 cents in every dollar of revenue generated by the Corporation was applied to service the Corporation's debt;
- with a ratio of interest bearing debts to total assets (historical cost) of 76 per cent in 1994-95, the level of debt financing in the Corporation was significantly above industry standards for water utilities in the United States, which operate with ratios in the order of 50 to 60 per cent; and
- with a ratio of profit before interest and tax to finance charges of 1.8 to 1, the Corporation had a low interest cover by international private sector water utility standards, e.g. Standard and Poor's A and BBB grade credit ratings in the United States of America require an interest cover ratio in the order of 3 to 1 and 2 to 1, respectively.

□ *RESPONSE provided by Secretary, Department of Treasury and Finance*

*Debt funding has been employed in the past as previous governments have extracted high levels of dividends, leaving insufficient funds in the business to service capital requirements. The current Government has significantly reduced dividend levels as a means of reducing debt, and to allow internal funding of capital programs.*

*Discussions with all retail companies indicate that the current planning process will realise substantial improvements in their interest cover ratios over the planning period, that is, to June 1998.*

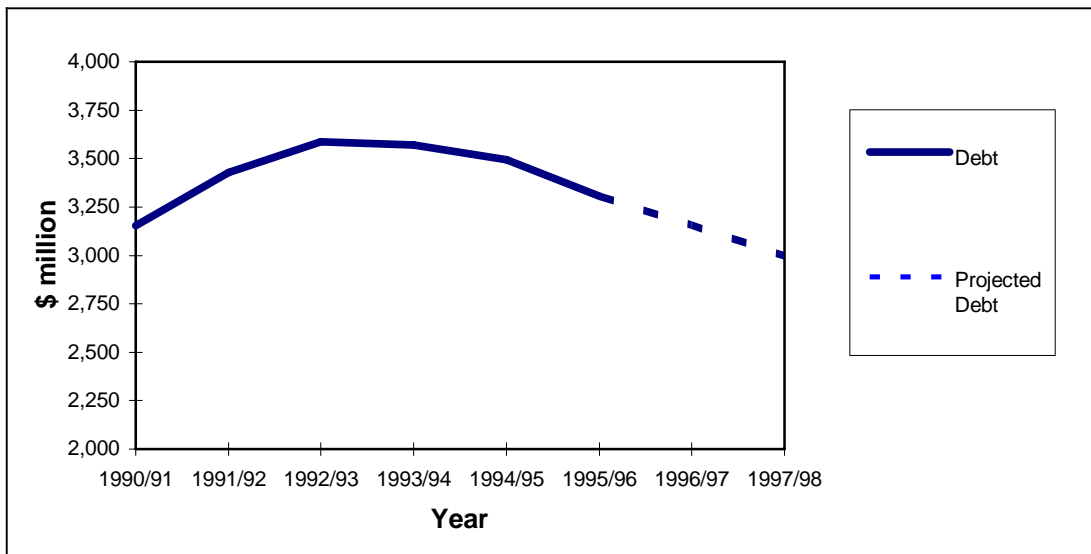
**3.5.64** This debt burden restricted the Corporation's ability to effectively fund its future water investment and infrastructure needs and resulted in higher costs for

customers. In order to address this situation the Government took action to reduce the overall debt level by:

- establishing the retail water companies with a commercial level of debt relative to their asset base, so that they were able to generate sufficient profits to fund a program of debt retirement;
- requiring all future capital works to be funded internally;
- reducing the level of dividends payable to the Consolidated Fund below historical levels;
- requiring a greater proportion of operating surpluses to be applied to fund debt retirement; and
- requiring the retail businesses to reduce their ratio of debt to total asset from an average of 57 percent on establishment to 43 percent by 30 June 1998.

**3.5.65** Using projections outlined in business plans prepared by the Corporation and the retail water companies, audit has graphed the combined debt and the associated financing costs for the 4 entities over a 3 year period to 1997-98. This information is outlined in Chart 3.5D. The amounts used for 1993-94 and earlier relate to the Corporation prior to disaggregation.

**CHART 3.5D  
ANALYSIS OF DEBT FOR MELBOURNE WATER CORPORATION  
AND RETAIL WATER COMPANIES**



**3.5.66** The planned overall debt reduction for the next 3 years is \$530 million (18 percent). This is to be achieved through debt reductions of \$345 million by the Corporation, \$85 million by South East Water, \$24 million by City West Water, and \$76 million by Yarra Valley Water.

**3.5.67** While the development of a structured debt reduction program is commendable, the attainment of debt reduction targets is dependent on the achievement of future revenue estimates and expenditure reductions. The accuracy of these projections is likely to be affected by the following factors:



- Revenue projections provided to audit assumed a continuation of historic water usage rates. The progressive introduction of a user-pays system for pricing, could reduce the demand for water and result in a reduction in revenue;
- The Corporation plans to reduce its full-time contract staff to 75 by 30 June 1996, but at the end of April 1996 107 contract staff were still employed; and
- South East Water was assigned an additional \$40 million debt in 1994-95, subsequent to the setting of the debt reduction targets. As indicated in its 1995-96 corporate plan the inclusion of this additional debt is likely to impact on the achievement of its debt reduction target. Achievement of this target now seems dependent on the postponement of its 1995-96 dividend payment and a reduction in tax payments.

□ **RESPONSE** provided by Secretary, Department of Treasury and Finance

*A shift towards user pays pricing would include reductions in the fixed charge and increases in the variable charge. The overall impact may be only a small change in revenue.*

*Each year the debt to asset ratios are negotiated with the businesses in the light of their total business plan. The use of the terms "Government objective" and "debt reduction targets" is too strong. One of the Government's reform goals is to achieve substantial debt reduction. However, this is but one of several goals which have to be assessed and ranked. Price reform, reduction of cross subsidies, improved operational efficiencies, whole of life asset condition management, and a competitive environment for the businesses are also important goals of reform that must be balanced with debt reduction in order to improve total water industry performance.*

**3.5.68** In addition, City West Water and Yarra Valley Water have incorporated into their business plans debt to asset ratios of 48 and 45 per cent, respectively, compared with the Government's objective of a 43 per cent ratio by 30 June 1998.

**3.5.69** As a result of the above factors there is some doubt over the industry's ability to meet its debt reduction targets.

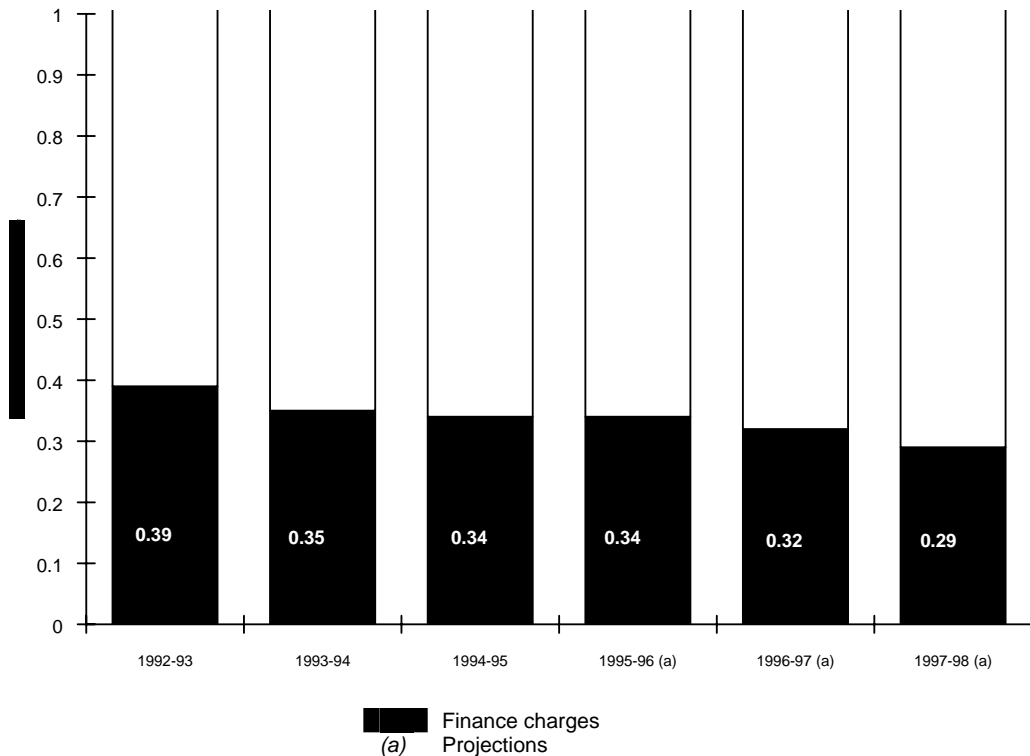
*Debt servicing costs*

**3.5.70** Based on information from the corporate plans, audit estimates that the costs of servicing the overall debt as a proportion of the revenue generated by the water entities will diminish over time. Audit projections indicate that the amount of revenue needed by the water entities to service their existing debt will be reduced from the 39 cents in the dollar of revenue required in 1992-93 to 29 cents (35 cents for the Corporation and an average of 21 cents for the retail water companies) in 1997-98, a 26 per cent reduction. This information is illustrated in Chart 3.5E.

**3.5.71** Despite the reduction in debt and the consequential decrease in finance charges, these charges still represent on average 45 percent of the projected annual operating expenditure of the 4 entities and the Corporation and the companies will continue to operate in an environment where a significant amount of resources will need to be allocated to debt servicing.

**3.5.72** While strategies have been developed to undertake a reduction in the total debt of the Melbourne metropolitan water industry to approximately \$3 billion by 30 June 1998, the level of debt will continue to significantly impact on the industry's ability to effectively utilise resources and provide services to customers at least cost.

**CHART 3.5E**  
**ANALYSIS OF FINANCE CHARGES TO OVERALL REVENUE FOR THE**  
**MELBOURNE WATER CORPORATION & THE RETAIL WATER COMPANIES**



**Pricing**

**3.5.73** Another major objective of the Government reform process involved setting a fair price for water and sewerage charges. Pricing also has significance as it impacts on the achievement of other reform objectives such as achieving a market return on assets invested, improved efficiency and ensuring the long-term viability of the industry.



**3.5.74** In addition to the requirement of achieving the above objectives, pricing decisions are also influenced by:

- the level of recovery under the "user pays" philosophy;
- strategies to reduce costs of providing water and sewerage services; and
- the recovery of investment in new assets (growth factor).

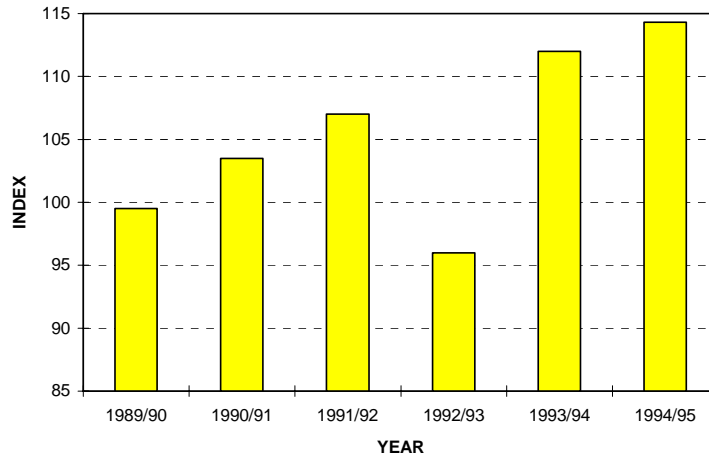
*Retail prices*

**3.5.75** Domestic water and sewerage rates and charges have 3 components: a fixed component linked to the value of the property serviced, a variable component related to water consumption and a sewerage disposal charge, which was introduced in January 1995. The fixed component and the rate applied to water consumption to calculate the variable component of retail prices for water and sewerage services provided to the public, were amended as from 1 July 1994 and have been frozen by the Government until 1 January 1997. The Government retains responsibility for the fixed and variable component of retail pricing until July 1998. From this date, the Regulator-General becomes responsible for pricing.

**3.5.76** The Government estimated that these changes would increase the price to the average household, using a constant amount of water, by 3.6 per cent per year. During 1994-95, the retail water companies commenced checking and replacing defective domestic water meters. The replacement of these meters in many households, although representing an efficiency saving to the retail water companies, has generally resulted in higher water consumption charges for the individual households affected.

**3.5.77** In order to assess the movement in retail prices and their comparability with other states, audit (using information contained in the April 1995 report of the Steering Committee on National Performance Monitoring of Government Trading Enterprises) has graphed in Chart 3.5F the average cost of Melbourne metropolitan water and sewerage services per household in real terms over a 6 year period. **From the chart it can be seen that the price charged to customers for water and sewerage rates and charges increased during 1994-95 by 4 per cent.**

**CHART 3.5F  
MELBOURNE METROPOLITAN WATER AND SEWERAGE CHARGES**



User-pays system

**3.5.78** In 1994 the Government announced that greater reliance would be placed on a user pays system in the setting of prices for domestic customers. This involved a movement away from fixed property-based pricing to one based on consumption.

**3.5.79** Adoption of a user-pays system is an effective demand management strategy, in that it provides customers with an incentive not to waste water and is also considered by many to be a fairer system of charging.

**3.5.80** In an effective user-pays system the price charged to the customer reflects the cost associated with delivering the service. In respect of the Melbourne metropolitan water industry, with the cost to the customer still largely dependent on the value of the property serviced, the current customer charges do not reflect the cost of providing the services, resulting in a significant level of cross-subsidisation. Domestic customers in high value properties are subsidising those in lower valued properties, customers adjacent to storage and sewerage treatment facilities are subsidising those more distant and industrial customers are subsidising domestic customers.

**3.5.81** The most significant cross-subsidy involves Melbourne central business district (CBD) customers. The reliance on property-based charging for commercial properties, in conjunction with the relatively high value of those properties, results in CBD businesses paying a high average price for water use than domestic customers.

**3.5.82** In announcing in June 1994, the move to a user pay system, the Minister for Natural Resources stated that it would be planned in over 8 years with full implementation by 2002.





**3.5.83** However, the objective of the reform program had been amended by January 1995 when the Government announced in the policy document *Reforming Victoria Water Industry* that it now aimed to achieve a 50/50 split between property based fixed charges and user pays variable charges by 2002. The Office of the Regulator-General will oversight the partial user-pays water pricing regime from July 1998.

**3.5.84** The consequence of delaying the full implementation of a user-pays system is that subsidisation will continue.

*Wholesale prices*

**3.5.85** Prior to disaggregation, the Corporation as the wholesaler and retailer of water and sewerage services only needed to establish appropriate retail prices for its services. Following the split of the wholesale and retail businesses, responsibility for retail and wholesale pricing was transferred to the Government.

**3.5.86** The Government effectively controls the wholesale price by requiring the Corporation to meet its finance charges, tax and dividend payments out of an amount equivalent to a 7 per cent return on the assets it employs.

**3.5.87** The initial wholesale price for water and sewerage services was set at a level sufficient to enable recovery of the Corporation's historic operating costs. However, the Corporation plans to adopt a commercial approach to pricing its water and sewerage services by setting the price at a level which will ensure recovery of its operating, maintenance, current cost depreciation and administrative costs. It will also provide for a 7 per cent return on the value of assets employed to meet finance costs and dividend and tax payments.

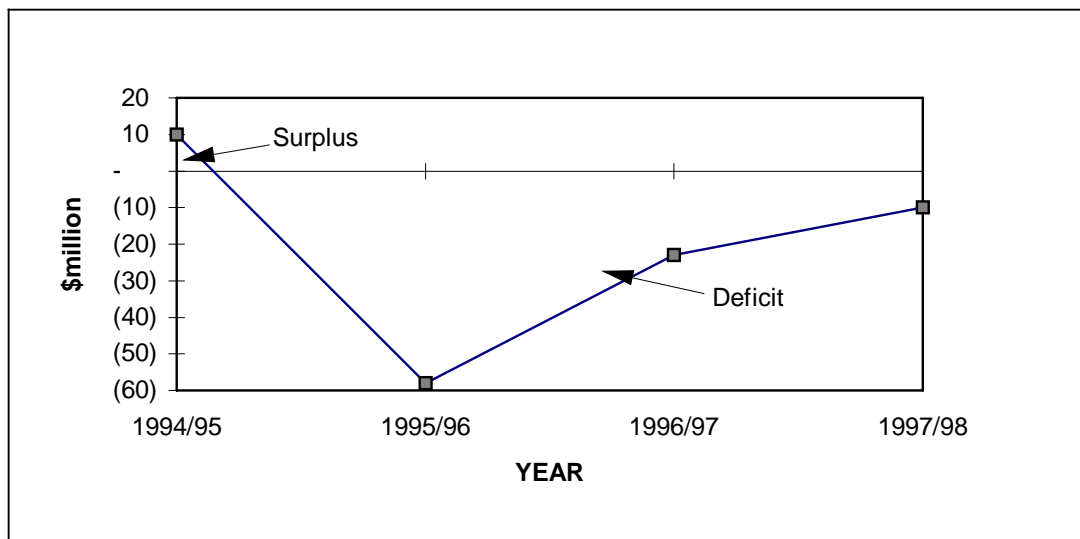
**3.5.88** The setting of the wholesale price will still be calculated on a cost-plus basis, which may result in inefficiencies in the operations of the wholesale business to flow into wholesale and retail prices. As indicated earlier, authorising the Regulator-General to review the wholesale as well as the retail price of water and sewerage services may resolve this problem.

**3.5.89** In addition, if the Corporation is to operate efficiently it needs to sell its water and sewerage services to the retail water companies at a price reflecting the full cost of providing those services. The Corporation considers that, as the cost of financing its debt and equity may vary from an amount equivalent to 7 per cent of assets employed, its restricted pricing policy cannot ensure sufficient funds are available to ensure its long term viability.

**Viability of the water industry**

**3.5.90** As indicated earlier, the success of the water reform process was reliant on a strong viable water industry. In order to assess the future viability of the Corporation and the retail water companies, audit reviewed the projected cash flows of each business over the period from 1994-95 to 1997-98. Information on the combined cash flows of the 4 entities is demonstrated in Chart 3.5G. The cash flow projections, which are based on information extracted from each organisation's 1994-95 financial statements and business plans, included maintenance expenditure, capital acquisitions, dividend and debt repayments.

**CHART 3.5G  
ANALYSIS OF FUTURE CASH FLOWS**



**3.5.91** From the chart it can be seen that the combined entities will have a cash surplus of \$10 million in 1994-95 and deficits of \$59 million, \$23 million and \$10 million over the next 3 years. **The projected deficits include non-mandatory payments such as dividends and debt retirement. It is therefore possible to reduce these payments in order to achieve positive cash flows in 1995-96 and the following 2 years, without impacting on the viability of the organisations and on service charges.**

**3.5.92** However, reducing planned debt reduction and dividend payments will impact on the achievement of the industry's debt reduction targets and the Government's projected dividend revenue.

□ **RESPONSE** provided by Secretary, Department of Treasury and Finance

*Chart 3.5G is based on cashflows in the 1995/96 Business Plan, but has subtracted from these cashflows actual dividends declared in 1994-95, which were not previously included in forecasts. The chart has not included other factors which have improved cashflows since the plans were developed. Based upon forecast data, the net decline in cashflows for the entire metropolitan water industry is expected to be in the order of \$7.4m in the 1995-96 year and not \$59m as stated.*



*Maintenance expenditure*

**3.5.93** Audit review of the asset management systems of the Corporation indicated that, traditionally, most of the maintenance activities undertaken represented reactive maintenance, such as repairs to damaged or leaking infrastructure. Systems and procedures had not been developed to effectively:

- assess the condition of infrastructure and other fixed assets;
- monitor the performance of these assets;
- undertake needs analysis; and
- perform economic evaluations of asset management options.

**3.5.94** In the absence of these systems and procedures, the Corporation was not in a position to develop an appropriate asset maintenance strategy or accurately estimate their future maintenance expenditure.

**3.5.95** A number of initiatives have recently been established to address these problems, including:

- development of a methodology and generic set of standards addressing condition and hydraulic status of water and sewer assets;
- monitoring assets in accordance with established programs, which include structural inspection and hydraulic monitoring;
- upgrading assets to a condition where they can be safely operated to meet prescribed standards of service;
- implementation of closed-circuit cameras and other surveillance procedures to monitor assets; and
- expediting assessments of hydraulic conditions of its sewer systems which would facilitate comprehensive assessments on sewer assets.

**3.5.96** Although these initiatives are commendable they do not go far enough to ensure effective management of the Corporation's fixed assets, as an overall condition assessment of all the Corporation's infrastructure assets is still to be completed. In addition, only limited use has been made of needs analysis and economic evaluations of asset management options.

**3.5.97** A review of the maintenance expenditure of the wholesale business indicated the following:

- The Corporation spent on average \$16 million a year on maintenance expenditure over the last 4 years. This expenditure is \$10 million a year more than the expenditure planned for the next 3 years; and
- Preventative maintenance expenditure for 1993-94 of \$6 million was considerably less than the \$17 million spent by the Hunter Water Corporation and the \$24 million spent, by the Sydney Water Board in the same period.



**3.5.98** In the absence of appropriate systems to accurately assess maintenance requirements, the above statistics may indicate that the projected maintenance expenditure for the Corporation may be understated. Any maintenance costs in addition to those provided for in the plan would further impact on the projected cash deficiencies.

□ *RESPONSE provided by Secretary, Department of Treasury and Finance*

*Comparisons between MWC's level of asset management expenditure and the Hunter Water Corporation and Sydney Water Board is an unreliable method of identifying potential asset condition problems in Melbourne. There are a number of reasons for this:*

- *the geology of the central east coast of NSW is substantially different to that of Melbourne, producing significantly higher maintenance and construction costs;*
- *the NSW environmental standards differ from those of Melbourne;*
- *NSW uses different and high cost technology to treat sewage; and*
- *the asset age profile and geographic dispersion of customers differs.*

*Capital expenditure*

**3.5.99** As with maintenance expenditure, the information systems operated by the Corporation are not capable of effectively determining the condition of the existing infrastructure assets and the timing and cost of major capital enhancement and renewal expenditure. In the absence of this information, it is very difficult to evaluate the adequacy of the future capital expenditure of the Corporation.

**3.5.100** However, any understatement of future capital expenditure needs will again impact on the above cash flow projections.

*Dividend and taxation payments*

**3.5.101** Traditionally the Corporation's pricing has been set at a level which would allow for a significant return for the Government on its investment in the organisation. These returns were 18.2, 17.3 and 25.6 per cent for 1992-93, 1993-94 and 1994-95 respectively. As demonstrated by the size of the returns, (the NSW Government received a 6 per cent and 2 per cent return on its equity in the Sydney Water Board and Hunter Water Corporation, respectively, in 1994-95) the water and sewerage charges appear to have been used as a mechanism to generate additional revenue from ratepayers in the past.

**3.5.102** With a planned return on equity of 28 percent for 1995-96 it appears that the Government intends to continue with this approach in the future. **This significant return on equity is likely to result in higher prices for customers.**



□ **RESPONSE** provided by Secretary, Department of Treasury and Finance

*The use of return on equity (ROE) and comparisons with the Hunter Water Corporation and Sydney Water Board are inappropriate. ROE is a largely irrelevant measure for the retailers whose equity is derived from net assets at disaggregation and does not reflect market driven positions and historical reinvestment in business. Given the MWC paid major portions of its net profit after tax in dividends to government prior to disaggregation, this distorts the ROE of both the retailers and Melbourne Water, post disaggregation.*

*The Hunter Water Corporation and the Sydney Water Board revalue their assets at replacement cost for ratio calculation purposes. This increases the equity figure in the balance sheet (Asset Revaluation Reserve) and yields a low return figure for ratio purposes.*

**Disaggregation process**

*Asset write-offs*

**3.5.103** The Auditor-General's May 1995 *Report on Ministerial Portfolios* referred to the write-off of development costs on information technology (IT) assets amounting to \$17.5 million on an integrated customer billing system known as "Customlink".

**3.5.104** In 1994-95, the Corporation and the retail companies wrote-off a further \$13.2 million and \$23.9 million in assets, respectively, resulting in a total write-off of \$54.6 million over the last 2 years. These asset write-offs are outlined in Table 3.5H.

**TABLE 3.5H**  
**1994-95 ASSET WRITE-OFFS**  
((\$million))

| <i>Entity</i>      | <i>IT</i>   | <i>Other</i> | <i>Total</i> |
|--------------------|-------------|--------------|--------------|
| Melbourne Water    | 4.2         | 9.0          | 13.2         |
| South East Water   | 2.6         | 8.7          | 11.3         |
| Yarra Valley Water | 5.1         | -            | 5.1          |
| City West Water    | 4.0         | 3.5          | 7.5          |
| <b>Total</b>       | <b>15.9</b> | <b>21.2</b>  | <b>37.1</b>  |

**3.5.105** In addition, it is envisaged that a further \$20 million of IT development expenditure, previously capitalised, will be written-off in the 1995-96 year due to the introduction of new systems at the Corporation and the retail water companies.

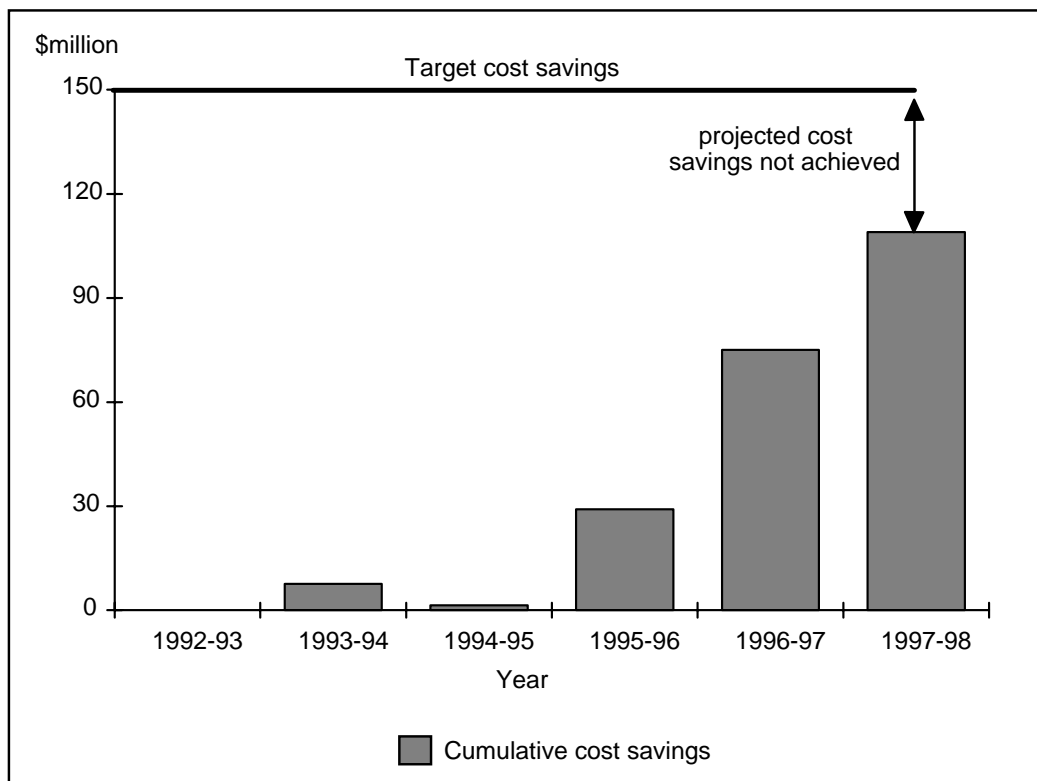
□ **RESPONSE** provided by Secretary, Department of Treasury and Finance

*The inclusion of write-offs for 1993-94, some of which precede disaggregation, is inappropriate.*

**Estimated savings from implementation of the reform program**

**3.5.106** The water industry reform document titled *Reforming Victoria's Water Industry: A Competitive Future, October 1993*, projected cost savings of \$150 million over the next 5 years, as a result of the reform process. Savings were to be achieved through a clearer focus on core activities, the introduction of an operating licence discipline and the competition generated by internal comparisons. However, details of the composition of these potential savings could not be provide to audit. In order to determine whether the target of \$150 million cost savings will be achieved, audit graphed the actual and projected combined operating costs of the Corporation and the retail water companies over a 5 year period. This information is shown in Chart 3.5I. From the chart it can be seen that the projected cost savings of the combined entities for a 5 year period 1992-93 is \$109 million, which is \$41 million (27 per cent) less than originally forecast. The achievement of the \$109 million is dependent on the accuracy of the forward expenditure estimates.

**CHART 3.5I  
ANALYSIS OF CUMULATIVE COST SAVINGS**



□ **RESPONSE** provided by Secretary, Department of Treasury and Finance

*This paragraph appears to criticise the reform program for not achieving the full \$150 million cost savings. Even if these costs savings are not realised, the currently projected \$109 million cost reduction would still be a considerable achievement. Calculations within DTF suggest that the \$150 million projected savings target will be achieved within 5 years from 1994-95 and may be realised within 3 years.*



**SCHEDULE A  
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS**

| <i>Report</i>                                                                                                | <i>Subject</i>                                                                                                                                                                                                    | <i>Status at date of preparation of this Report</i>                                                                                                                                                                                                                                                                             |
|--------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>MATTERS RESOLVED OR ACTION COMMENCED</b>                                                                  |                                                                                                                                                                                                                   |                                                                                                                                                                                                                                                                                                                                 |
| <b>DEPARTMENT OF NATURAL RESOURCES AND THE ENVIRONMENT</b>                                                   |                                                                                                                                                                                                                   |                                                                                                                                                                                                                                                                                                                                 |
| <i>Second Reports, 1985-86 and 1986-87. Ministerial Portfolios, May 1989, pp. 45-6. May 1990, pp. 68-70.</i> | Deficiencies in the debtors/revenue collection system. Potential interest forgone.                                                                                                                                | Although a high priority has been placed on debt recovery, there is still scope to improve the management of debtors.                                                                                                                                                                                                           |
| <b>ENVIRONMENT PROTECTION AUTHORITY</b>                                                                      |                                                                                                                                                                                                                   |                                                                                                                                                                                                                                                                                                                                 |
| <i>Ministerial Portfolios, April 1991, pp. 59-60.</i>                                                        | The Authority needs to extend its role into the areas of environment protection and pollution prevention to more adequately fulfil its role.                                                                      | Self-monitoring by industry is complemented by EPA enforcement action.                                                                                                                                                                                                                                                          |
| <b>MELBOURNE WATER CORPORATION</b>                                                                           |                                                                                                                                                                                                                   |                                                                                                                                                                                                                                                                                                                                 |
| <i>Ministerial Portfolios, April 1993, pp. 90-1.</i>                                                         | The delay and subsequent breakdown in negotiations on the joint venture relating to the Braeside Park project resulted in substantial costs to the Corporation and a delay in disposal of the property.           | The Corporation is in the process of subdividing the property (now known as Woodlands Industrial Estate) which will be sold in 5 or 6 stages. The Corporation has completed the sale of lots in stage 1 and 60 per cent of lots in stage 2. The Board of Management of the Corporation has approved the development of stage 3. |
| <b>ROYAL BOTANIC GARDENS BOARD</b>                                                                           |                                                                                                                                                                                                                   |                                                                                                                                                                                                                                                                                                                                 |
| <i>Ministerial Portfolios, May 1994, pp. 136-46.</i>                                                         | Agreement with the Government is required on the future level of funding to be provided to the Board.<br><br>Action is required to ensure adequate registration and storage of the National Herbarium collection. | While there has been no agreement yet reached, funding has been addressed in the Board's business plan covering the period 1997 to 1999.<br><br>Plans developed to address backlog in registration. Funding requirements included in the Board's business plan.                                                                 |
| <b>VICTORIAN INSTITUTE OF MARINE SCIENCES</b>                                                                |                                                                                                                                                                                                                   |                                                                                                                                                                                                                                                                                                                                 |
| <i>Ministerial Portfolios, May 1994, pp. 151-3.</i>                                                          | To ensure the future financial viability of the Institute, action is required to implement effective management and financial policies, practices and information systems.                                        | The Institute is to amalgamate in 1996 with the Victorian Fisheries Research Institute to form a new institute operating under the framework provided by existing legislation.                                                                                                                                                  |
| <i>Ministerial Portfolios, May 1994, pp. 154-5.</i>                                                          | Annual action plans, incorporating performance measures, should be developed and implemented as a means of supporting the Institute's strategic direction plan.                                                   | A strategic business plan is in preparation for the new institute formed upon amalgamation with the Victorian Fisheries Research Institute.                                                                                                                                                                                     |



**SCHEDULE A  
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS**

| <i>Report</i>                                                                                                    | <i>Subject</i>                                                                                                                                                                                                                                 | <i>Status at date of preparation of this Report</i> |
|------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------|
| <b>NO ACTION TAKEN</b>                                                                                           |                                                                                                                                                                                                                                                |                                                     |
| <b>ALPINE RESORTS COMMISSION</b>                                                                                 |                                                                                                                                                                                                                                                |                                                     |
| <i>Ministerial Portfolios, April 1992 p.408</i>                                                                  | There was an absence of appropriate performance measures which provide assurance to the Government that the Commission is meeting the aims of the Tourism strategy and fulfilling its role and objectives under its legislation.               | Position unchanged.                                 |
| <b>MELBOURNE WATER CORPORATION</b>                                                                               |                                                                                                                                                                                                                                                |                                                     |
| <i>Second Report, 1986-87, pp. 164-5<br/><br/>Ministerial Portfolios, May 1990, p. 343.<br/>May 1992, p. 432</i> | The enabling legislation does not confer on the Corporation the authority to levy interest on arrears of rates and charges. In contrast, the legislation of other major rating bodies provides for the levying of interest on overdue amounts. | Position unchanged.                                 |



**SCHEDULE B  
COMPLETED/INCOMPLETE AUDITS**

| <i>Entity</i>                                                  | <i>Financial year ended</i>        | <i>Reporting to Parliament</i>                        | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|----------------------------------------------------------------|------------------------------------|-------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS</b>                                        |                                    |                                                       |                                              |                                        |
| Department of Agriculture, Energy and Minerals(a)              | 30 June 1995                       | 31 Oct. <i>Financial Management Act 1994</i> , s.45.  | 29 Sept. 1995                                | 29 Sept. 1995                          |
| Department of Conservation and Natural Resources (b)           | 30 June 1995                       | " "                                                   | 3 Oct. 1995                                  | 26 Oct. 1995                           |
| <b>AGRICULTURE, ENERGY AND MINERALS</b>                        |                                    |                                                       |                                              |                                        |
| City West Water Ltd                                            | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 6 Sept. 1995                                 | 9 Sept. 1995                           |
| Daratech Pty Ltd                                               | 30 June 1995                       | 31 Oct. <i>Financial Management Act 1994</i> , s.53A. | 28 Sept. 1995                                | 20 Nov. 1995                           |
| Gippsland Rural Water Authority (d)                            | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 16 Oct. 1995                                 | 31 Oct. 1995                           |
| Goulburn Murray Rural Water Authority                          | 30 June 1995                       | " "                                                   | 21 Sept. 1995                                | 21 Sept. 1995                          |
| Grain Elevators Board (c)                                      | Period 1 Oct. 1994 to 30 June 1995 | " "                                                   | 9 Nov. 1995                                  | 9 Nov. 1995                            |
| Grain Elevators Board (c)                                      | Period 1 Oct. 1994 to 31 Dec. 1995 | 31 Mar. <i>Financial Management Act 1994</i> , s.46.  | 19 Dec. 1995                                 | 31 Jan. 1996                           |
| Melbourne Market Authority                                     | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 15 Aug. 1995                                 | 22 Sept. 1995                          |
| Melbourne Water Corporation                                    | 30 June 1995                       | " "                                                   | 18 Aug. 1995                                 | 18 Aug. 1995                           |
| Murray Valley Citrus Marketing Board                           | 30 June 1995                       | " "                                                   | 16 Oct. 1995                                 | 17 Oct. 1995                           |
| Murray Valley Wine Grape Industry Development Committee        | 31 July 1995                       | 31 Oct. <i>Financial Management Act 1994</i> , s.46.  | 1 Nov. 1995                                  | 22 Jan. 1995                           |
| Northern Victorian Fresh Tomato Industry Development Committee | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 16 Oct. 1995                                 | 26 Oct. 1995                           |
| Radius Computing Pty Ltd                                       | 9 June 1994 - 30 June 1995         | No reporting requirements.                            | 15 Sept. 1995                                | 18 Sept. 1995                          |

**SCHEDULE B  
COMPLETED/INCOMPLETE AUDITS**

| <i>Entity</i>                                       | <i>Financial year ended</i>        | <i>Reporting to Parliament</i>                                           | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|-----------------------------------------------------|------------------------------------|--------------------------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS - continued</b>                 |                                    |                                                                          |                                              |                                        |
| <b>AGRICULTURE, ENERGY AND MINERALS cont.</b>       |                                    |                                                                          |                                              |                                        |
| Rural Water Corporation                             | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46.                    | 5 Dec. 1995                                  | 12 Dec. 1995                           |
| South East Water Ltd                                | 30 June 1995                       | " "                                                                      | 25 Sept. 1995                                | 25 Sept. 1995                          |
| Southern Rural Water Authority (d)                  | 30 June 1995                       | " "                                                                      | 29 Sept. 1995                                | 29 Sept. 1995                          |
| Sunraysia Rural Water Authority                     | 30 June 1995                       | " "                                                                      | 10 October 1995                              | 24 October 1995                        |
| Veterinary Board of Victoria                        | 31 Dec. 1995                       | 31 Mar. <i>Financial Management Act 1994</i> , s.46.                     | 31 Mar. 1996                                 | 11 Apr. 1996                           |
| Victorian Dairy Industry Authority                  | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46.                    | 4 Sept. 1995                                 | 10 Oct. 1995                           |
| Victorian Dried Fruits Board                        | Period 1 Jan. 1995 to 30 June 1995 | " "                                                                      | 31 Oct. 1995                                 | 9 Nov. 1995                            |
| Victorian Institute of Marine Sciences              | 31 Dec. 1994                       | 31 March. <i>Victorian Institute of Marine Sciences Act 1974</i> , s.26. | 24 Aug. 1995                                 | 6 Oct. 1995                            |
| Victorian Institute of Marine Sciences              | 1 Jan. 1995 to 30 June 1995        | 30 Sept. <i>Financial Management Act 1994</i> , s.46                     | 15 Sept. 1995                                | 11 Oct. 1995                           |
| Victorian Meat Authority                            | 30 June 1995                       | " "                                                                      | 7 Sept. 1995                                 | 8 Sept. 1995                           |
| Victorian Plantations Corporation                   | 30 June 1995                       | " "                                                                      | 6 Sept. 1995                                 | 8 Sept. 1995                           |
| Victorian Strawberry Industry Development Committee | 30 June 1995                       | " "                                                                      | 6 Nov. 1995                                  | 9 Nov. 1995                            |
| Water Training Centre                               | 30 June 1995                       | " "                                                                      | 26 Sept. 1995                                | 29 Sept. 1995                          |
| Wimmera Malley Rural Water Authority                | 30 June 1995                       | " "                                                                      | 7 Sept. 1995                                 | 29 Sept. 1995                          |
| Yarra Valley Water Ltd                              | 30 June 1995                       | " "                                                                      | 25 Sept. 1995                                | 25 Sept. 1995                          |

**SCHEDULE B  
COMPLETED/INCOMPLETE AUDITS**

| <i>Entity</i>                                              | <i>Financial year ended</i> | <i>Reporting to Parliament</i>                                                                                 | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|------------------------------------------------------------|-----------------------------|----------------------------------------------------------------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS - continued</b>                        |                             |                                                                                                                |                                              |                                        |
| <b>CONSERVATION AND NATURAL RESOURCES</b>                  |                             |                                                                                                                |                                              |                                        |
| Alpine Resorts Commission                                  | 31 Oct. 1994                | 31 Jan. <i>Annual Reporting Act 1983, s.9.</i>                                                                 | 29 Dec. 1994                                 | 30 Dec 1994                            |
| Bundoora Park Committee of Management                      | 30 June 1994                | No reporting requirements <i>Crown Land (Reserves) Act 1978, s.15.</i> provides for the audit of the Accounts. | 21 June 1995                                 | 16 Oct. 1995                           |
| Environment Protection Authority                           | 30 June 1995                | " "                                                                                                            | 29 Sept. 1995                                | 29 Sept. 1995                          |
| Melbourne Water Corporation Employees' Superannuation Fund | 30 June 1995                | " "                                                                                                            | 28 Aug. 1995                                 | 28 Aug. 1995                           |
| Northern Regional Refuse Disposal Group                    | 30 June 1995                | " "                                                                                                            | 28 Nov. 1995                                 | 11 Dec. 1995                           |
| Olympic Park Committee of Management ( <i>h</i> )          | 30 June 1995                | " "                                                                                                            | 27 Oct. 1995                                 | 30 Oct. 1995                           |
| Penguin Reserve Committee of Management                    | 30 June 1995                | " "                                                                                                            | 3 Nov. 1995                                  | 16 Nov. 1995                           |
| Recycling and Resource Recovery Council                    | 30 June 1995                | " "                                                                                                            | 14 Sept. 1995                                | 18 Sept. 1995                          |
| Royal Botanic Gardens Board                                | 30 June 1995                | " "                                                                                                            | 6 Sept. 1995                                 | 8 Sept. 1995                           |
| South Eastern Regional Waste Management Group              | 30 June 1995                | " "                                                                                                            | 7 Dec. 1995                                  | 7 Feb. 1996                            |
| State Swimming Centre Committee of Management              | 30 June 1994                | " "                                                                                                            | 16 Feb. 1996                                 | 29 Feb. 1996                           |
| Surveyors Board of Victoria                                | 30 June 1995                | 30 Sept. <i>Financial Management Act 1994, s.46.</i>                                                           | 8 Aug. 1995                                  | 15 Aug. 1995                           |
| Victorian Conservation Trust                               | 30 June 1995                | " "                                                                                                            | 25 Sept. 1995                                | 29 Sept. 1995                          |
| Water EcoScience Pty Ltd                                   | 2 May 1994 - 30 June 1995   | No reporting requirements. Audit conducted at request of Treasurer and under the Corporations Law.             | 6 Sept. 1995                                 | 8 Sept. 1995                           |
| Waste Management Council                                   | 30 June 1995                | 30 Sept. <i>Financial Management Act 1994, s.46</i>                                                            | 25 Sept. 1995                                | 26 Oct. 1995                           |
| Western Regional Waste Management Group                    | 30 June 1995                | " "                                                                                                            | 18 Jan. 1996                                 | 13 Feb. 1996                           |

**SCHEDULE B  
COMPLETED/INCOMPLETE AUDITS**

| <i>Entity</i>                                                  | <i>Financial year ended</i>                                          | <i>Reporting to Parliament</i>                                                                                           | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|----------------------------------------------------------------|----------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS - continued</b>                            |                                                                      |                                                                                                                          |                                              |                                        |
| <b>CONSERVATION AND NATURAL RESOURCES - continued</b>          |                                                                      |                                                                                                                          |                                              |                                        |
| Yarra Bend Park Trust                                          | 30 June 1995                                                         | 30 Sept. <i>Financial Management Act 1994</i> , s.46                                                                     | 27 Oct. 1995                                 | 30 Oct. 1995                           |
| Zoological Board of Victoria                                   | 30 June 1995                                                         | " "                                                                                                                      | 24 Aug. 1995                                 | 18 Sept. 1995                          |
| Zoological Board of Victoria Superannuation Fund               | 30 June 1994                                                         | No reporting requirements. Audit conducted at request of Treasurer.                                                      | 18 May. 1995                                 | 18 May. 1995                           |
| Zoological Board of Victoria Superannuation Fund               | 30 June 1995                                                         | 30 Sept. <i>Financial Management Act 1994</i> , s.46                                                                     | 24 Oct. 1995                                 | 31 Oct. 1995                           |
| <b>INCOMPLETE AUDITS</b>                                       |                                                                      |                                                                                                                          |                                              |                                        |
| <b>AGRICULTURE, ENERGY AND MINERALS</b>                        |                                                                      |                                                                                                                          |                                              |                                        |
| Victorian Institute of Marine Sciences Superannuation Fund (e) | 30 June 1989 and 30 June 1990                                        | No reporting requirements. Audit conducted at request of Treasurer.                                                      | Audits substantially completed.              |                                        |
| <b>CONSERVATION AND NATURAL RESOURCES</b>                      |                                                                      |                                                                                                                          |                                              |                                        |
| Bairnsdale Waste Management Group                              | 30 June 1995                                                         | 30 Sept. <i>Financial Management Act 1994</i> , s.46                                                                     | Audit substantially completed.               |                                        |
| Bundoora Park Committee of Management (f)                      | 30 June 1995                                                         | 30 Sept. <i>Financial Management Act 1994</i> , s.46                                                                     | Audit substantially completed.               |                                        |
| Eastern Regional Waste Management Group                        | 30 June 1995                                                         | " "                                                                                                                      | Audit substantially completed.               |                                        |
| Mount Macedon Memorial Cross Committee of Management (g)       | 31 Dec. 1992, 31 Dec. 1993, 31 Dec. 1994 and 1 Jan. to 18 April 1995 | No reporting requirements. Audit conducted at request of Treasurer.                                                      | Audits substantially completed.              |                                        |
| Port Bellarine Committee of Management                         | 30 Sept. 1994                                                        | No reporting requirements. <i>Port Bellarine Tourist Reserve Act 1981</i> , s.21 provides for the audit of the accounts. | Audit substantially completed.               |                                        |



**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                         | <i>Financial<br/>year<br/>ended</i> | <i>Reporting to Parliament</i>                                          | <i>Financial<br/>statements<br/>signed by<br/>entity</i> | <i>Auditor-<br/>General's<br/>report<br/>signed</i> |
|-------------------------------------------------------|-------------------------------------|-------------------------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------------|
| <b>INCOMPLETE AUDITS - continued</b>                  |                                     |                                                                         |                                                          |                                                     |
| <b>CONSERVATION AND NATURAL RESOURCES - continued</b> |                                     |                                                                         |                                                          |                                                     |
| Port Bellarine Committee of Management                | 30 June 1995                        | 30 Sept. <i>Financial Management Act</i> 1994, s.46                     | Financial statements not received.                       |                                                     |
| Shrine of Remembrance Trustees                        | 30 June 1994                        | No reporting requirements. Audit conducted at request of the Treasurer. | Audit substantially completed.                           |                                                     |
| State Swimming Centre Committee of Management         | 30 June 1995                        | 30 Sept. <i>Financial Management Act</i> 1994, s.46                     | Financial statements not yet received from Committee.    |                                                     |

- (a) The Ministry of the Department of Agriculture, Energy and Minerals was absorbed into the Department of Natural Resources and the Environment.
- (b) The Department of Conservation and Natural Resources was absorbed into the Department of Natural Resources and the Environment.
- (c) The net assets of the Board were sold to VicGrain as at 30 June 1995. The Board was subsequently wound up as at 31 December 1995.
- (c) Ceased operations on 30 June 1995.
- (e) Ceased operations on 30 June 1990.
- (f) Ceased operations on 18 January 1996.
- (g) Ceased operations on 18 April 1995.
- (h) Ceased operations on 4 October 1995 and incorporated into the Melbourne and Olympic Parks Trust.

# Part 3.6

## Premier and Cabinet

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### KEY FINDINGS

#### EXECUTIVE SALARIES

- Executive officer contracts were generally entered into and administered in accordance with the guidelines issued by the Public Service Commissioner.  
*Paras 3.6.4 to 3.6.10*
- Payments of \$70 581 were made to a former senior public servant in excess of contract entitlements.  
*Paras 3.6.11 to 3.6.13*
- While certain public servants in the past have received approval to be members of non-Victorian public bodies, it is my opinion that only in extenuating circumstances should such appointments be approved and that government employees should not personally benefit from such arrangements.  
*Para. 3.6.14*
- In my view, the provision of a gift valued at \$9 500 to a senior public servant upon departure from the Victorian public service was extravagant.  
*Paras 3.6.15 to 3.6.16*
- Executive officer performance assessments were generally satisfactorily managed.  
*Paras 3.6.17 to 3.6.19*



**3.6.1** The Premier, who is also the Minister for Arts and Multicultural Affairs, has responsibility for operations within the Premier and Cabinet sector.

**3.6.2** Details of the specific ministerial responsibilities for agencies within the Premier and Cabinet sector are listed in Table 3.6A. These agencies, together with the Department of the Premier and Cabinet, were subject to audit during the 1994-95 financial year.

**TABLE 3.6A  
MINISTERIAL RESPONSIBILITY FOR  
PUBLIC SECTOR AGENCIES WITHIN THE PREMIER AND CABINET SECTOR**

| <i>Ministerial portfolio</i> | <i>Agencies subject to audit</i>                                                                                                                                                                                |
|------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Arts</b>                  | Council of the Museum of Victoria<br>Council of the State Library of Victoria<br>Council of Trustees of the National Gallery of Victoria<br>Geelong Performing Arts Centre Trust<br>Victorian Arts Centre Trust |
| <b>Multicultural Affairs</b> | Victorian Interpreting and Translation Service                                                                                                                                                                  |
| <b>Premier</b>               | Ombudsman, Office of the<br>Public Service Commissioner, Office of the<br>Victorian Auditor-General's Office<br>Victorian Relief Committee                                                                      |

**3.6.3** Comments on matters of significance arising from the audit of entities within the Premier and Cabinet sector is provided below.

**EXECUTIVE SALARIES**

**3.6.4** As a part of the Government's public sector reform program, a new structure for the employment of its executive officers within the public service was introduced in November 1992. The new structure provided for a movement away from tenured employment to the engagement by contract, for terms not exceeding 5 years. As part of the new structure, executive remuneration packaging was also introduced together with a performance incentive payment scheme, and the termination of tenure with a 4 week notice period. These changes were brought into effect by way of the *Public Sector Management Act* 1992. The key aim of the introduction of this initiative was to establish an employment structure that would attract, motivate, reward and retain high calibre executives as a corporate resource for the Government in the achievement of its objectives.

**3.6.5** At the time of implementation of the reforms, officers in the former Senior Executive Service were generally offered the option of entering into a contract of employment under the new arrangements, or remaining employed under their existing terms and conditions. Only a small number of executive officers elected not to enter into contracts under the new arrangements.

**3.6.6** The position of the Public Service Commissioner was established under the *Public Sector Management Act 1992* with responsibility, inter alia, for establishing guidelines relating to public sector employment and advising government on remuneration issues. The guidelines issued by the Public Service Commissioner include the provision of standard wording for contracts outlining the terms and conditions of employment which can be offered to executives. These terms and conditions include:

- periodic reviews of the performance of executive officers to be undertaken at least every 12 months;
- performance incentive payments to be made up to 20 per cent of the total remuneration package at the completion of the contract period based on the results of the periodic performance reviews; and
- the contract may be terminated by either party on giving 4 weeks notice, with neither party entitled to any compensation for such termination for any unexpired period of the contract, with the executive officer forfeiting any accrued performance pay.

**3.6.7** The Public Sector Management Act stipulates that remuneration packages payable under contracts can range from \$84 542 to \$297 500. However, the vast majority of executives are on remuneration packages at the lower end of this range.

**3.6.8** Since May 1995, executive officers have been grouped into 3 broad bands instead of the old 9 levels. The Premier has responsibility for authorising remuneration packages for individuals within level 1, which mainly comprises heads of organisations who are remunerated in excess of \$166 000. The authorisation of remuneration packages of executive positions within level 2 has been delegated to the Public Service Commissioner, with the Heads of Departments responsible for authorising remuneration packages within level 3 who are remunerated up to \$112 339.

**3.6.9** Audit conducted a review to ascertain whether executive officer contracts were entered into in accordance with government policy.

## Contract remuneration

**3.6.10** Audit found that executive officer contracts were generally entered into and administered in accordance with the guidelines issued by the Public Service Commissioner. However, **a number of exceptions** were identified, which included:

- cases where contracts had not been entered into and the respective officers received a remuneration package as if they had signed contracts;
- all pages and schedules of contracts were not signed or initialled, possibly exposing the employer in cases of contract dispute;
- one department awarded a general salary increase of 3 per cent to its executive officers while in all other departments no general remuneration increases had occurred; and
- while some departments had completed work value and remuneration assessments to promptly determine appropriate remuneration levels for executive officers in relation to the new 3 broad-banded structure, other departments had either not commenced, or were still in the process of, undertaking such assessments.





**3.6.11** However, the most serious exception identified during the review concerned payments made to a former senior public servant of \$70 581 in excess of contract entitlements. In this case, the officer served as a member of a board of a non-Victorian public body and received remuneration from the respective body for performing this role. Under the legislation establishing the particular public body, the officer was obligated to pay, within one month of receipt, the remuneration received from the body to the State. Audit identified that during the period June 1993 to April 1994, the officer paid to the State an amount of \$42 859 on account of remuneration received from the public body. In respect of the amount paid by the officer to the State, the officer directed the respective department to repay an amount equivalent to that received.

**3.6.12** However, at the date of audit in April 1996, no amount was received by the State for the period May 1994 to April 1995, although the officer remained a member of the board. In relation to the this period, audit requested the relevant Department to ascertain whether any amounts were due to the State on account of board fees that may have been received by the officer. Following the department's inquires, the officer paid to the department in May 1996, an amount of \$27 722 which was received from the particular public body for the above period. In turn, the department immediately paid an equivalent amount back to the officer.

**3.6.13** The amount covering both periods of \$70 581 was in excess of the remuneration payable under the executive officer's contract of employment.

**3.6.14** This matter raises the more general issue of public servants being members of boards of non-Victorian public bodies and receiving remuneration for such services. **While I am aware that certain public servants in the past have received approval to be members of such boards, it is my opinion that only in extenuating circumstances should such appointments be approved and that government employees should not personally benefit from such arrangements.** This would be consistent with current government policy in relation to public servants serving on boards of Victorian public bodies.

**□ RESPONSE** by Secretary Department of Premier and Cabinet

*You raised the question of the fact that public servants are members of other bodies and expressed the view that approval for this should only occur in "extenuating circumstances".*

*I have discussed your opinion with the Premier. Neither the Premier nor I share that view. The senior public servant was one of a very small number of public servants who were (and are) allowed to have outside appointments. It is likely that the practice will continue, but will be limited. The Premier also believes that there will always be circumstances in which it will be appropriate for senior Victorian public servants both to use their expertise and to gain experience in outside bodies.*

*The Premier approved the senior public servant continuing appointment to the relevant public body before joining the Victorian public service. He believes that this approval was essential in securing the senior public servant's services.*

*The Premier believes that it is, and will remain, a matter for him as to whether public servants serve on non-Victorian public bodies and whether they are able to keep their remuneration as a result.*

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## Gift to senior public servant

**3.6.15** During the course of an audit examination of departmental expenditure vouchers, audit identified the purchase of a painting in April 1995 for an amount of \$9 500 which was provided as a gift to a senior public servant upon departure from the Victorian public service. The senior public servant resigned prior to the end of the term of the contract of employment, thus forfeiting any accrued performance pay.

**3.6.16** **In my view, the provision of this gift valued at \$9 500 was extravagant.**

*□ RESPONSE by Secretary Department of Premier and Cabinet*

*The gift was in lieu of a bonus. While the contract provided that the bonus not be payable until the end of the contract period, the Premier is of the view that it was an entirely appropriate gift given the bonuses forgone (over \$150 000) and the very significant savings achieved by the senior public servant during 2½ years of employment in Victoria and the contribution made to the reform of the public sector generally.*

## Performance assessments

**3.6.17** As indicated previously, a key element of the revised senior executive employment structure is the performance incentive payment scheme. This scheme provides the sole basis for recognising and remunerating performance of executive officers. In accordance with government policy, an amount of up to 20 per cent of the executive officer's remuneration package may be payable based on annual performance assessments, with the amount actually paid at the end of the contract period. However, if an executive officer resigns prior to the end of the contract period the amount accrued in performance pay is forfeited.

**3.6.18** The review found that, generally, performance assessments were managed in a satisfactory manner, but the following isolated exceptions were identified across various departments:

- criteria had not been established for executive officer positions against which performance could be assessed;
- performance assessments did not address the relevant criteria stipulated in the performance plan;
- incorrect calculation of performance incentive payments; and
- performance assessments were not undertaken in a timely manner.

**3.6.19** **The above matters have been raised with the Public Service Commissioner who intends to address the specific issues with departments after publication of this Report, with a view to providing further guidance in the *Executive Officer Handbook* as appropriate.**



□ **RESPONSE** from the Secretary Department of Premier and Cabinet

*The other comments in relation to minor matters about executive contracts have been noted and I will ensure that your Report is brought to the attention of Secretaries when tabled.*

□ **RESPONSE** by the Public Service Commissioner

*I am pleased to note your finding that executive officer contracts are generally being administered in accordance with guidelines established by this Office. Once your Report is published, I believe it will provide a useful basis for me to discuss executive officer contract administration with Department Heads.*

**SCHEDULE A  
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS**

| Report                                            | Subject                                                                                                                                                                                                                                                         | Status at date of preparation of this Report                                                                                                                                                                                                        |
|---------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>MATTERS RESOLVED OR ACTION COMMENCED</b>       |                                                                                                                                                                                                                                                                 |                                                                                                                                                                                                                                                     |
| <b>VICTORIAN ARTS CENTRE TRUST</b>                |                                                                                                                                                                                                                                                                 |                                                                                                                                                                                                                                                     |
| <i>Ministerial Portfolios, May 1994, pp.58-9.</i> | A long standing policy of non-allocation of significant levels of indirect overhead expenses (almost \$10 million in 1992-93) to individual operating units has impeded decision-making and led to incomplete transparency of accountability to the Parliament. | The Trust has allocated indirect overhead expenses to operating units in its <i>internal</i> audit reports. However, the allocation of indirect overhead expenses within the annual financial statements of the Trust is still under consideration. |
| <i>Ministerial Portfolios, May 1994, pp.68-9.</i> | Since 1987, the Trust has pursued legal action to recover damages against a number of contractors and consultants over defects in the Arts Centre spire.                                                                                                        | While considerable progress had been made by the Trust to determine the extent and cause of damage to the spire, at the date of preparation of this Report, court proceedings had not commenced.                                                    |

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**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS**

| <i>Entity</i>                                           | <i>Financial<br/>year<br/>ended</i> | <i>Reporting to Parliament</i>                        | <i>Financial<br/>statements<br/>signed by<br/>entity</i> | <i>Auditor-<br/>General's<br/>report<br/>signed</i> |
|---------------------------------------------------------|-------------------------------------|-------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------------|
| <b>COMPLETED AUDITS</b>                                 |                                     |                                                       |                                                          |                                                     |
| Department of the Premier and Cabinet                   | 30 June 1995                        | 31 Oct. <i>Financial Management Act 1994</i> , s.45.  | 31 Oct. 1995                                             | 31 Oct. 1995                                        |
| <b>ARTS</b>                                             |                                     |                                                       |                                                          |                                                     |
| Council of the Museum of Victoria                       | 30 June 1995                        | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 29 Sept. 1995                                            | 29 Sept. 1995 (a)                                   |
| Council of the State Library of Victoria                | 30 June 1995                        | " "                                                   | 29 Sept. 1995                                            | 29 Sept. 1995(a)                                    |
| Council of Trustees of the National Gallery of Victoria | 30 June 1995                        | " "                                                   | 30 Sept. 1995                                            | 30 Sept. 1995(a)                                    |
| Geelong Performing Arts Centre Trust                    | 30 June 1995                        | " "                                                   | 29 Sept. 1995                                            | 29 Sept. 1995                                       |
| Victorian Arts Centre Trust                             | 30 June 1995                        | " "                                                   | 29 Sept. 1995                                            | 29 Sept. 1995                                       |
| <b>MULTICULTURAL AFFAIRS</b>                            |                                     |                                                       |                                                          |                                                     |
| Victorian Interpreting and Translation Service          | 30 June 1995                        | " "                                                   | 29 Sept. 1995                                            | 29 Sept. 1995                                       |
| <b>PREMIER</b>                                          |                                     |                                                       |                                                          |                                                     |
| Office of the Ombudsman                                 | 30 June 1995                        | 31 Oct. <i>Financial Management Act 1994</i> , s.45.  | 17 Oct. 1995                                             | 26 Oct. 1995                                        |
| Office of the Public Service Commissioner               | 30 June 1995                        | " "                                                   | 25 Oct. 1995                                             | 27 Oct. 1995                                        |
| Victorian Auditor-General's Office (b)                  | 30 June 1995                        | " "                                                   | 10 Oct. 1995                                             | 10 Oct. 1995                                        |
| Victorian Relief Committee                              | 30 June 1995                        | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 29 Sept. 1995                                            | 29 Sept. 1995                                       |

(a) Qualified audit report issued.

(b) The Victorian Auditor-General's Office was audited by a firm of private auditors.

# Part 3.7

## State Development

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### KEY FINDING

- The audit of the entities within the portfolio proved satisfactory.



**3.7.1** The Minister for Industry, Science and Technology, the Minister for Multimedia, the Minister for Rural Development, the Minister for Small Business, the Minister for Sport and the Minister for Tourism, have responsibility for operations within the State Development sector. These Ministers have collective responsibility for the Department of State Development.

**3.7.2** Details of the specific ministerial responsibilities for public bodies within the State Development sector are listed in Table 3.7A. These public bodies, together with the former Departments of Arts, Sport and Tourism, and Business and Employment were subject to audit by the Auditor-General during 1994-95 financial year.

**TABLE 3.7A  
MINISTERIAL RESPONSIBILITIES FOR  
PUBLIC BODIES WITHIN THE STATE DEVELOPMENT**

| <i>Ministerial portfolio</i>            | <i>Entities subject to audit</i>                                                                                                                                                                                                              |
|-----------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Industry, Science and Technology</b> | Construction Industry Long Service Leave Board<br>Exhibition Trustees (a)<br>Melbourne Exhibition Centre Trust<br>Overseas Projects Corporation of Victoria Ltd<br>Victorian Medical Consortium Pty Ltd                                       |
| <b>Multimedia</b>                       | Film Victoria<br>State Film Centre of Victoria Council                                                                                                                                                                                        |
| <b>Rural Development</b>                | Latrobe Regional Commission (b)                                                                                                                                                                                                               |
| <b>Small Business</b>                   | Liquor Licensing Commission<br>Small Business Development Corporation                                                                                                                                                                         |
| <b>Sport</b>                            | Greyhound Racing Control Board<br>Harness Racing Board<br>National Tennis Centre Trust (c)<br>National Tennis Centre Services Pty. Ltd.<br>Second Navinto Pty. Ltd.<br>Victorian Institute of Sport Ltd<br>Victorian Institute of Sport Trust |
| <b>Tourism</b>                          | Australian Grand Prix Corporation<br>Emerald Tourist Railway Board<br>Swan Hill Pioneer Settlement Authority (d)<br>Tourism Victoria                                                                                                          |

(a) Ceased operations on 31 March 1996.  
 (b) Ceased operations on 15 August 1995.  
 (c) Melbourne and Olympic Park's Trust was established on 5 October 1995, incorporating the former National Tennis Centre Trust and the Olympic Park Committee of Management.  
 (d) Ceased operations on 1 July 1994.

**3.7.3** The audit of entities within the portfolio proved satisfactory.

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**SCHEDULE A**  
**STATUS OF MATTERS RAISED IN PREVIOUS REPORTS**

| <i>Report</i>                                         | <i>Subject</i>                                                                                                                                                                                                                                                                                           | <i>Status at date of preparation of this Report</i>                                                                                                                                                                                                                                                                                                                   |
|-------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>MATTERS RESOLVED OR ACTION COMMENCED</b>           |                                                                                                                                                                                                                                                                                                          |                                                                                                                                                                                                                                                                                                                                                                       |
| <b>FORMER DEPARTMENT OF BUSINESS AND EMPLOYMENT</b>   |                                                                                                                                                                                                                                                                                                          |                                                                                                                                                                                                                                                                                                                                                                       |
| <i>Ministerial Portfolios, May 1994, p. 91.</i>       | The Occupational Health and Safety Authority's work place inspection program relating to targeted industries and activities was not based on a sound risk-based planning framework.                                                                                                                      | While the Authority is continuing to utilise its historically- based planning model, a new "site-assessment" targeting system is currently being piloted by the Authority with an expected implementation date of June 1996.                                                                                                                                          |
| <i>Ministerial Portfolios, May 1994, p. 93.</i>       | The Occupational Health and Safety Authority needs to ensure that material which provides guidance on workplace health and safety is made available to all employers.                                                                                                                                    | A review undertaken by the Authority has determined that it is not cost-effective to provide health and safety information to all employers.                                                                                                                                                                                                                          |
| <i>Ministerial Portfolios, May 1994, p. 96.</i>       | The Authority was not in a position to assess the adequacy of its inspectorial activities as it had not established benchmarks for the number of workplaces to be inspected to address risks within targeted industries.                                                                                 | The Authority has now implemented an annual target of 10 per cent of all employers to be contacted by way of site visits, provision of information or provision of advice.                                                                                                                                                                                            |
| <i>Ministerial Portfolios, May 1994, pp. 98-9.</i>    | Given the complementary activities of the Authority and the Victorian WorkCover Authority, a review should be undertaken to investigate the potential for the integration of the 2 bodies to form a single entity responsible for workplace injury prevention, compensation and employee rehabilitation. | A review of the integration of the Authority and the Victorian WorkCover Authority has not occurred. Audit was advised that such a review would only be undertaken at the directive of the Government.                                                                                                                                                                |
| <b>CONSTRUCTION INDUSTRY LONG SERVICE LEAVE BOARD</b> |                                                                                                                                                                                                                                                                                                          |                                                                                                                                                                                                                                                                                                                                                                       |
| <i>Ministerial Portfolios, May 1994, p. 101.</i>      | The level of surplus funds continued to increase even though employer contributions were waived in December 1993.                                                                                                                                                                                        | Since December 1993, the Construction Industry Long Service Leave Fund has continued to provide its services at no cost to the industry through a zero contribution rate. The impact of the zero contribution policy was evident in the 1994-95 financial year, with the Board recording an operating deficit of \$17 million and invested funds remaining unchanged. |

**SCHEDULE B  
COMPLETED/INCOMPLETE AUDITS**

| <i>Entity</i>                                  | <i>Financial<br/>year<br/>ended</i> | <i>Reporting to Parliament</i>                         | <i>Financial<br/>statements<br/>signed by<br/>entity</i> | <i>Auditor-<br/>General's<br/>report<br/>signed</i> |
|------------------------------------------------|-------------------------------------|--------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------------|
| <b>COMPLETED AUDITS</b>                        |                                     |                                                        |                                                          |                                                     |
| Department of Arts, Sport and Tourism          | 30 June 1995                        | 31 Oct. <i>Financial Management Act 1994</i> , s.45.   | 27 Oct. 1995                                             | 31 Oct. 1995                                        |
| Department of Business and Employment          | 30 June 1995                        | " "                                                    | 26 Sept. 1995                                            | 26 Sept. 1995                                       |
| <b>INDUSTRY, SCIENCE AND TECHNOLOGY</b>        |                                     |                                                        |                                                          |                                                     |
| Construction Industry Long Service Leave Board | 30 June 1995                        | 30 Sept. <i>Financial Management Act 1994</i> , s.46.  | 12 Sept. 1995                                            | 14 Sept. 1995                                       |
| Exhibition Trustees (b)                        | 31 Dec. 1995                        | 31 March. <i>Financial Management Act 1994</i> , s.46. | 29 Mar. 1996                                             | 29 Mar. 1996 (a)                                    |
| Melbourne Exhibition Centre Trust              | Period 18 Aug. 1994 to 30 June 1995 | 30 Sept. <i>Financial Management Act 1994</i> , s.46.  | 29 Sept. 1995                                            | 29 Sept. 1995                                       |
| Overseas Projects Corporation of Victoria Ltd  | 30 June 1995                        | 31 Oct. <i>Financial Management Act 1994</i> , s.53A.  | 25 Sept. 1995                                            | 13 Nov. 1995                                        |
| Victorian Medical Consortium Pty Ltd           | 30 June 1995                        | " "                                                    | 27 Sept. 1995                                            | 12 Oct. 1995                                        |
| <b>MULTIMEDIA</b>                              |                                     |                                                        |                                                          |                                                     |
| Film Victoria                                  | 30 June 1995                        | 30 Sept. <i>Financial Management Act 1994</i> , s.46.  | 19 Aug. 1995                                             | 30 Sept. 1995                                       |
| State Film Centre of Victoria Council          | 30 June 1995                        | " "                                                    | 9 Oct. 1995                                              | 12 Oct. 1995 (a)                                    |
| <b>RURAL DEVELOPMENT</b>                       |                                     |                                                        |                                                          |                                                     |
| Latrobe Regional Commission (c)                | Period 1 July 1994 to 15 Aug. 1995  | 15 Nov. <i>Financial Management Act 1994</i> , s.46.   | 15 Nov. 1995                                             | 15 Nov. 1995                                        |
| <b>SMALL BUSINESS</b>                          |                                     |                                                        |                                                          |                                                     |
| Liquor Licensing Commission                    | 30 June 1995                        | 30 Sept. <i>Financial Management Act 1994</i> , s.46.  | 28 Sept. 1995                                            | 29 Sept. 1995                                       |
| Small Business Development Corporation         | 30 June 1995                        | " "                                                    | 15 Sept. 1995                                            | 18 Sept. 1995                                       |



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**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                            | <i>Financial year ended</i>  | <i>Reporting to Parliament</i>                        | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|------------------------------------------|------------------------------|-------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS - continued</b>      |                              |                                                       |                                              |                                        |
| <b>SPORT</b>                             |                              |                                                       |                                              |                                        |
| Greyhound Racing Control Board           | 1 Aug. 1994 to 30 June 1995  | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 21 Sept. 1995                                | 29 Sept. 1995                          |
| Harness Racing Board                     | 1 Aug. 1994 to 30 June 1995  | " "                                                   | 29 Sept. 1995                                | 30 Oct. 1995                           |
| National Tennis Centre Trust (d)         | 30 June 1995                 | " "                                                   | 4 Oct. 1995                                  | 31 Oct. 1995                           |
| National Tennis Centre Service Pty. Ltd. | 30 June 1995                 | No reporting requirement.                             | 19 Sept. 1995                                | 31 Oct. 1995 (a)                       |
| Second Navinto Pty. Ltd.                 | 30 June 1995                 | " "                                                   | 19 Sept. 1995                                | 31 Oct. 1995 (a)                       |
| Victorian Institute of Sport Ltd         | 30 June 1995                 | 31 Oct. <i>Financial Management Act 1994</i> , s.53A. | 20 Oct. 1995                                 | 26 Oct. 1995                           |
| Victorian Institute of Sport Trust       | 30 June 1995                 | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 20 Oct. 1995                                 | 26 Oct. 1995                           |
| <b>TOURISM</b>                           |                              |                                                       |                                              |                                        |
| Australia Grand Prix Corporation         | 25 Oct. 1994 to 30 June 1995 | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 26 Sept. 1995                                | 28 Sept. 1995                          |
| Emerald Tourist Railway Board            | 30 June 1995                 | " "                                                   | 7 Sept. 1995                                 | 29 Sept. 1995                          |
| Swan Hill Pioneer Settlement Authority   | 30 June 1992                 | 30 Sept. <i>Annual Reporting Act 1983</i> , s.9.      | 11 Jan. 1996                                 | 31 Jan. 1996 (e)                       |
| " "                                      | 30 June 1993                 | " "                                                   | 11 Jan. 1996                                 | 31 Jan. 1996 (e)                       |
| " "                                      | 30 June 1994                 | " "                                                   | 11 Jan. 1996                                 | 31 Jan. 1996 (e)                       |
| Tourism Victoria                         | 30 June 1995                 | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 27 Sept. 1995                                | 30 Sept. 1995                          |

(a) Qualified audit report issued.

(b) Ceased operations on 31 March 1996.

(c) Ceased operations on 15 August 1995.

(d) Incorporated into Melbourne and Olympic Park's Trust effective from 5 October 1995.

(e) Ceased operations on 1 July 1994.

# Part 3.8

## Treasury and Finance

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**KEY FINDINGS**

**Gas industry reform in Victoria**

- The aggregate costs incurred by the State on the gas industry reform process to 31 March 1996 were around \$11 million.  
*Paras 3.8.4 to 3.8.9*
- On the split-up of the Gas and Fuel Corporation of Victoria, net liabilities of \$54.4 million, together with certain other substantial contingent liabilities, were not allocated to the newly established gas entities but were transferred to the State Electricity Commission of Victoria.  
*Paras 3.8.10 to 3.8.27*
- While GASCOR expects to achieve savings by outsourcing its mains and services function, it has retained significant obligations and exposures under the established arrangements.  
*Paras 3.8.28 to 3.8.32*

**Victorian electricity industry privatisation**

- The processes followed for the sale of the 5 distribution businesses were appropriate to ensure that the best available result was achieved by the State, with fair and equitable treatment accorded to all bidding parties.  
*Paras 3.8.39 to 3.8.65*
- Under the arrangements established for the sale of the distribution companies, the State is to receive total proceeds of \$8.4 billion, not including franchise fees.  
*Paras 3.8.66 to 3.8.71*
- The estimated cost directly incurred by the State in relation to these sales was in the order of \$40 million, with further indirect costs relating to electricity privatisation of \$5 million.  
*Para 3.8.69*



**KEY FINDINGS - continued**

**Victorian electricity industry privatisation- continued**

- The net benefit to the State from the sale of the 5 distribution companies is around \$4.1 billion. *Paras 3.8.67 to 3.8.69*
- Based on established projections, the sale of the distribution companies will result in a positive cashflow to the State over future years, given that the projected interest savings from the repayment of public sector debt will more than off-set the revenue forgone from dividends and State equivalent taxes. This ongoing net saving is estimated to be around \$350 million a year. *Paras 3.8.81 to 3.8.83*
- Under the sale arrangements, the State has provided certain indemnities and warranties to the purchasers, and has retained certain financial obligations, which may expose the State to future liability and cost. One of these liabilities relates to an agreement by the State to ultimately bear the financial costs of the companies' sales tax obligations estimated at \$35 million a year. *Paras 3.8.84 to 3.8.98*

**Final audit of United Energy Ltd**

- A qualified audit opinion was issued under the *Audit Act* 1994 by the Auditor-General on the financial statements of United Energy Ltd. for the period ended 30 June 1995. *Para 3.8.106*
- The financial statements of United Energy Ltd. for the period ended 30 June 1995 do not reflect the reality of its financial activities and position due to the inappropriate inclusion by the company after its sale of provisions and related expenditure totalling \$70.9 million. Had this amount not been provided for, the company would have reported an operating profit after tax of \$44.9 million. *Paras 3.8.107 to 3.8.127*
- The company was able to obtain a confirming audit opinion under the Corporations Law only after taking action to remove the Auditor-General as Corporations Law auditor at the time when the company was aware that its financial statements were likely to be qualified. *Paras 3.8.122 to 3.8.126*
- Difficulties will be experienced by the users of the company's financial statements, given that they are accompanied by 2 audit opinions, i.e. a confirming audit opinion issued under the Corporations Law and a heavily qualified audit opinion issued under the *Audit Act* 1994. *Para 3.8.127*

**Victorian Funds Management Corporation**

- The failure of the Corporation to attract the majority of public sector investment funds into its pooled trust products has meant that the expected benefits to the State from the Corporation's establishment, of between \$16 million and \$24 million a year, have not been realised. *Paras 3.8.128 to 3.8.134*

**KEY FINDINGS** - *continued***Victorian Funds Management Corporation** - *continued*

- The lack of a detailed understanding of client needs and expectations at the inception of the Corporation, together with delays in the development of appropriate investment products and an associated marketing strategy, were significant factors adversely impacting on the ability of the Corporation to attract new clients.

*Paras 3.8.136 to 3.8.149*

- Since the restructure of the Corporation's Board in November 1995, various initiatives have been commenced to establish appropriate products and structures for the Corporation. The effective implementation of these initiatives will be vital to the ongoing viability of the Corporation and to the achievement of cost-efficiencies to the public sector from centralised funds management.

*Paras 3.8.157 to 3.8.166***Utilisation of property**

- The Victorian Government Property Group of the Department of Treasury and Finance manages 56 State properties and 121 leased properties with an annual rental value of \$105 million, mainly located in the Melbourne central business district.

*Para 3.8.178*

- While the Property Group has prepared a strategic plan for the management of the State's leased and owned accommodation in the central business district and city fringe, the plan does not incorporate a costed long-term preventative maintenance program to ensure that recently renovated State properties do not again fall into disrepair and that other State properties do not continue to deteriorate.

*Paras 3.8.185 to 3.8.190*

- While the condition of some Treasury Reserve properties has been improved by recent renovation works, significant future funding allocations are still required to arrest ongoing deterioration and to enable further improvement in property utilisation.

*Para 3.8.220*

- There has been a substantial deterioration in the average space allocation per public servant since the last audit review in 1990, indicating continuing inefficient utilisation of accommodation.

*Paras 3.8.193 to 3.8.197*

- Even if key objectives contained in the Government's City Precinct Strategic Plan are realised by 1999, including a 36 per cent reduction in leased and owned accommodation space, the forecast average space allocation per public servant will still remain excessive.

*Paras 3.8.193 to 3.8.198*

- The Property Group has not undertaken regular monitoring of public sector agencies' property utilisation, putting at risk the realisation of forecasted rental savings and the efficient and effective utilisation of accommodation.

*Paras 3.8.204 to 3.8.209*



**KEY FINDINGS - continued**

**Utilisation of property - continued**

- Audit identified dead rent, i.e actual or imputed rent incurred on vacant accommodation space of a lettable size, amounting to \$12 million for the 18 month period to December 1995. *Paras 3.8.210 to 3.8.218*
- The annual opportunity cost of assets awaiting sale, under the Property Group's management, is approximately \$7.5 million. *Paras 3.8.232 to 3.8.242*

**Financial standing of WorkCover**

- When the Government announced the reforms to WorkCover, it anticipated that the Scheme would be fully funded within 5 years of its inception, i.e. it would have sufficient funds to fully cover all outstanding liabilities by December 1997. However, this milestone has been achieved by 30 June 1995, some 2½ years ahead of that anticipated. *Paras 3.8.256 to 3.8.260*
- The key reasons for the early achievement of the Scheme's fully-funded status included a change in the established entitlement criteria and benefit structure to compensate claimants for injuries sustained in the workplace, which effectively constrained compensation available to workers, the introduction of premium incentives to reduce the number and severity of claims, and a change in the strategic management of the Scheme. *Paras 3.8.261 to 3.8.277*
- The enhanced performance of WorkCover has resulted in substantial benefits to employers through reduced premiums and the elimination of an additional surcharge that was previously levied to improve the Scheme's poor financial standing. *Paras 3.8.278 to 3.8.287*

**Utilisation of consultants in the public sector**

- Given that some agencies did not comply with the annual reporting requirements relating to consultancy services, it is important that action be taken by the Department of Treasury and Finance to reinforce the reporting requirements and therefore improve disclosure to the Parliament in future years. *Paras 3.8.295 to 3.8.297*

**Amendment to the Casino licence**

- The Government allowed Crown Casino Ltd to increase the number of gaming tables at the new Casino from 200 to 350 for an additional licence fee of \$85 million. *Paras 3.8.303 to 3.8.320*
- The Department estimated that the additional profits over and above a return on investment to Crown from the additional 150 tables was between \$194 million and \$259 million (in present value terms), prior to the payment of the additional licence fee. However, there was inadequate support provided to audit for the Department's decision for Crown to retain any of these monopoly profits. *Paras 3.8.321 to 3.8.324*

**3.8.1** The Treasurer and Ministers for Finance and Gaming have responsibility for operations within the Treasury and Finance sector. These Ministers have collective responsibility for the Department of Treasury and Finance.

**3.8.2** Details of the specific ministerial responsibility for public bodies within the Treasury and Finance sector are listed in Table 3.8A. These public bodies, together with the Department of Treasury and Finance were subject to audit by the Auditor-General during the 1994-95 financial year.

**TABLE 3.8A  
MINISTERIAL RESPONSIBILITY FOR  
PUBLIC BODIES WITHIN THE TREASURY AND FINANCE SECTOR**

| <i>Ministerial portfolio</i> | <i>Entities subject to audit</i>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              |
|------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Finance</b>               | Emergency Services Superannuation Board<br>Government Employee Housing Authority (a)<br>Hospitals Superannuation Board<br>Local Authorities Superannuation Board<br>Port of Geelong Authority Superannuation Fund<br>Regulator General, Office of the<br>Victorian Superannuation Board, administering: <ul style="list-style-type: none"> <li>• Coal Mine Workers' Pensions Fund</li> <li>• Holmesglen Constructions Superannuation Plan</li> <li>• Parliamentary Contributory Superannuation Fund</li> <li>• State Casual Employees Superannuation Fund</li> <li>• State Employees Retirement Benefits Fund</li> <li>• State Superannuation Fund</li> <li>• Transport Superannuation Fund</li> <li>• Victorian Superannuation Fund</li> </ul> Victorian WorkCover Authority |
| <b>Gaming</b>                | Tabcorp Holdings Limited Club Keno Business Segment<br>Tabcorp Manager Pty Ltd Gaming Business Segment<br>Tattersall Gaming Machine Division<br>Tattersall Sweep Consultation<br>Tattersall's Club Keno<br>Totalizator Agency Board<br>Victorian Casino and Gaming Authority                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                  |
| <b>Treasurer</b>             | Aluminium Smelters of Victoria Pty Ltd<br>Citipower Ltd<br>Coal Corporation of Victoria (b)<br>Eastern Energy Ltd<br>Ecogen Energy Ltd<br>Electricity Services Victoria<br>Energy Brix Australia Corporation<br>Energy Business Centre Pty Ltd<br>Everton Dell Pty Ltd<br>Gas and Fuel Corporation of Victoria (c)<br>Gas and Fuel Corporation Superannuation Fund                                                                                                                                                                                                                                                                                                                                                                                                            |



|                          |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          |
|--------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Treasurer - cont.</b> | Gas Transmission Corporation<br>GASCOR<br>Generation Victoria<br>GFE Resources Ltd (d)<br>Hazelwood Power Corporation Ltd<br>Loy Yang B Power Station Pty Ltd<br>Loy Yang Power Ltd<br>National Electricity Pty Ltd<br>Powercor Australia Ltd<br>PowerNet Victoria<br>Powerworks Pty Ltd<br>Renewable Energy Authority of Victoria<br>Rural Finance Corporation<br>Securities Finance Corporation Ltd<br>SECV International Pty Ltd (d)<br>Solaris Power Ltd<br>Southern Hydro Ltd<br>State Electricity Commission of Victoria<br>State Insurance Office<br>State Trustees Ltd (e)<br>The Albury Gas Company Ltd<br>Transport Accident Commission<br>Treasury Corporation of Victoria<br>Tricontinental Australia Ltd<br>Tricontinental Corporations Ltd<br>Tricontinental Holdings Ltd<br>Twin Waters Resort Pty Ltd<br>United Energy Limited (d)<br>Utilities Insurance Company Pty Ltd<br>V.E.I. Superannuation Pty Ltd<br>Vicfleet Pty Ltd<br>Victorian Debt Retirement Fund (f)<br>Victorian Electricity Industry Superannuation Fund<br>Victorian Fund Management Corporation<br>Victorian Power Exchange<br>Vistel Ltd<br>Yallourn Energy Pty Ltd |
|--------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

(a) Ceased operations on 29 February 1996.  
 (b) Ceased operations on 20 June 1995.  
 (c) Ceased operations on 21 June 1995.  
 (d) Sold to a private sector entity as at 30 June 1995.  
 (e) Formerly known as State Trust Corporation of Victoria.  
 (f) Ceased operations on 1 July 1995.

**3.8.3** Comment on matters of significance arising from the audit of entities within the Treasury and Finance sector is provided below.



## GAS INDUSTRY REFORM IN VICTORIA

**3.8.4** The Gas and Fuel Corporation of Victoria (GFCV) was established as a public authority in 1950, following the amalgamation of 2 privately-owned utilities. The purpose of the amalgamation was to facilitate the unification of the gas industry in Victoria. At 30 June 1994, the GFCV economic entity, which included The Albury Gas Company Limited and GFE Resources Limited, was the largest government trading enterprise in the Australian gas industry, with activities including gas exploration, production, transmission and distribution.

**3.8.5** In September 1994, the Government outlined a program for reform of the gas industry in Victoria that involved the initial separation of the transmission and distribution businesses to be followed by the adoption of an optimal competitive structure. The Government acknowledged that completion of the reform process was dependent on the finalisation of the following matters:

- renegotiation of the current long-term gas supply contracts with ESSO/BHP;
- settlement of a dispute between the State and ESSO/BHP relating to the Petroleum Rent Resource Tax (PRRT) which is currently under arbitration; and
- co-ordination of gas industry reform at the national level.

**3.8.6** The Gas Industry Reform Unit (GIRU) within the Department of Treasury and Finance was established to develop and implement the Government's reform program.

**3.8.7** The reform vision as outlined in *The Gas Industry in Victoria - a Competitive Future Information Paper No. 1*, issued by the State Government, is to "... restructure the gas industry to optimise the competitive pressures at every level of the industry to achieve major ongoing efficiency gains and the lowest, long-term sustainable prices for consumers from the efficient use of resources".

**3.8.8** In order for the Government to achieve its reform objectives, the *Gas Industry Act 1994* was enacted with effect from 1 July 1994. The purpose of this Act was to restructure the gas industry in Victoria by disaggregating the GFCV through the transfer of property, rights and liabilities into 2 new State-owned corporations, in order to separate the distribution and transmission businesses. This was followed by the dissolution of the GFCV and the transfer of residual property, rights and liabilities to the State Electricity Commission of Victoria (SECV).

**3.8.9** Based on information provided by the GIRU and the gas entities, the aggregate costs incurred by the State on the reform process to 31 March 1996 were around \$11 million. Table 3.8B outlines these costs.



**TABLE 3.8B**  
**GAS INDUSTRY REFORM PROGRAM**  
**COSTS TO 31 MARCH 1996**  
 (\$million)

| <i>Item</i>                   | <i>Amount</i> |
|-------------------------------|---------------|
| GIRU costs -                  |               |
| Private sector specialists    | 5.1           |
| Gas industry entities costs - |               |
| Computer modifications        | 5.0           |
| Staff costs                   | 0.7           |
| Public relations              | 0.2           |
| <b>Total</b>                  | <b>11.0</b>   |

**Separation of transmission and distribution businesses**

**3.8.10** The *Gas Industry Act* 1994 provided for the establishment of:

- GASCOR (trading as Gas and Fuel) - the gas distribution corporation, responsible for the sale and distribution of natural gas and the sale of appliances at a retail level; and
- the Gas Transmission Corporation (GTC) principally responsible for the transportation of gas through transmission pipelines, the storage of gas for transport customers, and the construction and operation of transmission pipelines and storage facilities.

**3.8.11** Under the reform arrangements, the wholly-owned subsidiaries of the GFCV were allocated as follows:

- The Albury Gas Company Limited was vested in GASCOR; and
- GFE Resources Limited, the gas exploration company, was vested in the Treasurer of Victoria. Subsequently, in August 1995 this business was sold to private sector interests and comment on this sale was made in my October 1995 *Report on the Statement of Financial Operations, 1994-95*.

**3.8.12** Details of the transfer of the GFCV's assets and liabilities on disaggregation are provided in Table 3.8C.

**TABLE 3.8C**  
**ALLOCATION OF GFCV ASSETS AND LIABILITIES**  
(\\$'000)

| <i>Item</i>                                   | <i>GFCV<br/>financial<br/>position<br/>as at<br/>30 June<br/>1994</i> | <i>Transferred to</i> |                | <i>Remaining<br/>residual in<br/>GFCV</i> |
|-----------------------------------------------|-----------------------------------------------------------------------|-----------------------|----------------|-------------------------------------------|
|                                               |                                                                       | <i>GASCOR</i>         | <i>GTC</i>     |                                           |
| Assets                                        | 1 468 649                                                             | 1 141 308             | 205 293        | 122 048                                   |
| Liabilities                                   | 1 079 824                                                             | 743 504               | 208 892        | 127 428                                   |
| Net assets/(liabilities) prior to restatement | 388 825                                                               | 397 804               | (3 599)        | (5 380)                                   |
| Restatement of assets at fair value           | -                                                                     | 7 128                 |                |                                           |
| <b>Net assets/(liabilities)</b>               | <b>388 825</b>                                                        | <b>404 932</b>        | <b>(3 599)</b> | <b>(5 380)</b>                            |

**3.8.13** Following disaggregation, the assets and liabilities remaining in the GFCV included cash, land held for resale, freehold land, 2 exploration permits, and provisions for land remediation, lease withdrawal (head office accommodation) and associated litigation costs.

#### Wind-up of the GFCV

**3.8.14** The *Gas and Fuel Corporation (Repeal) Act 1995* which was assented to in June 1995, provided for the transfer of all residual assets and liabilities of the GFCV to the SECV upon dissolution of the Corporation in June 1995. Table 3.8D outlines the assets and liabilities transferred to the SECV at that date:

**TABLE 3.8D**  
**GFCV ASSETS AND LIABILITIES**  
**TRANSFERRED TO SECV**  
(\\$'000)

| <i>Details</i>                                                 | <i>Amount</i>   |
|----------------------------------------------------------------|-----------------|
| Assets -                                                       |                 |
| Cash                                                           | 10 318          |
| Receivables                                                    | 8 641           |
| Freehold properties (net of provision for related remediation) | 3 360           |
| Deferred exploration and development expenditure               | 4 860           |
| <b>Total assets</b>                                            | <b>27 179</b>   |
| Liabilities -                                                  |                 |
| Creditors                                                      | 1 248           |
| Provision for land remediation                                 | 56 661          |
| Provision for litigation                                       | 23 663          |
| <b>Total liabilities</b>                                       | <b>81 572</b>   |
| <b>Net liabilities transferred</b>                             | <b>(54 393)</b> |



**3.8.15** In addition to the above allocation of assets and liabilities, the following contingent liabilities were transferred to the SECV:

- a claim for damages of \$107 million by Gleem Pty Ltd relating to the GFCV's withdrawal from an agreement to lease certain office accommodation; and
- future remediation expenditure on contaminated properties, previously owned by the GFCV, that may be incurred should developments take place, and on adjoining sites which may have been affected by contamination.

**3.8.16** In relation to the net liabilities transferred to the SECV, an amendment to the *State Electricity Commission Act 1958* now incorporates a right of indemnity from the Treasurer of Victoria to the SECV for the discharge of obligations in relation to these liabilities.

**3.8.17** Comments follow on the 3 major financial exposures of the GFCV at the time of disaggregation.

*Head office accommodation lease*

**3.8.18** The Auditor-General's May 1995 *Report on Ministerial Portfolios* provided an outline on the protracted negotiations by the GFCV to secure suitable head office accommodation which culminated in the GFCV entering into a lease with the developer, Gleem Pty Ltd. Following a reassessment of its accommodation needs in May 1993 and after consultation with the Government, the Corporation formally repudiated the agreement to lease. Subsequently, the developer commenced legal proceedings claiming \$107 million in damages for the GFCV's withdrawal from the agreement to lease and the GFCV, in turn, lodged a counterclaim on the basis that it was entitled to terminate the lease.

**3.8.19** While not admitting liability, based on legal advice, the GFCV recognised a provision of \$20 million, plus associated legal costs, as a liability in its financial statements for the year ended 30 June 1994 in relation to the litigation. This provision, together with the associated contingent liability, was transferred to the SECV upon dissolution of the GFCV in June 1995.

**3.8.20** At the date of preparation of this Report, legal proceedings were still continuing. The State's total exposure relating to this matter can only be determined on finalisation of the legal proceedings.

*PRRT dispute*

**3.8.21** Bass Strait gas production became subject to Petroleum Rent Resources Tax (PRRT) on the enactment of the *Petroleum Resource Rent Legislation Amendment Act 1991*. Prior to this date, Bass Strait gas production attracted a 10 per cent royalty, under the Commonwealth Government's excise and royalty regime, which was an implicit cost in the gas supply agreements between ESSO/BHP and the GFCV which ultimately expire in the year 2015.

**3.8.22** The Auditor-General's May 1995 *Report on Ministerial Portfolios* commented on the status of arbitration proceedings associated with ESSO/BHP's right to on-pass PRRT costs to GASCOR and Generation Victoria.

**3.8.23** At the date of disaggregation, the GFCV's exposure of \$239 million relating to the PRRT was disclosed as a contingent liability in its financial statements. This

amount represented an accumulation of PRRT on Bass Strait gas production since 1 July 1990, invoiced to the GFCV by ESSO/BHP.

**3.8.24** Under the reform arrangements, the gas supply contracts and the associated PRRT exposures were allocated to GASCOR. At 30 June 1995, GASCOR disclosed a contingent liability of \$327 million in relation to the PRRT in its financial statements.

**3.8.25** Although discussions have taken place between the parties in an effort to resolve the matter, at the date of preparation of this Report no resolution had been reached. At 31 March 1996, GASCOR had incurred associated arbitration and litigation costs of \$21 million, a substantial increase from the amount of \$12 million incurred at 31 January 1995. As arbitration proceedings remain pending, these costs are likely to further increase.

*Land remediation*

**3.8.26** The Auditor-General's May 1995 *Report on Ministerial Portfolios* commented on the GFCV's exposure to costs relating to the remediation of contaminated gas production sites currently or previously owned by the Corporation. The GFCV had recognised a total exposure in relation to this matter of \$74.6 million within its financial statements. However, the Corporation had estimated its ultimate exposure for land remediation costs at \$244 million, in the event that it be required to perform remediation work to restore all contaminated sites to a pristine condition.

**3.8.27** Table 3.8E outlines the allocation of the exposure recorded in the GFCV's financial statements as at the date of disaggregation and a subsequent reassessment of this exposure during the 1994-95 financial year.

**TABLE 3.8E  
ALLOCATION OF  
LAND REMEDIATION EXPOSURES  
(\$million)**

| <i>Entity</i>                | <i>Liability<br/>as at<br/>1 July 1994</i> | <i>Reassessmen<br/>t<br/>of liability as at<br/>30 June 1995</i> |
|------------------------------|--------------------------------------------|------------------------------------------------------------------|
| GASCOR                       | 10.3                                       | 12.2                                                             |
| Gas Transmission Corporation | 0.4                                        | 0.4                                                              |
| SECV                         | 63.9                                       | 76.6                                                             |
| <b>Total</b>                 | <b>74.6</b>                                | <b>89.2</b>                                                      |

**Business restructures**

**3.8.28** Prior to, and following the commencement of, the restructuring of the gas industry, the GFCV and GASCOR rationalised their operations through outsourcing a number of activities, resulting in staff numbers being reduced from around 6 000 to 2 500.

**3.8.29** Table 3.8F summaries the key areas outsourced as well as areas designated for future outsourcing and the annual cost-savings estimated by GASCOR.

**TABLE 3.8F**  
**ESTIMATED ANNUAL SAVINGS**  
**FROM OUTSOURCING ACTIVITIES**  
(\$million)

| <i>Activity</i>                      | <i>Estimated annual savings</i> |
|--------------------------------------|---------------------------------|
| Areas outsourced since 1 July 1993   |                                 |
| -                                    |                                 |
| Appliance maintenance                | 9.0                             |
| Gas supply services                  | 3.0                             |
| Meter reading                        | 1.8                             |
| Mainframe data centre services       | 1.6                             |
| Internal audit                       | 0.5                             |
| Telephone management services        | 0.3                             |
| Remittance processing                | 0.2                             |
| Passenger fleet management           | 0.2                             |
|                                      | <b>16.6</b>                     |
| Areas to be outsourced in 1996 -     |                                 |
| Mains and services work              | 7.7                             |
| Messenger service                    | 0.2                             |
| Payroll/human resource system        | 0.2                             |
|                                      | <b>8.1</b>                      |
| <b>Estimated annual cost-savings</b> | <b>24.7</b>                     |

**3.8.30** During the early part of the current year, GASCOR entered into an innovative outsourcing arrangement whereby its mains and services functions, together with approximately 600 employees, were transferred to 3 private sector companies. This has been achieved by entering into *Alliance Partnerships* with the companies to undertake these functions on behalf of GASCOR. Separate *joint management* bodies, comprising GASCOR and respective company representatives, have been set up for each of the 3 companies to monitor performance and oversee compliance with the respective contracts. The contracts are for a period of 3 years effective from April 1996, with GASCOR having an option to either renew the contracts or negotiate new contracts with other private sector companies at the end of that period.



**3.8.31** As indicated in Table 3.8F, GASCOR anticipates to achieve savings of approximately \$7.7 million a year through the outsourcing of these functions. While these efficiencies may be gained from the arrangements, GASCOR has retained responsibility for:

- achievement of the objectives associated with this function, including the continuous improvement of service delivery;
- determining the priority of works and services to be provided by the companies;
- ensuring there is sufficient work to fully engage all transferred employees for as long as they remain employees of the companies;
- planning and allocating work to be performed by the companies; and
- determining when an emergency situation arises during which time GASCOR may take control of the management and resources of the companies.

**3.8.32** While savings are expected to be achieved by the outsourcing of this function, GASCOR has retained significant obligations and exposures under the established arrangements.

**Future directions for the gas industry**

**3.8.33** During 1995-96, the GIRU commissioned consultants to assist in developing an optimised structure for the gas industry.

**3.8.34** The GIRU has advised audit that the future direction of the reform process will involve increased competition at each level within the gas industry. The key elements in the reform process will include:

- resolution of the PRRT dispute to remove the associated uncertainty and impediment to comprehensive gas reform in Victoria;
- renegotiation of the existing gas supply contracts to remove contractual impediments for the emergence of a more competitive gas market;
- review of Victorian gas distribution and marketing to create viable and sustainable businesses which will actively compete in the distribution and retail of gas to all customers;
- implementation of an effective access regime for gas pipelines covering both the terms and conditions of access and pricing to encourage competition;
- staged implementation of "direct access" allowing gas customers to buy directly from any gas supplier, that is, phasing-in retail competition similar to the electricity industry; and
- review of the current Public Authority Contributions on GASCOR to facilitate competition in the contestable segments of the Victorian gas market.

*□ NO RESPONSE provided to the issues raised.*





**VICTORIAN ELECTRICITY INDUSTRY PRIVATISATION**

**3.8.35** In previous Auditor-General's Reports to the Parliament, audit has commented on the Government's substantial public sector reform program and, in particular, the disaggregation and privatisation of business enterprises within the Victorian electricity supply industry. The reform program centered around the disaggregation of the Victorian power industry and the establishment of 12 key entities, including:

- *5 regionally-based distribution and retail companies*, to operate the State's low voltage distribution network, including the network previously operated by 11 Municipal Electricity Undertakings which were managed by municipal councils, and to supply electricity at the retail level;
- *PowerNet Victoria*, to manage the high voltage transmission network for the transfer of electricity from power stations to the distribution companies;
- *Victorian Power Exchange*, to monitor and control the wholesale electricity market and ensure the security of the electricity supply system; and
- *5 generation entities* to operate the brown coal mines, thermal, gas and hydro power stations, and the associated power generation activities.

**3.8.36** In addition, the *Office of the Regulator-General* was established to independently regulate the Victorian electricity industry and, in particular, to promote competition in the generation and supply of electricity, and to ensure the maintenance of a safe, efficient and economic industry.

**3.8.37** The former State Electricity Commission of Victoria (SECV) was retained as a so-called *shell* to manage the assets and obligations not allocated to the newly created electricity entities. In June 1995, the SECV was also allocated responsibility of certain residual assets and liabilities of the former Gas and Fuel Corporation of Victoria and the Coal Corporation of Victoria, which were not allocated to new entities on their disaggregation.

**3.8.38** To establish a secure financial base for the financing of the residual responsibilities of the SECV, inter alia, the Treasurer of Victoria in June 1995 transferred the ownership of all shares in the new electricity generation and distribution entities for nil consideration to the SECV. This was designed to ensure that the obligations of the SECV were serviced by the cashflows to be generated from electricity industry dividends determined by the Treasurer and proceeds from future industry privatisations.

## Sale of electricity distribution companies

**3.8.39** As outlined in my *Report on the Statement of Financial Operations, 1994-95*, in December 1994 the Government agreed in principle to the privatisation of all 5 distribution businesses and one electricity generation company, commencing in 1995. Consistent with this decision, the 5 distribution businesses were sold to private sector interests during the period August 1995 to January 1996. In addition, in March 1996, the Government announced the sale of the designated generation company, Yallourn Energy Limited. The results of this later sale will be analysed by audit and reported in my October 1996 *Report on the Statement of Financial Operations, 1995-96*.

**3.8.40** The key objectives of the Government's electricity industry privatisation program have been to provide enduring incentives for efficiency improvements by the industry and to ensure that commercial risks are borne by private sector investors, and not by taxpayers and customers. The benefits of privatisations are anticipated by the Government to include:

- transfer of commercial risk to investors;
- promoting contestability in the supply of services;
- providing a return on public assets;
- reducing public debt; and
- through competitive pressure, delivering the lowest possible prices to customers.

**3.8.41** As outlined in my November 1995 *Special Report No. 38, Privatisation: An audit framework for the future*, it is essential that the complex economic, social and environmental issues that arise from the privatisation program are well managed to ensure the achievement of the program objectives.

**3.8.42** It is also essential that the management processes associated with the program are subject to audit examination. However, the long-term nature of the Government reforms may prevent audit in the short-term from forming firm conclusions on whether the policy objectives for privatisation have in fact been met, given that the success or otherwise of privatisation will not in many cases be fully known for many years.

**3.8.43** As an initial step to assist in laying the foundation for the future audit of privatised activities, and to promote sound management practices in future privatisations and enhance accountability in terms of processes implemented to date, the abovementioned Special Report set out a series of broad high level performance criteria that may be used in assessing the Government's management of a range of key issues associated with privatisation. The criteria encompassed, inter alia, the important areas of:

- research and analysis;
- cost-benefit analysis;
- risk strategies;
- key success benchmarks;
- pricing;
- service quality;





- social obligations and environmental considerations;
- safety;
- return on public assets; and
- risk allocation between the Government and the private sector.

**3.8.44** My October 1995 *Report on the Statement of Financial Operations, 1994-95* provided an analysis of the financial result achieved by the State from the sale of the first electricity business, namely, United Energy Limited, including the key terms of the sale and any residual obligations of the State. The sale of the State's remaining 4 electricity distribution businesses were completed subsequent to that Report.

**3.8.45** Given that the sales of all the State's distribution businesses have now been completed, it is opportune to provide to the Parliament an analysis of the financial results achieved by taxpayers from this privatisation program, including the costs incurred in relation to the program and any residual obligations of the State.

**3.8.46** While this audit review focuses on the provision of a financial analysis of the results achieved from the sale of the 5 distribution companies, it does not extend to an examination of issues of efficiency and effectiveness nor the achievement of economic policy objectives which, as previously stated, cannot be fully assessed for some years.

*Profile of the distribution companies*

**3.8.47** The 5 distribution companies were established by the Government in October 1994 following the disaggregation of the Victorian electricity industry. As indicated previously, the companies assumed the distribution activities and the assets and liabilities initially managed by the SECV and the 11 Municipal Electricity Undertakings that were previously managed by municipal councils. Three of the companies, namely, United Energy Limited (United Energy), Solaris Power Limited (Solaris) and CitiPower Limited (CitiPower) are predominantly based in metropolitan Melbourne, while Eastern Energy Limited (Eastern Energy) and Powercor Australia Limited (Powercor) operate distribution networks covering mainly rural Victoria.

**3.8.48** The companies charge their customers network connection and electricity consumption charges which were set by the Government at a level estimated to be sufficient to recover operating and capital costs, including a return on assets. The network connection charges were anticipated to generate the bulk of company revenues and profits.

**3.8.49** Each company has a regulated monopoly distribution network and a retail activity within a specific franchise area which is to be gradually exposed to competition. All retail customers will become contestable by December 2000. Large industrial electricity consumers already have the ability to freely choose the most cost-effective and reliable retailer to obtain their electricity services.



**3.8.50** A brief profile of each company's service responsibilities follows.

**DISTRIBUTION COMPANIES - A SNAPSHOT**

|  |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
|--|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|  | <p><b><i>United Energy</i></b></p> <p>The company's distribution network covers approximately 1 450 square kilometres in the south-eastern suburbs of the Melbourne metropolitan area, extending to the semi-rural and coastal resort area of the Mornington Peninsula. This region accounts for 26 per cent of Victoria's population. The company distributes power to over 520 000 customer sites, approximately 474 000 of which are residential customers.</p>                                   |
|  | <p><b><i>Solaris</i></b></p> <p>The company distributes electricity to the north-western suburbs of Melbourne. Its distribution network covers an area of approximately 956 square kilometres and includes the municipalities of Williamstown in the south through to Heidelberg in the east and includes the communities of Broadmeadows and Sunbury. The franchise area covers over 232 500 customer sites.</p>                                                                                    |
|  | <p><b><i>CitiPower</i></b></p> <p>The company's distribution area is the smallest of the 5 distributors, covering approximately 157 square kilometres. The area includes the central activities district and the densely populated inner suburbs of Melbourne. Citipower has the highest customer density, with 1 468 customers per square kilometre and the highest market share in the commercial sector, with 34 per cent of total commercial sales in Victoria.</p>                              |
|  | <p><b><i>Eastern Energy</i></b></p> <p>The company is a rural-based distribution business comprising 80 000 square kilometres from the outer-Eastern Melbourne metropolitan area to the eastern coastal areas and the Victoria/New South Wales border to the north. Eastern Energy currently services around 471 000 customer sites, including 405 000 residential customers.</p>                                                                                                                    |
|  | <p><b><i>Powercor</i></b></p> <p>The company is geographically the largest distribution business in Victoria. Its distribution area covers approximately 150 000 square kilometres in central and western Victoria and accounts for over one third of Victoria's population. The company supplies electricity to seven of the eight largest Victorian regional cities, including Geelong. The company distributes power to over 537 100 customer sites, including 446 000 residential customers.</p> |

*Sale process*

**3.8.51** Following the December 1994 decision to proceed with the sale of the distribution companies, the Government initially adopted a sale strategy that was to involve either trade sales or floats, or a combination of both. However, based on advice received from its financial advisors, it was subsequently decided to proceed with trade sales in all instances. As outlined in my *Report on the Statement of Financial Operations, 1994-95*, the key considerations underlying this decision included:

- trade sales were considered most likely to achieve the highest return to the State;
- strong interest was received from potential trade buyers, therefore ensuring a strong competitive sale environment;
- the float process was considered to be more vulnerable to political influences; and
- trade sales offered the opportunity to bring to the Victorian electricity industry expertise, international knowledge and methods to enhance the efficiency of service provision.

**3.8.52** Broadly, the sale process adopted by the Government involved the issue of Information Memorandums to potential purchasers which, following due diligence inquiries by bidders to establish the financial standing of the distribution companies, ultimately resulted in the submission of firm bids by interested parties. The bids were then evaluated by the Government to select the successful purchasers.

**3.8.53** To ensure that the most suitable purchasers were selected, all offers were assessed against predetermined criteria which included the value and structure of the bids, the certainty of the offers including the bidding parties' financial standing, and the quality of the proposals including the relevant skills and expertise of the bidding parties. In addition, to ensure the probity of the sale process, an independent process auditor was appointed for each sale to oversee the adopted processes and assist in ensuring that all bidding parties were accorded fair and equitable treatment.

**3.8.54** Under the sale arrangements for all companies except Powercor, the sale proceeds could be adjusted in respect of the final value of net assets sold, which is to be determined following the finalisation of a balance sheet review process.

**3.8.55** Specific comments on the processes adopted for the sale of the individual distribution companies follow.

*United Energy*

**3.8.56** As outlined in my *Report on the Statement of Financial Operations, 1994-95*, an Information Memorandum was issued in March 1995 to a number of potential bidders who had previously lodged an expression of interest in the acquisition of Victorian electricity businesses. Based on the details included in the Information Memorandum, indicative bids were received from potential purchasers in May 1995. The Government's evaluation of these bids resulted in the short-listing of 4 bidders who were then required to submit firm offers.



**3.8.57** The short-listed bidders lodged their final bids in early August 1995 following the conduct of due diligence inquiries. Shortly thereafter, following evaluation of the final bids, the Government announced the sale of United Energy to the Power Partnership consortium, comprising the AMP Society, the New South Wales State Authorities Superannuation Board and the United States-based company Utilicorp. The sale was actually completed in September 1995, with a financial effective date of 30 June 1995.

*Solaris*

**3.8.58** The Information Memorandum for the sale of Solaris was issued in August 1995 to parties who had previously expressed an interest in the purchase of the business. Following the completion of due diligence inquiries in October 1995 by potential bidders, 4 firm offers were received.

**3.8.59** The evaluation of bids was finalised with the Government announcing, in October 1995, the sale of Solaris to a joint venture between Australia's largest gas distributor, the Australian Gas Light Company, and Energy Initiatives Inc., a subsidiary of the United States-based power company General Public Utilities Corporation. The financial effective date of the sale was set as at 30 September 1995.

*Eastern Energy*

**3.8.60** A number of parties who had previously expressed an interest with the purchase of an electricity business were issued with an Information Memorandum for the sale of Eastern Energy in August 1995. Following the conduct of due diligence inquiries by potential bidders, 3 firm offers were received in November 1995. Given the proximity of the 2 leading bids and the desire to enhance the return to the State from the sale, the 2 bidders were subsequently given the opportunity to reconsider the financial aspects of their bids. Following the receipt and consideration of final bids, the Government announced that Texas Utilities Australia Pty Ltd, a subsidiary of Texas Utilities, a large electricity utility in the United States, was the successful purchaser. The financial effective date of the sale was set as at 30 September 1995.

*Powercor*

**3.8.61** The process for the sale of Powercor commenced with the issue of the Information Memorandum in October 1995 to parties who had previously expressed an interest in the acquisition of the distribution businesses. Interested parties were required to lodge final offers by 1 December 1995. However, the Government also gave all parties the opportunity to submit pre-emptive offers by 14 November 1995.



**3.8.62** The Government received 5 pre-emptive offers from potential purchasers following completion of their due diligence inquiries. However, given the proximity of the 2 highest offers, the parties associated with these bids were provided with the opportunity to review their offers. Following consideration of the final offers, the Government announced that Pacificorp Australia Holdings Pty Ltd, a wholly-owned subsidiary of the United States-based utility Pacificorp Holdings Incorporated, was the successful bidder. The sale was completed in December 1995, with a financial effective date of 30 September 1995. Unlike other sales, the final price for Powercor was not conditional on the finalisation of a balance sheet review due to the Government's view that, in this case, the review mechanism may have resulted in a discount in the bid price which exceeded the benefit to the State from its retention.

*CitiPower*

**3.8.63** The Information Memorandum for the sale of CitiPower was issued to interested parties in October 1995, with potential purchasers required to submit final offers by 1 December 1995. Similar to Powercor, the Government agreed to receive pre-emptive offers by 14 November 1995. Initially, only one offer was received, however, following finalisation of the sale of Powercor, unsuccessful bidders were invited to make offers for the purchase of CitiPower, which subsequently led to the submission of an additional firm offer.

**3.8.64** In December 1995, an agreement was reached with the original bidder for the sale of CitiPower to 2 companies, namely, Entergy Victoria and Entergy Victoria Holdings, subsidiaries of Entergy Corporation, a United States-based utility. To facilitate the prompt finalisation of the sale of the final distribution business, the sale was conditional on a number of factors, including the conduct of a due diligence review of CitiPower's financial standing, the approval of the purchasers' Board of Directors and financing approval from the bidder's financial backers. The sale was subsequently completed in January 1996, with a financial effective date of 30 September 1995.

*Overall comment*

**3.8.65** **The audit review concluded that the processes followed for the sale of the 5 distribution businesses were appropriate to ensure that the best available result was achieved by the State, with fair and equitable treatment accorded to all bidding parties.**

*Sale results*

**3.8.66** **Under the arrangements established for the sale of the distribution companies, the State is to receive total proceeds of \$9 billion, comprising amounts relating to:**

- sale of the State's interest in the net assets of the businesses (\$6.2 billion);
- repayment by the purchaser of outstanding business debt owed to the Treasury Corporation of Victoria (\$2.1 billion);
- dividends payable in relation to company profits earned up to 30 June 1995 (\$73 million);

- stamp duty on the sale transactions (\$30 million); and
- franchise fees receivable over the next 5 years based on forecast profits of the companies over that period (\$632 million, in present value terms estimated at the time of sale).

**3.8.67** Table 3.8G outlines the key components of the proceeds received by the State under the sale arrangements for each company.

**TABLE 3.8G**  
**COMPOSITION OF SALE PROCEEDS**  
((\$million))

| <i>Details</i>                                                               | <i>United<br/>Energy</i> | <i>Solaris</i> | <i>Eastern</i> | <i>Powercor</i> | <i>CitiPower</i> | <b>Total</b> |
|------------------------------------------------------------------------------|--------------------------|----------------|----------------|-----------------|------------------|--------------|
| Proceeds in excess of book value                                             | (a) 784                  | 539            | 1 271          | 1 107           | 958              | <b>4 659</b> |
| Proceeds equal to the SECV's interest<br>in the book value of the businesses | 339                      | 156            | 359            | 467             | 232              | <b>1 553</b> |
|                                                                              | 1 123                    | 695            | 1 630          | 1 574           | 1 190            | <b>6 212</b> |
| Repayment by purchaser of<br>outstanding debt of the businesses              | 471                      | 248            | 430            | 554             | 355              | <b>2 058</b> |
| Dividends owed to the State                                                  | 11                       | 8              | 17             | 24              | 13               | <b>73</b>    |
| Net State equivalent tax on company<br>trading operations                    | 4                        | (3)            | (2)            | (4)             | 5                | -            |
| Stamp duty on sale transactions                                              | 8                        | 2              | 6              | 2               | 12               | <b>30</b>    |
| Franchise fees receivable (net present<br>value)                             | 275                      | 137            | 47             | (b) -           | 173              | <b>632</b>   |
| <b>Total proceeds</b>                                                        | <b>1 892</b>             | <b>1 087</b>   | <b>2 128</b>   | <b>2 150</b>    | <b>1 748</b>     | <b>9 005</b> |

(a) This amount is \$60 million higher than that included in my *Report on the Statement of Financial Operations, 1994-95*, due to the inclusion of \$64 million received by the State representing State equivalent tax on company profits on the sale of its assets, and the separate disclosure in the above table of State equivalent tax on company trading operations. The initial amount of \$64 million was subsequently refunded by the State to the purchaser in accordance with the sale agreements.

(b) Franchise fees are not receivable from Powercor due to low forecast retail margins.

**3.8.68** Table 3.8G shows that the State received \$6.2 billion for the sale of the net assets of the companies, which at the effective date of sale had a value of \$1.6 billion. In effect, this resulted in the State obtaining \$4.6 billion more than the book value of the businesses.

**3.8.69** However, of the \$4.6 billion received in excess of the businesses book value, \$531 million was paid to municipal councils in relation to the electricity undertakings' net assets previously transferred to the distribution businesses. In addition, **the Department of Treasury and Finance estimates that costs directly incurred by the State in relation to these sales were in the order of \$40 million, with further indirect costs relating to electricity privatisation of \$5 million. Accordingly, the net benefit to the State from the sale of the 5 distribution companies is around \$4.1 billion.**

**3.8.70** As stated previously, under the sale arrangements for all companies except Powercor, the sale proceeds may be adjusted in respect of the final value of net assets sold, which is to be determined following the finalisation of the balance sheet reviews undertaken subsequent to the sales. At the date of preparation of this Report, the completion process in respect of United Energy had been concluded with no adjustments required to the sale price. The completion processes in relation to the other 3 companies were still in progress.

*Application of sale proceeds*

**3.8.71** A major aim of the electricity industry privatisation program is to reduce debt not allocated to the electricity companies (residual SECV debt) and then apply the remaining proceeds towards budget sector debt reduction. The audit review identified that the total proceeds of \$8.4 billion received by the State, not including franchise fees receivable in future years, were mainly applied towards State debt reduction (\$7.5 billion) and the financing of payments to municipal councils (\$531 million), with the balance (\$265 million) retained by the SECV for working capital purposes and the State to meet amounts payable in relation to the sales. Table 3.8H illustrates the application of the sale proceeds.

**TABLE 3.8H  
APPLICATION OF SALE PROCEEDS  
(\$billion)**

| <i>Details</i>                                                                                               | <i>Amount</i> |                |
|--------------------------------------------------------------------------------------------------------------|---------------|----------------|
| Retirement of State debt -                                                                                   |               |                |
| Budget sector debt                                                                                           | (a) 2.8       |                |
| SECV debt                                                                                                    | 2.6           |                |
| Distribution business borrowings                                                                             | 2.1           | 7.5            |
| Payments to municipal councils and costs of sale                                                             |               | 0.5            |
| Retention by SECV for working capital purposes and by the State for amounts payable in relation to the sales |               | (b) 0.4        |
| <b>Total sale proceeds</b>                                                                                   |               | <b>(c) 8.4</b> |

(a) Of this amount, \$2.1 billion was initially received by the SECV, with the balance of \$674 million received by the Consolidated Fund.

(b) Includes cost of sales of \$45 million and a payment of \$64 million to the purchaser of United Energy under an indemnity provided by the State within the sale agreement, representing a refund of State equivalent tax paid by the company to the State subsequent to the effective date of sale.

(c) In addition to the \$8.4 billion received from the sales, the State is entitled to receive franchise fees from the purchasers over the next 5 years with an estimated present value at the time of sales of \$632 million.

*Adequacy of results*

**3.8.72** To ensure that reasonable returns were achieved by the State from the sale of the companies, prior to their sale the Government obtained external valuations of the businesses based on the float and trade sale options. In addition, following the sale of United Energy, the bids submitted by potential purchasers provided guidance to the Government as to the price-earnings ratios the market was willing to bear.

**3.8.73** In February 1995, the Government's financial consultants advised an aggregate valuation for the companies (not including an amount receivable equal to the debt of the businesses of \$2.1 billion owed to the Treasury Corporation of Victoria) of \$4.5 billion as at July 1995, based on projected pre-tax discounted cash flows. A valuation of \$3.9 billion was also provided by the financial consultants based on price-earnings multiples.

**3.8.74** Preliminary valuations from 2 private sector stockbrokers valuers in May 1995 estimated that the flotation of the companies would raise proceeds of between \$3.3 billion and \$3.5 billion, not including an amount receivable equal to the debt of the businesses owed to the Treasury Corporation of Victoria. However, an assessment of these valuations by the Government's financial advisors suggested that public floats would be inherently more difficult to control than competitive trade sales and, therefore, float valuations should be viewed with greater uncertainty than trade sale values.

**3.8.75** Furthermore, it was identified by the financial advisors that based on the indicative bids received for United Energy, a trade sale premium in the order of 15 per cent to 25 per cent should be available to the State in relation to that sale should the Government proceed with the trade sale option. It was also considered that the trade sale premiums would be in the order of 5 per cent to 10 per cent for the 2 rural distribution companies (Eastern Energy and Powercor) due to the higher level of capital investment required for these companies and the gradual unwinding of the existing cross subsidies which could lead to higher rural tariffs in the future relative to urban tariffs. However, the Government has issued a tariff order which provides that these cross-subsidies will be maintained to the year 2000 and electricity prices overseen by the Regulator-General after that date, with the tariff order requiring that these cross-subsidies be phased out in the longer-term.

**3.8.76** In September 1995, the 2 private sector stockbrokers reviewed their earlier float valuations and indicated that, mainly due to the availability of more accurate information, the valuations should be revised to between \$4 billion and \$4.2 billion.

**3.8.77** **Based on the most recent float valuations for the individual companies prior to their sale, the proceeds of \$6.2 billion received by the State from the sale of the business net assets compared favourably with the valuations of \$3.9 billion, resulting in \$2.3 billion being received in excess of the float valuations.**

**3.8.78** Table 3.8I shows the proceeds received by the State from the sale of each company, and the earnings multiples achieved from the sales based on the actual earnings before interest and taxation for 1994-95, and the projections for the following 3 financial years.



**TABLE 3.81**  
**SALE PROCEEDS AND EARNINGS MULTIPLES**  
**ACHIEVED FROM THE SALES (a)**

| Company        | Sale<br>proceeds (b)<br>(\$m) | Price to earnings multiples |         |         |         | Average |
|----------------|-------------------------------|-----------------------------|---------|---------|---------|---------|
|                |                               | 1994-95                     | 1995-96 | 1996-97 | 1997-98 |         |
| United Energy  | 1 594                         | 14.4                        | 12.7    | 10.9    | -       | 12.6    |
| Solaris        | 943                           | 19.0                        | 16.9    | 14.7    | 13.0    | 15.9    |
| Eastern Energy | 2 060                         | 14.9                        | 14.9    | 13.6    | 12.6    | 14.0    |
| Powercor       | 2 128                         | 15.2                        | 16.2    | 12.3    | 10.6    | 13.6    |
| CitiPower      | 1 545                         | 19.1                        | 15.5    | 13.7    | 12.9    | 15.3    |

(a) The earnings multiples are based on projected earnings before interest and tax (including 1994-95) as per the Information Memorandum for each company (in nominal dollars).

(b) Represents proceeds for the sale of business net assets and the repayment of debt.

**3.8.79** While the result achieved from the sale of United Energy compared favourably with the available business valuations and was considered by the Government to be the benchmark for future sales, the results achieved from the sale of the remaining 4 companies were even better than those achieved for United Energy, on an earnings multiples basis.

**3.8.80** The Department of Treasury and Finance advised that the lower earnings ratio from the sale of United Energy was mainly due to the fact that it was the first distribution business to be privatised, in an environment that was less certain as to the availability of bank finance and the processes to be followed in relation to the sales. The outcome of this sale contributed to a higher level of interest and competition for the remaining businesses, with sale prices and therefore the earnings ratios achieved from the sales increasing beyond the outcome achieved for United Energy.

*What will be the ongoing impact of the sales on State finances?*

**3.8.81** Subsequent to the sale of the companies, substantial public debate has ensued regarding the ongoing impact of the privatisation program on the State's finances. To provide an analysis of the impact, audit identified the net interest savings to be achieved from the repayment of State debt resulting from the sales, after taking into account revenue to be forgone in the form of dividends and State equivalent taxes.

**3.8.82** Table 3.8J shows the impact of the company sales on State finances over the next 3 years.

**TABLE 3.8J**  
**PROJECTED NET INTEREST SAVINGS FROM APPLICATION**  
**OF SALE PROCEEDS TOWARDS REPAYMENT OF PUBLIC SECTOR DEBT**  
(\$million)

| <i>Details</i>                                            | <i>1995-96</i> | <i>1996-97</i> | <i>1997-98</i> | <i>Total</i> |
|-----------------------------------------------------------|----------------|----------------|----------------|--------------|
| Revenue forgone -                                         |                |                |                |              |
| Dividends (a)                                             | 141            | 159            | 209            | <b>509</b>   |
| State equivalent tax (b)                                  | -              | 11             | 43             | <b>54</b>    |
|                                                           | 141            | 170            | 252            | <b>563</b>   |
| Less income entitlement payments<br>to Municipal Councils | (25)           | (26)           | (28)           | <b>(79)</b>  |
|                                                           | 116            | 144            | 224            | <b>484</b>   |
| Interest savings (c)(d) -                                 |                |                |                |              |
| Budget sector debt                                        | 100            | 275            | 283            | <b>658</b>   |
| SECV debt                                                 | 140            | 258            | 258            | <b>656</b>   |
|                                                           | 240            | 533            | 541            | <b>1 314</b> |
| <b>Net interest savings</b>                               | <b>124</b>     | <b>389</b>     | <b>317</b>     | <b>830</b>   |

(a) Based on revenue projections contained in the Information Memorandums issued by the Government in relation to the sales and an estimate relating to United Energy Limited for 1997-98.

(b) Provided by the Department of Treasury and Finance based on a 'no privatisation' assumption.

(c) Based on estimates of interest savings provided by the Department of Treasury and Finance, and the Treasury Corporation of Victoria.

(d) Does not include interest savings relating to distribution businesses' debt owed to the Treasury Corporation of Victoria as the impact is already taken into account in arriving at the businesses' profits upon which dividends are based.

**3.8.83** Based on established projections, the sale of the distribution companies will result in a positive cashflow to the State over future years, given that the projected interest savings from the repayment of public sector debt will more than off-set the revenue forgone from dividends and State equivalent taxes. **This on-going net saving is estimated to be around \$350 million a year. In addition, the substantial reduction in State debt may positively impact on the State's credit rating which may result in a further reduction in interest rates payable on State debt.**

#### *Remaining obligations of the State*

**3.8.84** Under the sale arrangements, the State has provided certain indemnities and warranties to the purchasers, and has retained certain financial obligations, which may expose the State to future liability and cost.



*General indemnities and warranties*

**3.8.85** Various general warranties and indemnities have been provided by the State to purchasers of the various distribution businesses which, in relation to United Energy, Eastern Energy, CitiPower and Powercor, give rise to an aggregate maximum exposure to the State of \$145 million in the event that purchasers lodge claims within 12 months from the date of the relevant sale. In relation to Solaris, the State's maximum financial exposure under indemnities and warranties provided has not been specified or limited as no substantial undertakings were provided by the State in this sale agreement.

**3.8.86** In addition, the State has indemnified certain purchasers against a requirement to pay State equivalent taxation which was not fully provided for in the financial statements and arises in respect of the period up to the financial effective date of sale.

*Franchise fee indemnity*

**3.8.87** Under the sale agreement relating to United Energy, the Government provided an indemnity to the purchaser concerning the deductibility of franchise fees for taxation purposes. **The State may be required under this indemnity to make a payment of \$85 million to the purchaser in the event that an unfavourable ruling is received from the Australian Taxation Office (ATO), in relation to the deductibility of the franchise fees for taxation purposes, and the ruling is not overturned within the next 3 years.**

**3.8.88** In August 1995, the ATO issued a private ruling to United Energy which concluded that franchise fees payable by the company to the State were not tax deductible. However, taxation advice received by the Government and one of the purchasers of the distribution businesses has indicated that franchise fees are deductible for income tax purposes. Consequently, in October 1995, the Government lodged an objection to the ATO's ruling and has held discussions on the issue with the ATO. At the date of preparation of this Report, action by the State on the ATO ruling was in progress.

*Sales tax obligations*

**3.8.89** Given that the distribution companies were publicly-owned prior to their sale, they were exempt from the sales tax regime of the Commonwealth Government, which permitted the companies to acquire goods free of sales tax. However, following their sale, the companies became liable for such taxes. The Commonwealth (including the ATO) and the State Government have had protracted negotiations over the sales tax obligations of the privatised electricity distributors which had not been concluded at the time of privatisation.

**3.8.90** As part of the sale arrangements, the SECV on behalf of the State has entered into agreements with all the purchasers of the distribution companies so that the State ultimately bears the financial costs of the sales tax obligations met by the companies. This financial assistance was provided to ensure that electricity consumers are not disadvantaged by those costs being reflected in charges levied by the companies.

**3.8.91** The estimated total annual impost of sales tax on the distribution companies is \$35 million and is potentially an ongoing liability of the State. The negotiations relating to the sales tax obligations had not been finalised at the time of preparation of this Report.

#### *Community service obligations*

**3.8.92** The State has entered into agreements with all purchasers for the provision and funding of certain community services to eligible customers. Such community services include non-commercial programs and activities designed to meet community and social objectives determined by the Government.

**3.8.93** All agreements relating to community service obligations will expire on 31 December 2000. However, the parties have agreed to meet and discuss in good faith the possible extension of the agreements before 30 June 2000. Under the arrangements, the Government is obliged to reimburse the companies for costs incurred, including associated administrative costs, for the following community services provided to customers eligible for concessional benefits:

- *Winter Energy Concession* - a 17.5 per cent discount on 2 quarterly electricity accounts charged at the general domestic electricity tariff rate or its equivalent, and issued in winter;
- *Life Support Concession* - a discount on each electricity account charged at the general domestic electricity tariff rate for the use of a home-based life support machine;
- *Transfer Fee Waiver* - a waiver of an electricity connection fee when a customer moves into a principal place of residence which has an electricity connection;
- *Service to Property Charge Concession* - a discount equal to the amount by which the service to property charge exceeds the charge for electricity consumed on an electricity account, charged at the general domestic electricity tariff rate or its equivalent in relation to the customer's principal place of residence;
- *Summer Multiple Sclerosis Concession* - a 17.5 per cent discount on one quarterly electricity account charged at the general domestic electricity tariff rate or its equivalent, issued during summer in relation to a customer's principal place of residence; and
- *Group Homes Concession* - a 17.5 per cent discount to 2 quarterly electricity accounts charged at the general domestic electricity tariff rate or its equivalent, issued during winter.

**3.8.94** In addition, the Department of Human Services may provide written notice to the companies to provide certain further community services.

**3.8.95** The annual estimated cost to the State of funding community services delivered by the distribution companies on behalf of the Government is in the order of \$37 million. The funding of these community service obligations by the State is consistent with the arrangements operating prior to the sale of the companies.

*Tax compensation for the sale of State-owned enterprises*

**3.8.96** In my *Report on the Statement of Financial Operations, 1994-95*, I commented on the status of action taken by the Government to obtain compensation from the Commonwealth Government for revenues forgone on privatisation of business enterprises.

**3.8.97** In accordance with a *Statement of Policy Intent* agreed at the March 1994 Premiers Conference, the Treasurer forwarded a submission to the Commonwealth Government in April 1995 seeking tax compensation in relation to the privatisation of the former Totalizator Agency Board. The submission, which was to be used as a test case, concluded that the Commonwealth tax system imposed a loss on Victoria when it privatises its Government Business Enterprises and that the overall gain to the Commonwealth will be *more than sufficient* to meet proposed compensation relating to the privatisation of public sector entities.

**3.8.98** In December 1995, a Joint Commonwealth/State working group issued its *Final Report to Heads of Treasuries*, outlining the continuing disagreement by the Governments on the issue and stating that, in the opinion of the Commonwealth Treasury, further work was unlikely to resolve the conflicting positions. Subsequently, this matter has been proposed for discussion at the June 1996 Premiers Conference.

**Financial obligations of the SECV**

**3.8.99** As stated earlier in this Report, following disaggregation of the electricity and gas industries, the SECV has been retained as a so-called *shell* to manage the assets and obligations not allocated to the newly established entities. The role of the Administrator appointed to manage the *shell's* responsibilities is to effectively administer and, where appropriate, dispose of the assets and resolve the residual obligations of the entity. At the time of preparation of this Report, the key responsibilities of the SECV included:

- Management of rights and obligations under electricity supply contracts with the wholesale electricity market relating to the Loy Yang B power station, the Snowy Mountains power consortium inter-connecting agreement and the flexible electricity tariff arrangements relating to the Portland and Point Henry aluminium smelters;
- Completion of construction and commissioning of Unit 2 of the Loy Yang B power station. This Unit was operational and earning revenue for the SECV, however, the formal handover of the Unit to a joint venture of Mission Energy Australia Pty Ltd and Loy Yang Power Station Pty Ltd is not expected until September 1996;
- Resolution of legal proceedings against the former Gas and Fuel Corporation of Victoria by Gleem Pty Ltd, relating to alleged damages arising from the withdrawal by the Corporation from a lease of proposed new head office accommodation;
- Disposal of various properties, including surplus commercial and contaminated vacant land of the former Gas and Fuel Corporation of Victoria;



- Demolition of the former Yallourn Power Station complex, including the removal of hazardous metals and asbestos and site rehabilitation. Related clearance costs are estimated at \$43.5 million, with completion expected in August 1997;
- Administration of the unallocated electricity industry debt, which had a market value of \$45 million at 29 February 1996; and
- Resolution of other residual issues of the electricity and gas industries.

**3.8.100** Based on the SECV's management accounts as at 31 March 1996, its financial position not including its interest in (i.e. the amount receivable from) the State's electricity businesses of \$3.3 billion (30 June 1995, \$4.8 billion) was a net deficiency of \$428 million (30 June 1995, \$2.9 billion).

*Major developments since 30 June 1995*

**3.8.101** In my October 1995 *Report on the Statement of Financial Operations, 1994-95*, I outlined the financial position of the SECV as at 30 June 1995. Major developments and transactions since that date, covering the period to 31 January 1996, which have impacted upon the financial position of the SECV include:

- Reduction in the value of residual electricity industry debt from \$2.6 billion at 30 June 1995 to \$45 million at 29 February 1996, principally resulting from the application of proceeds from the sale of the 5 distribution companies towards debt retirement;
- Payment of \$2.1 billion of the distribution company sale proceeds to the Consolidated Fund, for subsequent application towards budget sector debt retirement;
- Payment of \$531 million to municipal councils relating to the net assets of Municipal Electricity Undertakings previously transferred to the distribution businesses;
- Sale of the Yallourn Mechanical Workshops in January 1996 for \$5 million, consistent with independent valuations, to the private sector entity which had leased the property since 1993. Under the sale arrangements, the purchaser agreed to retain certain strategic equipment required by local generating companies and, if it intended to sell the equipment, to give the State the first option for acquisition;
- Payment of \$3.5 million by the SECV to the private sector company that previously acquired the *Monash House* property at 15 William Street, Melbourne as full and final settlement relating to a legal dispute over certain aspects of the property sale;
- Sale of a former Coal Corporation of Victoria property site in Morwell in November 1995, at Valuer-General's valuation, for \$650 000; and
- Administration, on behalf of the State, of the remaining financial obligations and exposures, arising from the sale of the 5 distribution companies.

**3.8.102** In addition, during March 1996, the Government sold Yallourn Energy Ltd. As indicated previously, the results of this transaction will be analysed and reported in a subsequent Report to the Parliament.

*□ NO RESPONSE provided to the issues raised.*





**FINAL AUDIT OF UNITED ENERGY LIMITED**

**3.8.103** Under the established accountability framework, the Auditor-General has a dual audit responsibility in relation to all Victorian electricity distribution businesses.

**3.8.104** Firstly, under section 8(1) of the *Audit Act* 1994 the Auditor-General is responsible to the Parliament for the audit of all authorities, including companies *all the shares in which are owned by or on behalf of the State, whether directly or indirectly*. This provision empowers the Auditor-General to undertake the audit of all distribution businesses. Secondly, upon incorporation, the businesses requested the Auditor-General to accept appointment as their company auditor in accordance with the provisions of the Corporations Law.

**3.8.105** **Financial statements for each of the distribution businesses were prepared for the financial period ended 30 June 1995 and in accordance with the sale agreements as at the effective date of sale of each business.** In relation to United Energy Limited, the effective date of sale was as at 30 June 1995. Therefore, only one set of financial statements was required in relation to this business.

**Qualified audit opinion**

**3.8.106** The final financial statements of United Energy while in public sector ownership, for the period ended 30 June 1995, were audited by this Office and an audit opinion issued under the authority of the *Audit Act* 1994. Due to disagreement with the contents of the financial statements, a qualified audit opinion was issued by this Office in the following form:

*"As disclosed in notes 5 and 13 to the financial statements, United Energy Limited has included as an extraordinary item in the profit and loss account and as part of provisions in the balance sheet an amount of \$23 million in respect of income tax on revenue which will be earned subsequent to 30 June 1995. Accounting Standard AASB 1020 Accounting for Income Tax (Tax Effect Accounting) defines income tax expense as 'the amount of income tax which would be payable on the pre-tax accounting profit adjusted for permanent differences'. As the related revenue had not been earned as at 30 June 1995, it should not have been taken into account in determining the income tax expense and therefore, in my opinion, this accounting treatment is a departure from AASB 1020.*

*"United Energy Limited has also included as part of provisions in the balance sheet certain items totalling \$47.9 million which, in my opinion, should not have been raised. Of this amount \$29.7 million, which relates to provisions for losses on obligations to Tariff H customers, debt refinancing and uninsured claims, should not have been recognised as no present obligation existed at balance date. The remaining \$18.2 million relates to the incorrect measurement of provisions for losses on co-generation agreements, voluntary departure packages and regulatory compliance costs, resulting in the overstatement of these provisions by that amount.*

.....

*"As a result of the matters referred to above, the provisions as disclosed in the balance sheet are overstated by \$70.9 million and the operating loss and extraordinary items after tax as disclosed in the profit and loss account is overstated by the same amount. Had this amount not been provided for, the company would have reported an operating profit after tax of \$44.9 million."*

**3.8.107** Specific comments on the above qualification, other than the issue relating to taxation obligations which was a breach of a specific accounting standard, follow.

#### *Losses on Tariff H customers*

**3.8.108** The company provided for losses of \$12.8 million expected to be incurred as a result of legal obligations to supply power to certain customers at Tariff H rates which in its opinion were lower than the cost of providing the power. However, in my opinion, the provision for future losses on Tariff H customers was not appropriate for the following reasons:

- it was questionable that there was a future obligation on the company as there is contestability in the market place for Tariff H customers; and
- the company is in the business of supplying electricity to customers using a range of tariffs and therefore the business should be considered as a whole to determine if future losses exist which should be recognised in the financial statements.

#### *Debt refinancing*

**3.8.109** Upon disaggregation of Electricity Services Victoria on 1 July 1994, United Energy was allocated debt owing to the Treasury Corporation Victoria (TCV). Much of the debt transferred was at fixed interest rates, with the market value of the debt exceeding its face value.

**3.8.110** At the time of the actual sale of the company, the sale agreement required that the debt to TCV be immediately refinanced by the purchaser with external parties. This in effect would cause the company to incur a loss on refinancing this debt of \$16.4 million which was provided in its financial statements.

**3.8.111** However, in my opinion this amount should not have been recognised in the financial statements as the debt was refinanced subsequent to 30 June 1995 and there was no obligation to repay the debt and incur the additional costs of refinancing as at that date.





*Uninsured losses*

**3.8.112** The company provided in its financial statements an amount of \$511 000 for potential insurance claims. However, the company could not provide any evidence to support, and audit was not able to substantiate, this amount. Accordingly, in my opinion the company should not have disclosed this amount in its financial statements as at 30 June 1995.

*Losses on co-generation agreements*

**3.8.113** Future losses totalling \$10 million in relation to co-generation agreements for the purchase of power were provided in the company's financial statements.

**3.8.114** While it was agreed that there was an obligation on the company under the agreements to purchase power, the valuation of the provision for future losses was not considered appropriate as the company included certain costs in the calculation of future losses arising from such agreements which audit considered not to be relevant. When these costs are excluded these agreements do not result in future losses.

*Voluntary Departure Packages*

**3.8.115** The company provided \$24.9 million for future payments of Voluntary Departure Packages (VDPs) to its employees. In this instance, audit was unable to substantiate the valuation of the provision as the company did not provide satisfactory evidence to support the average salary rate used for the calculation of the provision relating to VDPs for 250 employees. Based on a recalculation by audit, the provision was overstated by approximately \$6.9 million.

*Compliance costs*

**3.8.116** Losses of \$4.5 million expected to be incurred by the company in complying with the *Electricity Industry Act 1993* and the regulations established by the Office of the Regulator General were provided for in the financial statements. However, \$1.3 million of this amount should not have been recognised as no obligation to incur this expenditure existed at 30 June 1995.

**3.8.117** Under generally accepted accounting practice for provisions to be recognised in the financial statements, the following criteria must be satisfied:

- there is a present obligation for a future sacrifice of service potential or economic benefit;
- the obligation arises as a result of a past transaction or event; and
- the amount of the liability can be reliably measured.

**3.8.118** Despite the above criteria, it is acknowledged in the accounting profession that the area of accounting for provisions requires judgement. However, in relation to United Energy, in my opinion, as previously stated, many of the provisions did not fulfil the requirements for recognition as liabilities and therefore should not have been brought to account in its financial statements.



**3.8.119** Also interestingly, many of the provisions brought to account by United Energy had not been previously recognised by the company's predecessor entities and were not brought to account by the company in the financial statements it prepared at 31 December 1994.

**3.8.120** Mainly due to the recognition of the \$70.9 million liabilities and associated expenditure which was subject to audit qualification, United Energy reported an operating loss of \$26 million compared with operating profits reported by each of the other 4 distribution businesses. Table 3.8K highlights the operating results for the period ended 30 June 1995 for all the distribution businesses.

**TABLE 3.8K**  
**OPERATING RESULTS OF DISTRIBUTION BUSINESSES**  
**FOR THE PERIOD ENDED 30 JUNE 1995(a)**  
(\$million)

| <i>Item</i>                                                                      | <i>Eastern<br/>Energy</i> | <i>Powercor</i> | <i>Solaris</i> | <i>CitiPower</i> | <i>United<br/>Energy</i> |
|----------------------------------------------------------------------------------|---------------------------|-----------------|----------------|------------------|--------------------------|
| Operating profit/(loss) after abnormal items, extraordinary items and income tax | 48.7                      | 67.9            | 23.4           | 37.3             | (26.0)                   |

(a) Period covers 11 May 1994 to 30 June 1995.

**3.8.121** Table 3.8K shows that all the electricity distribution businesses, except for United Energy, traded profitably consistent with the objectives established by the Government when the entities were established. If the items subject to audit qualification were eliminated, the operating result achieved by United Energy would have been a profit of \$44.9 million.

**Removal of the Auditor-General as the Corporations Law auditor of United Energy**

**3.8.122** The audit of United Energy's financial statements for the period ended 30 June was in progress at the time of its sale. Following the sale, the entity produced a draft set of financial statements that included the disputed items, which were subsequently discussed with management without resolution.

**3.8.123** Upon completion of the sale and the above referred discussions, the new owners of United Energy decided that since the company was now in private ownership, and, in their view, the audit had been completed, it would be appropriate for a chartered accounting firm to assume the role of the company's auditor under the Corporations Law. Consequently, the company requested the Auditor-General's resignation as the Corporations Law auditor of United Energy.



**3.8.124** In response to this request, the company was advised that the audit of its financial statements for the period ended 30 June 1995 had not been finalised and that a number of issues mainly relating to provisions recorded in the statement needed to be resolved. Furthermore, United Energy was advised that under the circumstances, until the audit report was issued on the 30 June 1995 financial statements, I would not resign as the auditor of the company to ensure that such action did not prejudice in any way my ability to finalise the audit of the company.

**3.8.125** Despite my refusal to resign as auditor of the company, United Energy proceeded with my removal as auditor, in accordance with the provisions of the Corporations Law. The removal became effective on 13 November 1995, with United Energy appointing a firm of chartered accountants as its Corporations Law auditor.

**3.8.126** This firm issued a clear audit opinion in December 1995 on the financial statements for the period ended 30 June 1995 which contrasted with the qualified audit opinion which I issued under the authority of the *Audit Act 1994* relating to the overstatement of liabilities and associated expenditure of \$70.9 million.

**3.8.127** There are 3 key issues that arise from the final audit of United Energy:

- the financial statements of the business for the period ended 30 June 1995 do not reflect the reality of its financial activities and position for the period due to the provisions and related expenditure inappropriately brought to account by the company after its sale;
- the company was able to obtain a confirming audit opinion under the Corporations Law only after taking action to remove myself as Corporations Law auditor at the time when the company was aware that its financial statements were likely to be qualified; and
- difficulties will be experienced by the users of the company's financial statements, given that they are accompanied by 2 audit opinions, i.e. a confirming audit opinion under the Corporations Law and a heavily qualified audit opinion issued under the *Audit Act 1994*.



## VICTORIAN FUNDS MANAGEMENT CORPORATION

**3.8.128** In December 1993, the Government announced the establishment of a central investment management body, namely, the Victorian Funds Management Corporation, to provide funds management and advisory services to public sector agencies on a voluntary and contractual basis. The Government anticipated that the establishment of the Corporation would provide significant benefits to the various public sector agencies, which jointly managed a combined investment portfolio of over \$14.5 billion, by:

- increasing the range of markets and managers available to these agencies, thereby enabling them to diversify their investment portfolios;
- generating economies of scale which would lead to lower fees and savings in administrative costs; and
- providing agencies with access to services of a corporation which is able to attract and retain skilled professionals, dedicated to overseeing the management of the investments of the public sector.

**3.8.129** An external consultant engaged by the Department of Treasury and Finance concluded that annual savings in the order of \$24 million were potentially available to the public sector from the centralisation of investment fund management, mainly attributable to reduced management costs and enhanced returns from improved portfolio diversification. However, a subsequent assessment by the Department of Treasury and Finance estimated the maximum value of available savings at around \$16 million. These potential savings were predicated on the establishment and provision by the Corporation of an investment product based on a pooled fund and trust structure, with the Corporation having the unilateral right to select and appoint external fund managers. However, such savings were expected to accrue only if the Corporation was able to attract a substantial portion of the investment funds held by its potential client base.

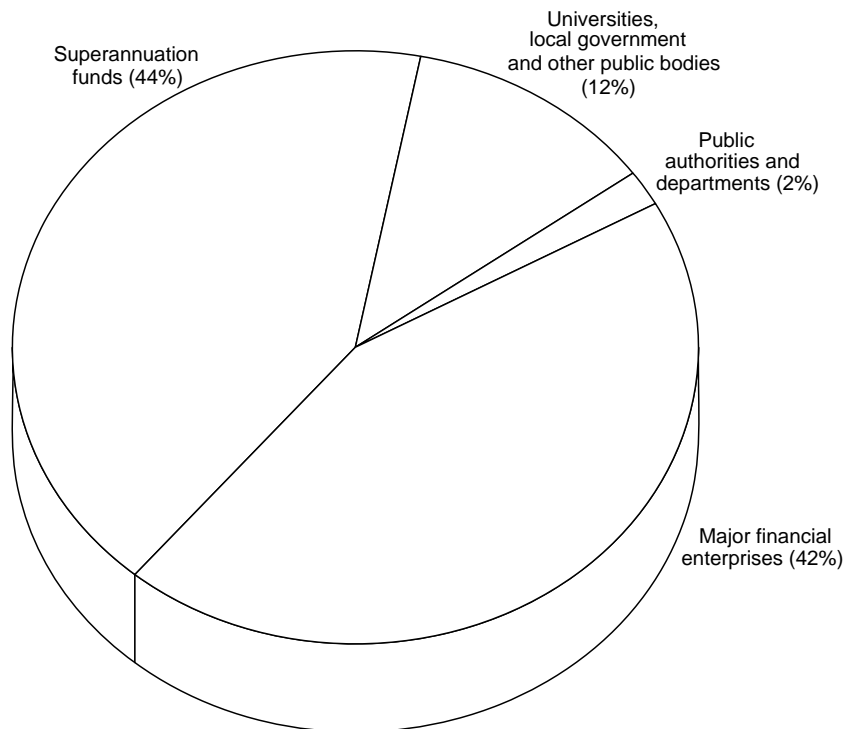
**3.8.130** In late July 1994, following the enactment of the *Victorian Funds Management Corporation Act 1994*, the Corporation commenced operations and was initially formed utilising the staff, infrastructure and systems of the Transport Accident Commission (TAC) Investment Group. The Government's vision was that the investment systems of the TAC, which in the past had produced good investment results, would be made available for the greater benefit of the public sector.

**3.8.131** The key objective of the Corporation was to provide investment and fund management services to participating bodies and the State in a commercially effective, efficient and competitive manner.

### Inability to attract an extensive client base

**3.8.132** At 30 June 1995, investments with an aggregate value of \$14.5 billion were held by public sector agencies, representing the potential client base of the Corporation. Public sector superannuation funds and financial enterprises, such as the TAC and the Victorian WorkCover Authority, accounted for the vast majority of public sector investment balances, as illustrated in Chart 3.8L.

**CHART 3.8L**  
**INVESTMENTS HELD WITHIN THE VICTORIAN PUBLIC SECTOR,**  
**AT 30 JUNE 1995**  
 (per cent)



**3.8.133** Audit found that, after one year of operation, the Corporation had only been able to attract around 25 per cent or \$3.7 billion of the State's total investment funds, with its only substantial client being the TAC. The key factors that adversely impacted on the Corporation's ability to extend its client base and investment portfolio were:

- Agency and market uncertainty and reluctance to engage the Corporation, given its recent establishment and the consequential absence of a track record;
- Legislative mandate only extended to the management of public sector investment funds on a contractual and voluntary basis, rather than on a compulsory basis;
- Inability of the Corporation to establish an investment product which was attractive to its major potential public sector clients. The initial investment products offered by the Corporation to agencies, namely, the master trust arrangement and the concept of pooled investment funds, were not favoured or embraced by agencies. This resistance was mainly due to the requirement of these products to be held in the name of the Corporation rather than the investing agency, with the agency only holding units in the master or pooled funds. It would appear that agencies considered that the transfer of substantial parts of their investment portfolios into pooled investment products would adversely impact on the discharge of their statutory and fiduciary responsibilities as trustees of these funds, even though components of their portfolios were already held in pooled products;



- Increased competition between, and with, private sector fund managers, which made it difficult for the Corporation to provide clients with substantial investment management efficiencies relative to the direct engagement by agencies of private sector fund managers; and
- Significant turnover of staff at the senior management level of the Corporation, possibly resulting in a lower level of agency confidence in its activities.

**3.8.134** The failure of the Corporation to attract the majority of public sector investment funds into its pooled trust products has meant that the expected benefits to the State from the Corporation's establishment, such as economies of scale and therefore lower investment management costs, have not been realised. Furthermore, the Corporation's overall objective of establishing itself as a commercially effective, efficient and competitive organisation had not been achieved.

**3.8.135** Comments on certain key aspects of the Corporation's first year of operations follow.

*Marketing of services and products*

**3.8.136** Critical to the Corporation's success was the establishment and appropriate resourcing of a marketing function to promote the Corporation and its products to current and potential clients. Audit found that, during the period July 1994 to April 1995, the marketing function was mainly performed by the former Chief Executive Officer. It was not until April 1995, in recognition of the importance of adequately resourcing this function, that the Marketing and Client Services Division was established within the Corporation.

**3.8.137** In addition, although identified as an integral part of the Corporation's corporate plan, a formal marketing plan had not been completed at the date of the audit review. The Corporation considered that until a marketable product was established, an effective marketing strategy could not be developed.

**3.8.138** In May 1995, a survey was conducted by the Corporation of its existing and potential clients, to gather information on their needs, the Corporation's competitors and the available opportunities to add value to the public sector. The survey responses indicated that:

- the cost of fund management services offered by the Corporation was similar to that offered by its competitors;
- investment management reporting by the Corporation to its clients was similar to its competitors;
- the Corporation's risk management and compliance practices were considered by the clients to be appropriate;
- custodian costs of other public sector investing bodies were generally higher than those achieved by the Corporation; and
- the Corporation's clients and potential clients generally wanted their investment portfolios to be managed on a discrete basis.

**3.8.139** In response to the above feedback from existing and potential clients, the Corporation commenced work to establish the *Umbrella Trust* investment product, which was perceived to be more attractive to clients.

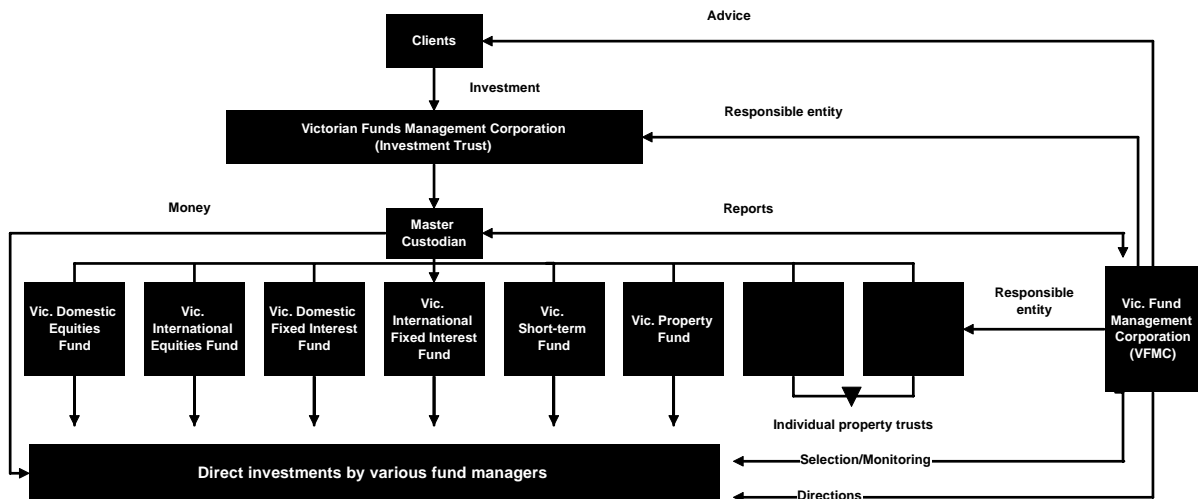


**3.8.140** The lack of a detailed understanding of client needs and expectations at the inception of the Corporation, together with delays in the development of appropriate investment products and an associated marketing strategy, were significant factors adversely impacting on the ability of the Corporation to attract new clients.

*Development of investment products*

**3.8.141** Prior to the establishment of the Corporation, the Government engaged external consultants at a cost of around \$700 000 to identify and assist in developing an appropriate investment product to attract public sector investment. As a consequence, the Corporation developed the master trust arrangement, involving a pooled trust in which investing agencies (clients of the Corporation) would hold units. The structure of this trust is outlined in Chart 3.8M.

**CHART 3.8M  
MASTER TRUST ARRANGEMENT, JULY 1994**



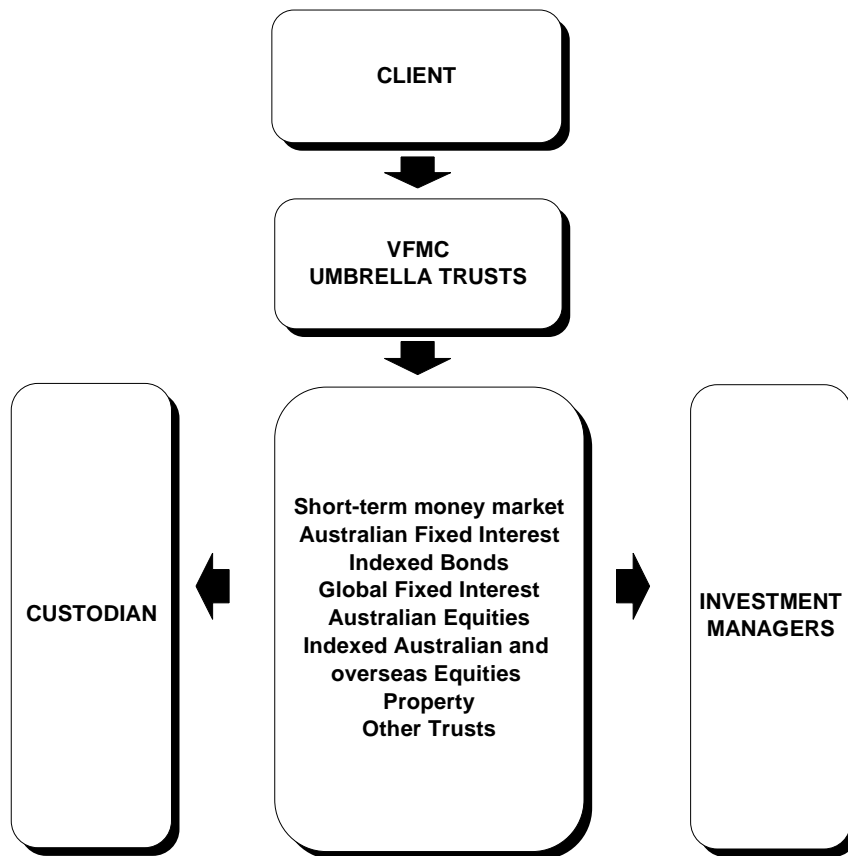


**3.8.142** As previously mentioned, **this master trust arrangement was subsequently discontinued because it failed to attract public sector clients.** Key factors that rendered this arrangement unattractive to clients included:

- capital gains tax implications on the transfer of investment fund ownership to the master trust;
- investment with market not in the name of the clients;
- contingent liabilities of the trust would be shared by all clients;
- not all targeted public sector agencies had the same investment objective as the master trust arrangement; and
- potential clients preferred their investment portfolios to be managed on a discrete basis.

**3.8.143** In May 1995, the *Umbrella Trust* arrangement was established as the successor investment product to be offered to clients in response to the diverse investment needs of the potential client groups within the public sector, as identified in the Corporation's marketing survey. Chart 3.8N illustrates the *Umbrella Trust* arrangement.

**CHART 3.8N  
UMBRELLA TRUST ARRANGEMENT, MAY 1995**







**3.8.144** The concept of pooling in a specialist trust was not considered desirable by major potential clients and, as a consequence, the umbrella trust product also failed to attract such clients. However, a number of smaller agencies, including the Manningham City Council, the State Trustee and the Department of Treasury and Finance (Managed Insurance Fund) have selected to invest in the *Umbrella Trusts*.

*Corporation's mandate in relation to client investment fund management*

**3.8.145** Under the established arrangements, the Corporation's clients determine their investment objectives based on their liability profile and the level of acceptable risk. Based on these parameters, the clients also determine the most desirable long-term strategic asset allocation, which is usually derived after taking into account the investment objectives, and the long-term historical and prospective risk and returns for each class of investment.

**3.8.146** Since the Corporation's establishment, its role in relation to client investment fund management can generally be summarised as follows:

- recommending to clients the most appropriate fund manager composition to achieve the client's risk and return objectives for each asset class;
- establishing fund management contracts with external fund managers, outlining the investment objectives and guidelines;
- ongoing monitoring and review of external fund manager performance on behalf of clients, which is normally stipulated in client service agreements;
- acting as trustee and manager of the *Umbrella Trusts*, or managing client funds on a discrete portfolio basis; and
- offering master custodian services for investment funds managed by the Corporation.

**3.8.147** The audit review found that **the implementation of the Corporation's responsibilities had significantly changed from the original fund management arrangements envisaged when it was first established**. In particular, while at the inception of the Corporation it was anticipated that pooled fund management arrangements would operate, the majority of investment funds were in fact managed as discrete portfolios and not part of the investment products offered by the Corporation.

**3.8.148** In addition, the under-utilisation of the Corporation's investment management services by public sector agencies, together with the absence of a direct presence of the Corporation in financial markets, made it difficult for the Corporation to establish a track record as an effective fund manager for public sector agencies. This further contributed to the reluctance by agencies to engage the Corporation.

.....

*Strategic direction*

**3.8.149** Since the establishment of the Corporation, significant changes occurred in its organisational structure, information systems and key management personnel, adversely impacting on the Corporation's operations up until November 1995. In particular, positions relating to the chief executive and senior management in such areas as marketing remained unfilled for significant periods early in the 1995 calendar year. These significant changes, together with a reduction in investment management operational resources and the non-finalisation prior to May 1995 of the Corporation's corporate plan, **until recently have contributed to a lack of clear strategic direction and management for the Corporation.**

**Investment performance**

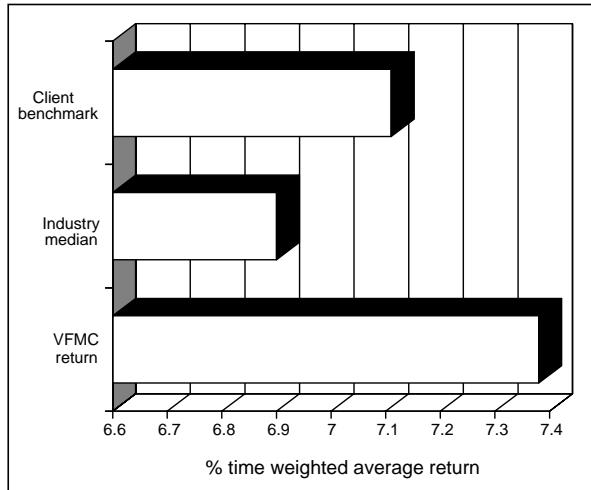
**3.8.150** A key objective of the Corporation is to achieve above-market returns for its clients within defined risk parameters. In relation to the Corporation's major client, namely, the TAC, audit conducted an analysis to determine the extent to which this objective was met.

**3.8.151** The analysis of the Corporation's performance involved a comparison of the time weighted rates of return it achieved for the 1994-95 financial year, for each major asset class, against the benchmarks established by the TAC and the average returns achieved generally by the industry. The major asset classes examined related to the short-term money market, fixed interest and equity portfolios.

**3.8.152** Charts 3.8O to 3.8R illustrate the result of the audit analysis of the Corporation's investment management performance.

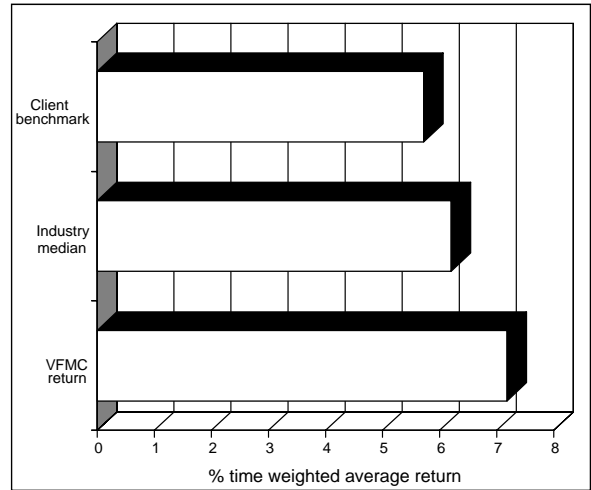
CHARTS 3.8O TO 3.8R  
 VFMC INVESTMENT RETURNS, 1994-95 FINANCIAL YEAR  
 (per cent)

CHART 3.8O  
 SHORT-TERM MONEY MARKET



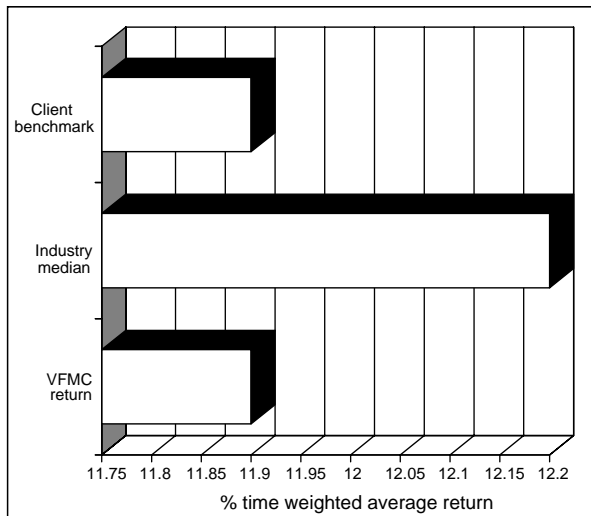
Benchmark: SBC Bank Bill Index.

CHART 3.8P  
 AUSTRALIAN EQUITY



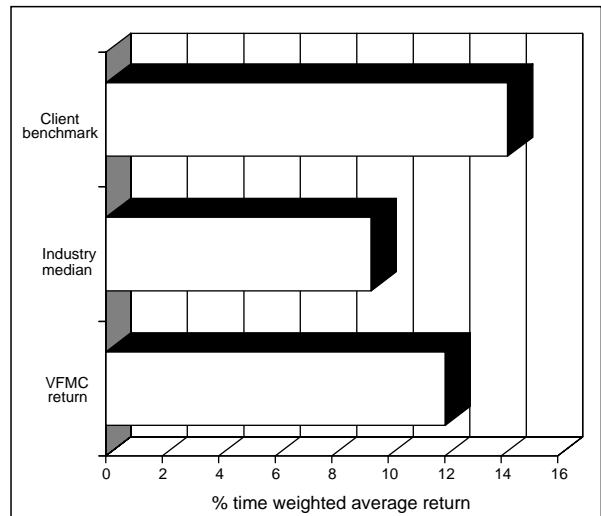
Benchmark: All Ordinaries Accumulation Index.

CHART 3.8Q  
 AUSTRALIAN FIXED INTEREST



Benchmark: SBC Composite Bond Index.

CHART 3.8R  
 INTERNATIONAL EQUITY



Benchmark: MSCI (ex-Australia) World Index in Australian dollars.

**3.8.153** The charts clearly indicate that the investment returns achieved by the Corporation during the 1994-95 financial year exceeded the client benchmarks and median industry returns in relation to the short-term money market and the Australian equities portfolios. However, the international equity portfolio returns achieved by the Corporation were lower than the client benchmark but exceeded the median industry returns. To improve its performance in this area, the Corporation identified the poorer performing fund managers and, as at the date of the audit review, was re-assessing the engagement of these managers.

**3.8.154** Based on the above analysis, in audit opinion, the Corporation has, in the main, met its corporate objective of achieving client benchmark returns.

#### *Investment management costs*

**3.8.155** The investment management costs of Victorian public sector bodies for the year ended 30 June 1995 were in excess of \$70 million or 0.5 per cent of the total investment portfolio analysed. These costs were mainly attributable to external fund manager fees and direct maintenance costs associated with real estate property holdings.

**3.8.156** The audit identified that these costs were significantly higher than interstate centralised investment bodies which have achieved substantial investment management cost savings due to their centralised pooled trust structures which have been established for some time. **The non-acceptance of the Corporation's pooled trust investments and the low utilisation of the Corporation's services by public sector agencies has meant that the estimated annual savings in investment management costs and enhanced returns of between \$16 million and \$24 million had not been realised.**

#### **Action taken to improve the Corporation's performance**

**3.8.157** Due to the difficulties experienced by the Corporation in attracting funds from public sector agencies, in November 1995 the Department of Treasury and Finance conducted an assessment of the ongoing viability of the Corporation. While the assessment concluded that the Corporation should continue to operate acting as a manager of fund managers, the Department considered that the Corporation should review its products and structures to enable it to meet its objectives. The Department's conclusion to retain the Corporation was based on the following key factors:

- given the shortage of talented staff in the expanding funds management industry, the centralisation of the management function performed by the best resources and improved prudential supervision were more likely to produce the best results for the State, similar to that achieved by the centralised public sector borrowing entity, the Treasury Corporation of Victoria; and
- centralisation will assist the larger bodies to concentrate on their core activities if they do not actively manage their investment portfolios, and will enable the achievement of economies of scale and cost savings.

**3.8.158** In forming the conclusion to retain the Corporation, the following options were considered by the Department:

- retention of the Corporation, with the establishment of a restructured board comprising members of the larger public sector investing agencies;
- closure of the Corporation with a wind-up cost of around \$4 million, if it was not possible to attract an extensive client base;
- closure of the Corporation but develop a limited funds management activity within the Treasury Corporation of Victoria; and
- collapse of the Corporation's operations back into the TAC with the possibility of creating a centralised fund management service at a later date.



□ *RESPONSE provided by Secretary, Department of Treasury and Finance*

*The original objective of the Department, when establishing the Victorian Fund Management Corporation (VFMC), was to create an organisation which would act as a central manager of funds managers for the public sector. This was also the VFMC's strategic direction. It was intended that the VFMC's clients would retain responsibility for determining their investment strategy which includes the setting of investment objectives, allocation of the portfolio between different asset classes and the establishment of risk and return targets. The VFMC's task was intended to be the selection of fund managers which were able to meet the requirements of the clients' investment strategy.*

*At the time the VFMC was established, it was envisaged that it would meet its objective through the implementation of a pooled investment product. The pooled product was not favoured or embraced by the VFMC's client base. This resistance was mainly due to the requirement of these products to be held in the name of the VFMC rather than in the name of the authority. The authorities reason seems to be at odds with current practice as the overseas portfolios of public sector authorities are generally in the name of the custodian and the authorities have invested in other pooled products.*

*Neither the Department's original objective nor the VFMC's strategic direction has changed. It is still the Department's objective that the VFMC operates as the central manager of fund managers for the public sector. To facilitate this objective, the Treasurer has appointed an interim Board which increased the representation of the VFMC's major client base. One of the tasks of the interim Board is to review the VFMC's products and structures which currently include pooled products and discrete portfolio management.*

*Restructuring of the Corporation's Board*

**3.8.159** Subsequent to the Department's assessment of the ongoing viability of the Corporation, and following an unsuccessful direct approach to the major potential clients of the Corporation, such as the Victorian WorkCover Authority and the Victorian Superannuation Board, to place their investment funds with the Corporation, in November 1995 the Treasurer announced the restructuring of the Corporation's Board. In particular, it was announced that an interim Board would be appointed to oversee the Corporation's operations for the following 12 months.

**3.8.160** Prior to the Government announcement, 4 of the 5 members of the former Board of the Corporation resigned and a new interim Board was subsequently appointed for a one year period. The members of the new Board now include the chief executive officers of the Corporation's potential major clients, namely, the Victorian WorkCover Authority, the Victorian Superannuation Board, and its major client, the Transport Accident Commission. In addition, a senior officer of the Victorian WorkCover Authority was seconded to perform the position of chief executive officer of the Corporation for a period of up to 12 months.

**3.8.161** While certain Board members are also involved in the strategic investment decision-making and the appointment of fund managers at the agency level, audit was pleased to note that the Board has moved quickly to overcome any possible conflicts of interest that may arise by resolving that where such circumstances prevail, the particular director will declare their interest and abstain from voting.



**□ RESPONSE** provided by Secretary, Department of Treasury and Finance

*The Board was restructured after discussions with the then VFMC Board and the Boards of the VFMC's major customers. The previous Board of the VFMC resigned so as to enable the VFMC's major customers to take a lead role in developing appropriate products to achieve the VFMC's strategic direction.*

*Subsequent increase in the Corporation's client base*

**3.8.162** In December 1995, subsequent to the interim Board's appointment, the Corporation entered into an agency arrangement with the Victorian WorkCover Authority, under which the Authority's investment funds were managed by the Corporation. As a consequence, as at 31 January 1996 the Corporation managed investments valued at \$6.7 billion on behalf of 5 public sector bodies, including the Transport Accident Commission (\$3.4 billion) and the Victorian WorkCover Authority (\$3 billion).

*Further initiatives to improve performance*

**3.8.163** Significant developments, which are summarised below, have occurred within the Corporation to improve its performance subsequent to the appointment of the Board by the Government:

- The corporate plan is currently being revisited by management and the Board in order to establish a clear strategic direction and effective implementation strategies. In the meantime, the investment and audit committees have been dissolved, pending the Board's re-assessment of the role and future direction of the Corporation, with the Board directly undertaking these roles;
- The *Umbrella Trust* product has been revised with the aim of improving the attractiveness of this product to clients. The revised product incorporates short-term money market and Australian fixed interest security portfolios and suspends, subject to review, all other specialist products; and
- Improvements have been made to the client service arrangement with the TAC which have resulted in an improved relationship with this major client. Further revisions to existing client service agreements are also likely to be made by the Corporation.

**3.8.164** Furthermore, in April 1996, the Board approved a revised organisational structure for the Corporation, aimed at improving client service delivery, and re-affirmed the future role of the Corporation as a manager of fund managers.

**Overall conclusion**

**3.8.165** The audit review concluded that in the first 18 months of operations, the Corporation had experienced substantial difficulties in attracting new clients to its business due to a number of factors, including the inability to establish a marketable investment product and a reluctance by public sector agencies to engage the Corporation due to the absence of a track record of performance. As a result, the initial Government expectations of annual savings of between \$16 million and \$24 million to the State from the Corporation's operations have not been realised, and are unlikely to be realised in the future unless revised products are successful in attracting a sufficient level of public sector investment and generate enhanced returns.

**3.8.166** Since the restructure of the Corporation's Board in November 1995, various initiatives have been commenced to establish appropriate products and structures for the Corporation. The effective implementation of these initiatives will be vital to the ongoing viability of the Corporation and to the achievement of cost-efficiencies to the public sector from centralised funds management.

*□ RESPONSE provided by Chief Executive, Victorian Funds Management Corporation*

*This Report contains a mixture of fact and opinion covering the period of pre-incorporation in 1993 until April 1996. It appears to contain certain matters to which the Corporation itself has not been privy. The Corporation does not wish to comment on Victorian Auditor-General's Office observations made with hindsight, save to say that it is working towards full implementation of current government policy within the competitive investment management environment prevailing in Australia.*

*It should be noted that the current volume of client funds under management is \$6.7 billion, which is a significant portion of the Victorian Auditor-General Office's own assessment of available aggregate public sector investments.*

*□ RESPONSE provided by Secretary, Department of Treasury and Finance*

*It has always been intended and is still intended that the VFMC acts a central manager of fund managers for the public sector. The interim Board is responsible for reviewing existing products and, if necessary, developing new products and structures to enable the VFMC to meet its objective.*



## UTILISATION OF PROPERTY

### Auditor-General's 1990 review of accommodation management

**3.8.167** An audit review of accommodation management was conducted in 1990. Details of the earlier audit are contained in the Auditor-General's *Special Report No. 14, Accommodation Management* tabled in the Parliament in October 1990.

**3.8.168** The 1990 Special Report concluded that substantial scope existed for improved management of accommodation facilities in both the budget and non-budget sectors. Key findings from the review included:

- many State properties had remained vacant or underutilised for a number of years;
- lack of forward planning with accommodation strategies focused on cost containment in the short-term;
- low priority had been given to the maintenance or upgrade of State buildings over many years resulting in their poor condition and substantially diminished capital value;
- significant areas of owned accommodation space in the Melbourne central business district and city fringe were inappropriately used for storage purposes;
- certain leased facilities had remained vacant for extended periods primarily due to delays in the fitout of premises or inadequate planning for future accommodation requirements; and
- major deficiencies in accommodation management information systems.

**3.8.169** At the time of the Auditor-General's 1990 review responsibility for the management of budget sector-owned and leased accommodation generally rested with the then Department of Property and Services (DPS). These responsibilities have since been assumed by the Victorian Government Property Group (the Property Group) of the Department of Treasury and Finance.

**3.8.170** Since 1990 there has been a more commercial approach to management of public sector accommodation with the devolution of responsibilities to individual agencies. Agencies have gained responsibility for the management of leased facilities in country and suburban locations while the Property Group has concentrated its efforts and expertise on major accommodation arrangements in the Melbourne central business district (CBD) and city fringe. Rental budgets have been devolved to individual agencies.

**3.8.171** The Property Group now charges rent and recoups outgoings, such as power and security costs, from agencies on owned and leased properties under its management.

**3.8.172** There has been a significant reduction in the Property Group's staffing levels compared with the former DPS, through the contracting-out of a variety of accommodation services, including cleaning, security, engineering and telecommunications to the private sector.



**Objectives of the audit review**

**3.8.173** A further review of property management has been conducted with the overall objective to provide information and recommendations for the more efficient, effective and economic management of the property portfolio under the control of the Property Group, with a primary focus on office accommodation. Special regard was given to the following areas, including the follow-up of related findings contained in the 1990 Auditor-General's Special Report:

- strategic planning and policy;
- utilisation of property; and
- information systems and performance management.

**3.8.174** A review of property management, following on from the 1990 Auditor-General's Special Report, was first suggested by Mr Fergus Ryan in his 1992 *Report on Performance Audit of the Auditor-General of Victoria pursuant to Section 48B of the Audit Act 1958*. Subsequently, a review of property management was also suggested by representatives of the Department of Treasury and Finance. The decision to conduct the review was taken by the Auditor-General after having consulted with Parliament's Public Accounts and Estimates Committee.

**Victorian Government Property Group**

**3.8.175** The Property Group consists of 2 parts, namely, Government Accommodation and Commercial Property.

**3.8.176** Government Accommodation's overall objective is to facilitate the provision of operationally efficient and cost-effective office accommodation to government agencies. Government Accommodation provides strategic planning, leasing and property management services for the State's owned and leased property portfolio.

**3.8.177** Commercial Property's main objective is to identify and sell surplus and underutilised assets and maximise the financial returns to the State from its property portfolio.

**Property portfolio**

**3.8.178** Table 3.8N summarises the property portfolio under the management of the Property Group as at 31 December 1995. At that date, the Property Group was responsible for the management of 56 State properties, comprised of some 176 000 square metres with an annual imputed rental value of approximately \$18.7 million. In addition, the Property Group managed 121 property leases totalling approximately 405 000 square metres with annual rental costs of \$86.6 million.

**3.8.179** As the Table indicates, a large proportion of accommodation under the Property Group's management is located in the CBD (45 per cent by area, 54 per cent by cost) and city fringe (31 per cent by area, 30 per cent by cost). The relatively low total average rental value for State properties in part reflects the poor condition of a number of these properties.

**TABLE 3.8S  
ACCOMMODATION MANAGED BY THE  
PROPERTY GROUP AS AT 31 DECEMBER 1995**

| <i>Location/Property type</i> |          | <i>Annual rental</i> | <i>No. of leases/<br/>buildings</i> | <i>Area</i>       | <i>Average rent per m<sup>2</sup></i> |
|-------------------------------|----------|----------------------|-------------------------------------|-------------------|---------------------------------------|
|                               |          | (\$m)                |                                     | (m <sup>2</sup> ) | (\$)                                  |
| CBD                           | - State  | 6.23                 | 10                                  | 47 207            | 132                                   |
|                               | - Leased | 51.80                | 35                                  | 212 551           | 244                                   |
| City fringe                   | - State  | 8.29                 | 15                                  | 72 984            | 114                                   |
|                               | - Leased | 22.82                | 27                                  | 111 209           | 205                                   |
| Suburban                      | - State  | 0.97                 | 3                                   | 15 783            | 62                                    |
|                               | - Leased | 9.96                 | 33                                  | 68 882            | 145                                   |
| Country                       | - State  | 3.22                 | 28                                  | 39 668            | 81                                    |
|                               | - Leased | 1.45                 | 21                                  | 11 859            | 122                                   |
| Interstate                    | - State  | -                    | -                                   | -                 | -                                     |
|                               | - Leased | 0.56                 | 5                                   | 891               | (a) 623                               |
| <b>Total</b>                  |          | <b>105.30</b>        | <b>177</b>                          | <b>581 034</b>    | <b>-</b>                              |

(a) Largely relates to shopfront offices leased for Tourism Victoria.

Source: Property Group property records.

**3.8.180** As a result of the delegation of responsibilities to individual agencies, the number of leases managed by the Property Group has fallen by 278 since 1990 although the total leased space has remained relatively static (having reduced by approximately 13 500 square metres). There has also been a reduction in the number of State properties managed by the Property Group, falling to 56 from 67 in 1990, a loss of approximately 60 000 square metres. According to advice provided by the Property Group, individual agencies directly managed and paid for 317 leases in suburban and country areas as at 31 December 1995.

### **Strategic planning and its implementation**

#### *City Precinct Strategic Plan*

**3.8.181** The Auditor-General's 1990 review found that a low priority had been given to forward planning for accommodation requirements, with the main focus placed on short-term cost containment. This had resulted in the application of substantial funds towards leasing accommodation from the private sector while many State buildings remained underutilised and in need of substantial capital outlays to upgrade them to an efficient operating condition.

**3.8.182** It is pleasing to report that the Property Group has since prepared a strategic plan for the management of the Government's leased and owned accommodation in the Melbourne CBD and city fringe. The purpose of the plan is to provide directions and a strategic context for future accommodation decision-making through to the year 2000.



**3.8.183** The City Precinct Strategic Plan is aimed at consolidating and rationalising government departments' office accommodation in the CBD and city fringe in a cost-effective manner over time while taking account of the existing owned and leased property portfolio and property market opportunities. Based on the realisation of certain strategic assumptions, in particular a 36 per cent reduction in leased and State accommodation, it has been estimated by the Property Group that recurrent rental savings could grow to approximately \$32 million a year by 1999-2000 over 1993 levels. The overwhelming majority of the planned space reductions are targeted to occur between 1995 and mid-1999. At the date of preparation of this Report, a number of the strategic components of the Plan had not been finalised.

**3.8.184** The key strategy principles of the plan are:

- Development of medium and long-term accommodation strategies which will lead to consolidation of each government department in a single building or single precinct in a cost-effective manner;
- Target major lease expirations to reduce leased accommodation commitments in line with public service staff reductions;
- Minimise new lease commitments reflecting the downsized public service;
- Consideration to be given to accommodation in strategically placed properties owned by certain statutory bodies;
- Lease renewals or replacements generally to concentrate in the Melbourne CBD except where suburban or regional locations are required by government policies;
- New leases or renewals to lock away favourable market conditions to provide long-term benefits;
- Retention of core cost-effective State buildings provided proper refurbishment and ongoing maintenance funds can be secured. Properties will otherwise be disposed of unless special reasons exist for their retention; and
- Space allocation based on a functional needs basis stressing flexibility, open planning principles and minimum office enclosure.

*Long-term preventative maintenance program*

**3.8.185** The City Precinct Strategic Plan notes that certain owned buildings within the Treasury Reserve hold a special benefit for government operations through their strategic location close to Parliament. Funding submissions to the Budget and Expenditure Review Committee under the Plan have included funding requests for renovations to Treasury Reserve properties. To date, funding has been provided for the renovation of some of the properties on the Treasury Reserve precinct.



**3.8.186** The funding requirements for renovation of the Treasury Reserve properties are extensive, due in part to their poor condition after many years of neglect and the failure to provide adequate maintenance budget allocations in the past. These funding limitations have largely resulted from the absence of a long-term systematic approach to maintenance through the development of a preventive maintenance program to support maintenance funding submissions. The lack of adequate preventive maintenance of assets, and appropriate refurbishment programs, leads to an escalation in building costs over time with the incidence of costly emergency repairs and higher operating costs such as energy and cleaning until a point is reached where extensive renovations are required.

**3.8.187** The need for long-term preventative maintenance programs was previously raised in the Auditor-General's 1990 Special Report and earlier Auditor-General's Reports have also referred to the absence of a planned approach to maintenance with regard to the various types of assets including buildings.

**3.8.188** A key strategic principle of the City Precinct Strategic Plan involves the need to secure funding for ongoing property maintenance. The Property Group, however, has not developed and costed a long-term preventative maintenance program for incorporation in the Plan. This is a necessary prerequisite to obtaining Budget commitment for the long-term maintenance of publicly-owned properties. In these circumstances, there is a very real risk that those properties which have recently received significant funding for renovation may again fall into disrepair over the longer-term while other current property holdings continue to deteriorate and remain underutilised.

**3.8.189** **In audit opinion, the Property Group should give high priority to the development of a long-term preventative maintenance program for those State properties which are to be retained. This maintenance program and its estimated ongoing cost should be incorporated in current and future accommodation management strategic plans.**

**3.8.190** This would also ensure that the Property Group is well placed to comply with the Minister for Finance's recent guideline issued under the *Building Act 1993* which requires that all government buildings meet private sector standards within 5 years, be safe and fit to occupy, and be capable of delivering their full potential in supporting the delivery of services.

**□ RESPONSE** *provided by Secretary, Department of Treasury and Finance*

*A high priority is being given to the development of a long-term preventative maintenance program for the core government-owned offices that are to be retained. The funds for implementing the program will be included in the annual update of the strategic plans and budget bids.*

.....

## Monitoring of policy implementation by the Property Group

**3.8.191** The 1995-96 Budget Speech introduced a range of measures to reduce budget sector outlays by up to \$500 million over the next few years through continued expenditure restraint, improved productivity and increased efficiency in the utilisation of resources. The \$32 million rental savings estimated under the City Precinct Strategic Plan are a contributing factor to the achievement of the Government's overall savings objective.

**3.8.192** The Property Group is responsible for the achievement of savings targets envisaged under the City Precinct Strategic Plan. As a result, it is essential that the Property Group fulfil an ongoing monitoring role over the effective implementation of the Plan. This is especially important given that a number of the assumptions upon which the original savings forecasts were based have been subject to change as the plan has been put into effect. Further, as detailed below, the monitoring of accommodation space usage within the sector by the Property Group forms an integral and essential element in ensuring the successful implementation of the City Precinct Strategic Plan and the efficient and effective utilisation of space.

### *Accommodation space standard and usage levels*

**3.8.193** Government guidelines were developed in 1984 to assist departments and agencies in the design, development and procurement of office accommodation. The guidelines, although not mandatory, included space allocation entitlements determined by the former Department of Property Services which stipulated that a maximum average office space allocation of 15 square metres per person had been adopted by the then Government as a standard.

**3.8.194** The Auditor-General's 1990 Special Report found that there was widespread non-compliance with this standard with an overall average allocation per person in the CBD at that time of 20 square metres.

**3.8.195** In keeping with the City Precinct Strategic Plan's space allocation principles, the Property Group reviewed workspace guidelines during 1994-95. The re-drafted workspace guidelines were subsequently issued to departments for comment during June 1995. At the date of preparation of this Report the guidelines have yet to be formally adopted.

**3.8.196** The re-drafted guidelines sought to simplify workspace standards to reflect the broadbanded non-executive structures introduced in the public service during 1994-95. Enclosed offices were to be allocated on a functional needs basis as opposed to previous allocations based on staff classification levels and open planning was to be adopted wherever practicable. However, the same overall space allocation target of 15 square metres per person adopted in 1984 was retained.

**3.8.197** Audit analysis of Property Group data for the CBD and city fringe disclosed that overall average accommodation space per person had actually increased to 25 square metres at June 1993 from 20 square metres per person previously reported by the Auditor-General in 1990. The overall average space usage has remained stable between 1993 and 1996 at just over 25 square metres per person, which indicates that space reduction during this period (of approximately 15 per cent) has kept pace with the reduction in public service numbers (of approximately 16 per cent) for the CBD and city fringe.

**3.8.198** The City Precinct Strategic Plan includes forecasts up to 1999 based on preliminary estimates of property holdings and staff numbers. If key strategic assumptions are realised, in particular a 36 per cent reduction in leased and owned accommodation, the average space allocation per person in 1999 would approximate the level reported by the Auditor-General in 1990, that is an overall average of approximately 20 square metres per person.

*□ RESPONSE provided by Secretary, Department of Treasury and Finance*

*The space allocation target of 15m<sup>2</sup> per person overall, remains the target and the basis on which the accommodation strategy has been based. The move toward use of workstations to more efficiently utilise floorspace and reduce the number of enclosed offices, will lead to a reduction in area occupied per person. This, together with the implementation of the strategy for consolidation of government departments in new leased or refitted government-owned premises, should result in achievement of this target by 1999.*

*Incentive scheme*

**3.8.199** The 1990 Auditor-General's accommodation management review found that the former Department of Property Services (DPS), while scrutinising departmental space utilisation levels at the time of arranging or renewing accommodation arrangements, did not sustain a monitoring function throughout the duration of a department's accommodation occupancy. It was recommended that the DPS regularly monitor agency compliance with the Government's space guidelines and assess whether initiatives had resulted in the more efficient use of space.

**3.8.200** In responding to the Auditor-General's 1990 recommendation, the DPS advised that a new initiative which had been introduced from 1 July 1990 would provide an incentive for agencies to monitor their own accommodation usage and relinquish or better utilise accommodation where possible. This initiative related to the re-allocation of previously centralised rental budgets to individual agencies as part of an overall government policy to devolve more responsibility directly to departments, while increasing their accountability. A key element of this initiative was to provide agencies with an incentive to improve their management of accommodation by allowing them to retain the first year rental savings from any efficiency gain on the utilisation of space. Over time, this incentive was expanded to allow departments to retain first year savings on accommodation outgoings, such as electricity, which were also subsequently budgeted directly to agencies.



**3.8.201** Unfortunately, audit analysis of Property Group data suggests that there has not been any significant benefit gained from the introduction of the incentive scheme, as indicated by the substantial increase in the overall average space usage per person. One possible reason for the apparent failure of the incentive scheme is that accommodation costs and possible savings incentives may not have been significant in the context of a department's total budget. As a result, the effort involved in achieving savings on these costs could have been seen as somewhat insignificant in the context of a department's overall operations. In audit opinion, another possible contributing factor to the failure of the incentive scheme has been the lack of accountability imposed on departments to justify their current space allocation levels.

**3.8.202** A further incentive for departments to focus on their use of accommodation was introduced subsequent to the Auditor-General's 1990 Special Report, in the form of a capital charge. Departments will incur a capital charge on all asset holdings under their management from 1996-97. It should be noted that the capital charge was first introduced in 1994-95 but its application was limited to new capital works undertaken by departments. The partial capital charge was an interim measure pending finalisation of departmental asset registers to coincide with the introduction of accrual reporting by all departments in 1996-97.

**3.8.203** The purpose of the capital charge is to make departments aware of the value of all assets and the costs associated with their custody and use, while improving the costing of services. The capital charge will also act as an incentive for departments to reduce their usage of accommodation by more efficient asset portfolio performance through rationalisation and higher utilisation levels of asset holdings. It is too early to judge the success or otherwise of this incentive in encouraging real and substantial reductions in accommodation levels.

**□ RESPONSE** provided by Secretary, Department of Treasury and Finance

*It is not accepted that there have been no significant benefits gained from the introduction of the incentive scheme. On the contrary, it is estimated that rental savings of some \$11 million per annum have already been achieved, through the implementation to date, of the City Precinct Strategic Plan. The savings have generally been absorbed by the relevant Departments or applied to other priority program areas, through the budget process.*

*From late 1995 it has been decided that as a matter of Government policy, savings achieved through implementation of the strategic plan will be taken from Department recurrent budgets as overall savings in Government expenditure.*

.....

### Monitoring of accommodation usage

**3.8.204** The DPS also stated in their response to the 1990 Special Report that "... a program of direct audit and monitoring activities will be carried out to identify the key pockets of poor utilisation and greater potential savings". At another point in the 1990 Special Report the DPS further commented that:

*"The Department [DPS] will audit space utilisation under the new delegation of financial and leasing responsibilities to agencies. Agencies will be encouraged to measure space utilisation and the Department will provide consultant advisory services to assist departments achieve space and cost savings on their accommodation".*

**3.8.205** As occurred with its predecessor, the Property Group provides advice to departments when they are arranging or renewing accommodation arrangements, which takes into account the space standard guidelines. **However, in contrast to the response provided to the previous Special Report, the Property Group does not sustain any regular or formalised monitoring function over utilisation levels throughout the period of an agency's accommodation occupancy.** The Property Group has instead concentrated on the development and implementation of the City Precinct Strategic Plan.

**3.8.206** Departmental compliance with the Government's Workspace Guidelines is not compulsory. However, the accountability envisaged by the Government under the devolution of responsibilities to departments cannot be properly established without the existence of a central monitoring function. The establishment of a compliance monitoring function is especially important in relation to the achievement of the savings targets envisaged in the City Precinct Strategic Plan as they are fundamentally linked to the successful application of the space allocation principles embodied in the workspace guidelines. The Auditor-General's November 1993 *Special Report No. 26: Investment Management* recognised that compliance monitoring was fundamental to the establishment of accountability in stating that:

*"... the effectiveness of any guidelines depends, to a large degree, on the effectiveness of compliance monitoring procedures established to support the guidelines. Such monitoring not only provides incentive to agencies subject to the guidelines to achieve compliance but also provides information vital to the assessment of the extent to which the guidelines have met their objectives".*

**3.8.207** The Commission of Audit in its 1993 review of the State's finances expressed similar views when it reported that there were no *enforced* policies or guidelines over agencies' asset management functions.

**3.8.208** The Property Group is considered to be the most appropriate body to fulfil a central monitoring role over departmental compliance with accommodation space standards as it is responsible for the successful implementation of the City Precinct Strategic Plan and formulated the workspace guidelines. Further, the Group is well placed to undertake this compliance monitoring role given its skill base and the fact that its accommodation management information system (AMIS) has the facility to record staff numbers and area occupied.





**3.8.209** In summary, it is recommended that:

- the Property Group routinely monitor and report on the level of utilisation of accommodation through regular information requests and random space audits;
- periodic reporting of the Property Group's findings on accommodation usage should be made to the Minister responsible for implementation of the City Precinct Strategic Plan, currently the Minister for Finance; and
- the revised Workspace Guidelines be submitted for Ministerial endorsement and formal adoption as soon as possible.

□ *RESPONSE provided by Secretary, Department of Treasury and Finance*

*Although agencies are now charged rent for office accommodation occupied (both leased and Government owned) it is acknowledged that there needs to be appropriate monitoring of space usage, to ensure efficient and effective utilisation of the space and related facilities. An appropriate monitoring and review process will be developed in consultation with agencies. Periodic reporting on accommodation usage will be included in the reporting of the implementation of the Strategic Plan.*

## **Utilisation of properties**

### *Vacant space and definition of dead rent*

**3.8.210** One of the key performance indicators monitored by the Property Group is the extent of dead rent incurred in respect of both State and leased property. The Property Group, however, adopts a very narrow definition of "dead rent" which precludes reporting on a significant number of instances of under-utilisation of properties, particularly related to owned properties.

**3.8.211** The Property Group view is that dead rent only occurs where a property or space of lettable size is vacant, not subject to fitout and is "suitable" for accommodation. Under this definition, for example, any vacant properties/areas currently deemed suitable only for storage purposes would be excluded from dead rent, as would properties in poor condition, properties under fitout and those awaiting refurbishment.

**3.8.212** In audit opinion, all vacant space of a lettable size should be reported as dead rent or similarly classified for reporting purposes as vacant and therefore under-utilised. It is not appropriate that a property be excluded from dead rent calculations due to its "unsuitability", especially in cases where such unsuitability has resulted directly from a failure to adequately maintain the property in the past.

**3.8.213** The Property Group's interpretation of dead rent was also subject to comment following a 1993 management consultant's review of the Group's asset management function. The consultants, in their report entitled *Review of the Property Asset Management Function for Department of Finance*, 23 November 1993, noted the distorted view provided when using the Property Group's interpretation of dead rent. They observed that the Group did not run State buildings on a commercial basis due to the fact that a number of buildings had been allowed to run down to a stage where they were not suitable for accommodation. When excluding these unsuitable buildings, they found that the dead rent ratio was at a satisfactory level. However, the dead rent ratio rose substantially if all State buildings were included and was well outside commercially acceptable benchmarks.

**3.8.214** Further, audit's view is consistent with that of the Commonwealth Joint Committee on Public Accounts (JCPA). The JCPA's April 1987 Report defined dead rent as including "... any rent paid for unoccupied office and other accommodation space. This includes the portion paid on properties undergoing fit-out".

**3.8.215** **Audit considers that the level of dead rent reported by the Property Group has been substantially understated.** Table 3.8T illustrates the substantial differences in the levels of dead rent as reported by the Property Group and calculated by audit. As can be seen from the table, by far the largest variances between the level of dead rent calculated by the Property Group and audit relate to owned properties.

**3.8.216** **As a ratio of dead rent over total rent, the Property Group had calculated dead rent at 2.65 per cent for State properties and 1.5 per cent for leased properties for the 6 months to 31 December 1995. This compares with audit's estimates for the same period of dead rent at 23 per cent on State properties and 3.6 per cent on leased properties.**

**TABLE 3.8T**  
**DEAD RENT COSTS**  
(\$'000)

| <i>Year/Property type</i>    | <i>Dead rent<br/>(per the<br/>Property<br/>Group)</i> | <i>Additional<br/>dead rent<br/>(per audit)</i> | <i>Total</i> |
|------------------------------|-------------------------------------------------------|-------------------------------------------------|--------------|
| 1994-95 -                    |                                                       |                                                 |              |
| Owned                        | 658                                                   | 6 194                                           | <b>6 852</b> |
| Leased                       | 873                                                   | 588                                             | <b>1 461</b> |
| <b>Total 1994-95</b>         | <b>1 531</b>                                          | <b>6 782</b>                                    | <b>8 313</b> |
| To 31 Dec. 1995 -            |                                                       |                                                 |              |
| Owned                        | 223                                                   | 1 929                                           | <b>2 152</b> |
| Leased                       | 517                                                   | 1 033                                           | <b>1 550</b> |
| <b>Total to 31 Dec. 1995</b> | <b>740</b>                                            | <b>2 962</b>                                    | <b>3 702</b> |



**3.8.217** It is recommended that all vacant space of a lettable size should be costed and reported by the Property Group as "dead rent". The reporting of this cost could be classified under separate categories of "dead rent" such as:

- dead rent incurred or imputed on leased and State properties of a lettable size;
- dead rent incurred or imputed on leased and State properties undergoing fit-out; or
- dead rent incurred or imputed on properties withdrawn from service (sub-classified by reason for withdrawal, e.g. poor condition) and/or currently deemed to be unsuitable for accommodation purposes.

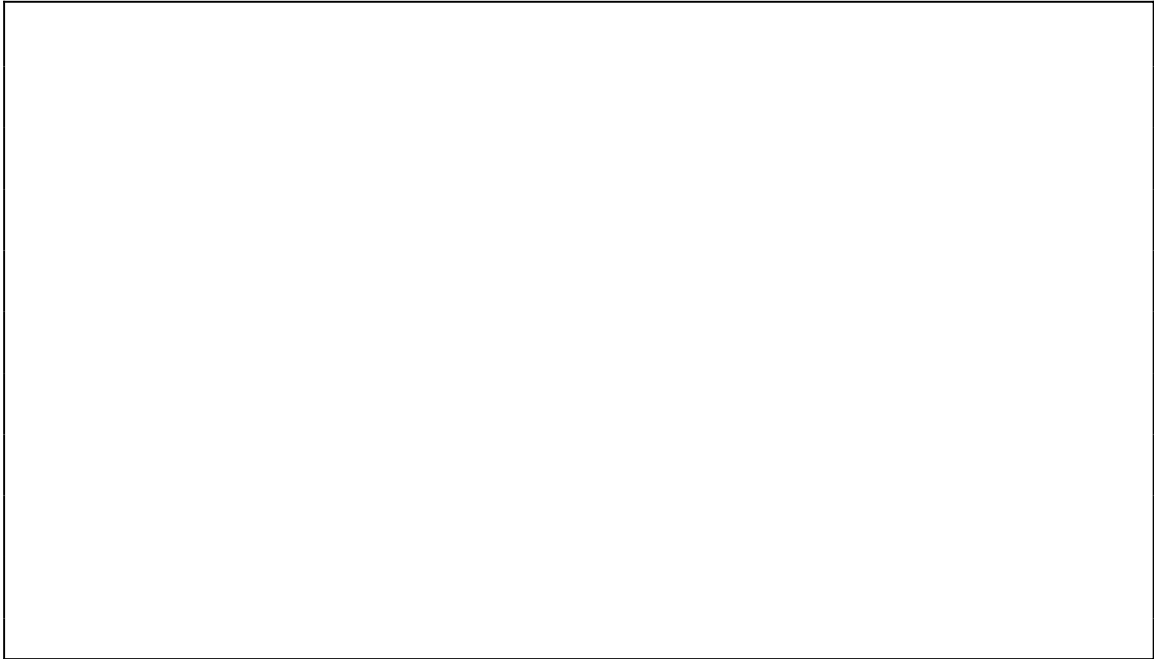
**3.8.218** Currently, the Property Group's AMIS system is unable to automatically produce dead rent reports for management. Existing dead rent reports are manually prepared using data extracted from the AMIS system. It is recommended that the AMIS system be modified so that dead rent reports are automatically produced.

*□ RESPONSE provided by Secretary, Department of Treasury and Finance*

*The current definition used for identifying areas of dead rent is generally consistent with practices adopted by BOMA and the property industry. Nevertheless, audit's suggestion is accepted, that rent applying to areas under fitout or refurbishment should be reported. Notional rent applying to properties withdrawn from service as offices, if they are used for a new function, i.e. storage, will also be reported. However, the term "dead rent" is not applicable under industry standards and will not be applied to these categories of costs. Properties withdrawn from use for disposal or demolition will also not be included as the disposal decision has been taken.*

### Treasury Reserve

**3.8.219** The condition of properties within the Treasury Reserve illustrates the possible consequences of not reporting certain classes of vacant space as dead rent. The Treasury Reserve is an area of East Melbourne bound by Spring Street, Treasury Place, Macarthur Street and St Andrews Place. The Auditor-General's 1990 Special Report noted this prime city area had been substantially under-utilised for many years, largely due to the poor condition of the properties. It was found that they were in need of urgent repairs to bring them in line with then current building regulations and enable them to be effectively used.

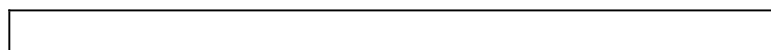


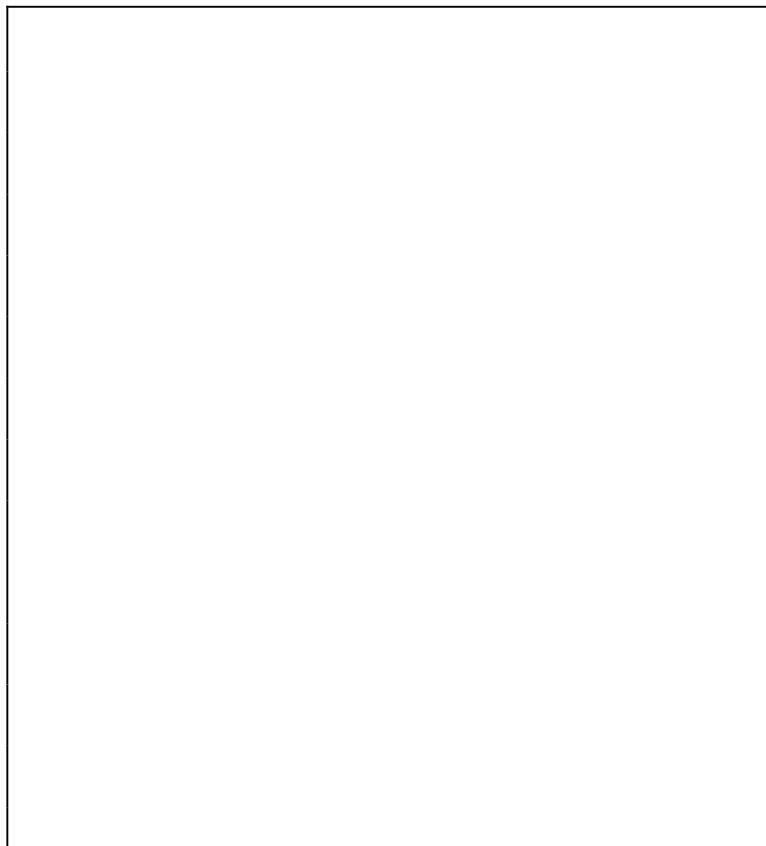
*Aerial view of Treasury Reserve.*

**3.8.220** It is pleasing to report that the Property Group has incorporated funding requests in the City Precinct Strategic Plan for many Treasury Reserve properties. In particular, recent renovation works at 1 Treasury Place and 1 Macarthur Street have been completed. Capital works have also been budgeted for the refurbishment of 3-5 Macarthur Street and some upgrade work has commenced at 2 Treasury Place. It should be noted, however, that significant future funding allocations will be required to bring 2 Treasury Place up to an acceptable level of operational efficiency. In addition, other Treasury Reserve properties currently remain in a state of under-utilisation and significant disrepair.



*2 Treasury Place, East Melbourne.*





*2 Treasury Place, East Melbourne.*

**3.8.221** While acknowledging that a corrective action program for a number of Treasury Reserve properties commenced in 1994-95 under the City Precinct Strategic Plan, in audit opinion, the deterioration in the condition and utilisation levels of these properties over many years has largely resulted from the Property Group and its predecessors' failure to recognise the cost of such under-utilisation in the disclosure of dead rent. As these properties represent a capital investment of public funds, it is essential for the purposes of public accountability and effective government decision-making processes that the return or otherwise on these investments is adequately reported.

*27 Francis Street, Melbourne*

**3.8.222** The property at 27 Francis Street, Melbourne was originally purchased in 1986 for \$7.5 million with a further \$900 000 spent on fit-out. Although the property was not specifically designed for laboratory or office purposes, at the time of purchase it was considered suitable for short-term use as a government laboratory until a new facility was constructed in the outer suburbs. The Auditor-General's 1990 Special Report found the 4 floor building to be significantly underutilised with only 70 officers accommodated in the 6 700 square metres of floor space and a large proportion used for the storage of documents. It was concluded that its use as a laboratory and storage facility was inappropriate and highly inefficient.

**3.8.223** A DPS assessment of the building concurred with audit findings. It was determined by the DPS that the building was not a suitable location for laboratories in the long-term with some 36 per cent of available space inappropriate for office or laboratory use. Under the circumstances, the DPS concluded that storage was the only

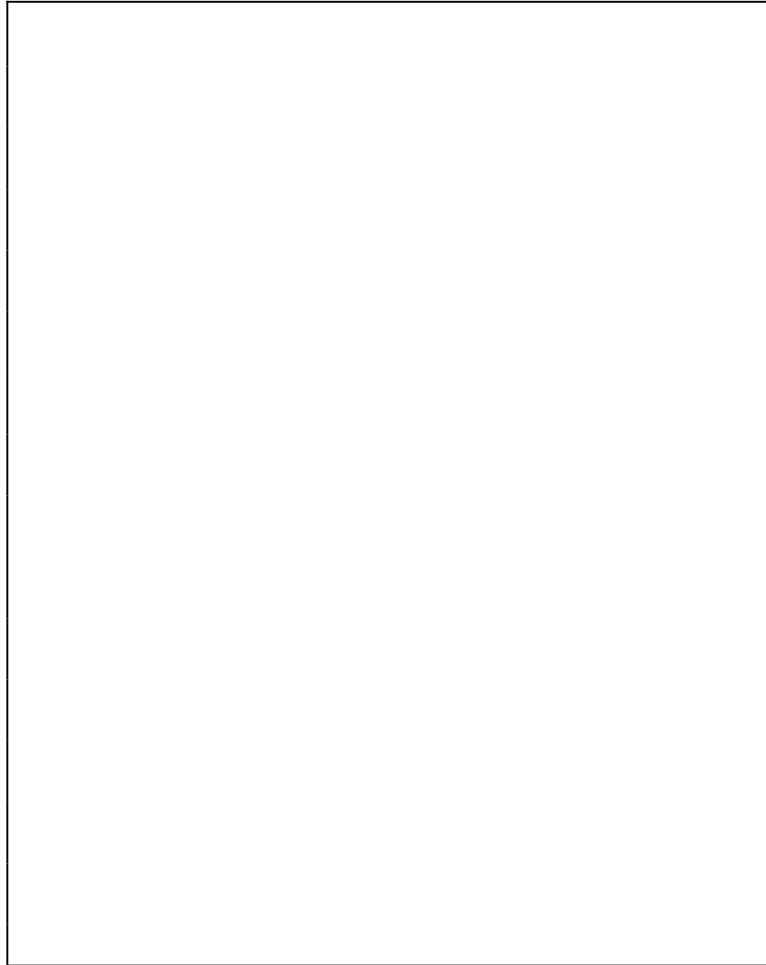
.....

viable option while a detailed analysis was required to determine the long-term costs and benefits of various options for disposal or refurbishment.

**3.8.224** Audit's current review of the property found that the situation had remained virtually unchanged from 1990, apart from some improvement in the total area utilised. Data extracted from the Property Group's accommodation management information system disclosed that 43 per cent of the property's floor space was devoted to storage, 37 per cent to laboratories, with 11 per cent used for offices and the remaining 9 per cent vacant. The principal tenant in current occupancy of the property is the Environment Protection Authority with various other agencies utilising some areas mainly for storage purposes.

**3.8.225** Since 1990, the Property Group has considered a number of proposals for the future use of the premises. Originally, the Property Group proposed that the Environment Protection Authority remain at 27 Francis Street until 1999 when a lease expired on other premises occupied by the Authority's administrative section. This would then have allowed the Authority to consolidate its operations in a single property.

**3.8.226** However, the Property Group has expressed concerns over the deteriorating condition of the building. Scaffolding is currently erected around the building's facade to protect the public from potential injury. As a result, the Property Group now considers it preferable for the Authority to move into alternative premises as soon as possible in order that the property can be disposed of. This proposal is dependent on the provision of funding estimated at \$3 million to establish the Authority's laboratory facilities elsewhere. **At the date of preparation of this Report, a funding decision on the property's future was yet to be made.**



*Part of facade of 27 Francis Street, Melbourne.*

*Storage*

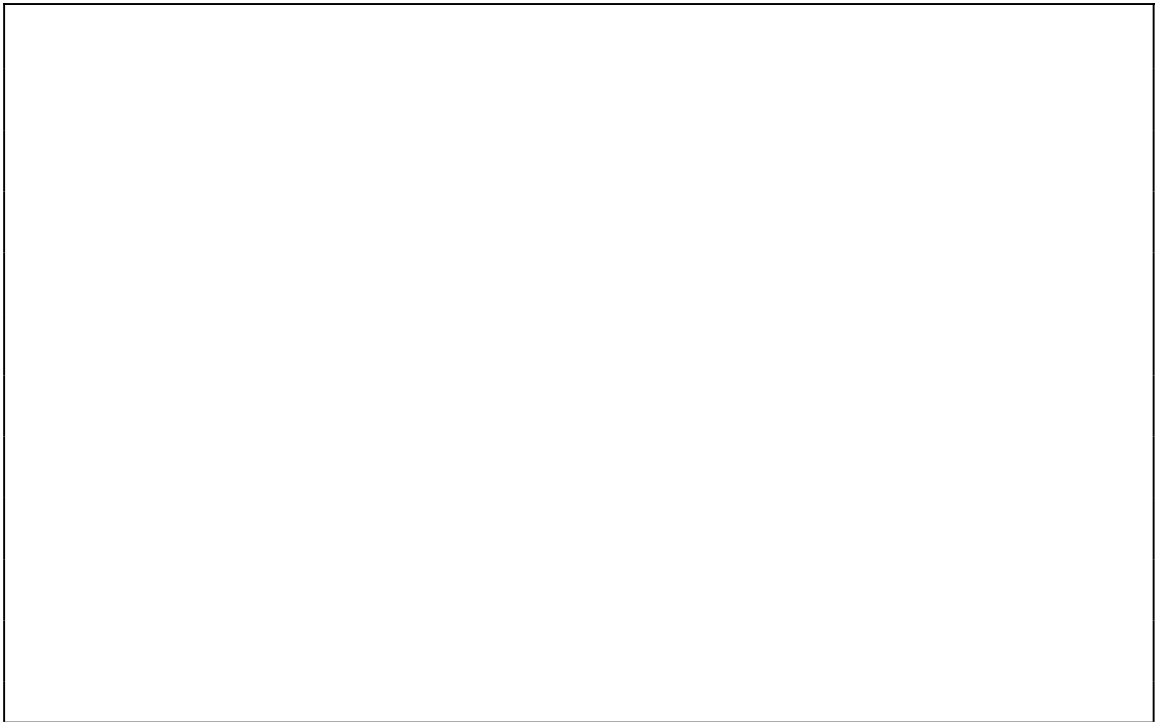
**3.8.227** The Property Group's information systems revealed that, at January 1996, **there has been a significant reduction in the level of relatively high cost CBD and city fringe properties being used for storage purposes when compared with that previously reported in the Auditor-General's 1990 Special Report.** This has largely been brought about through the destruction of non-current departmental records and the transfer of others to the Public Records Office suburban storage site at Laverton as permanent archival records. The Property Group has also contributed to the achievement of savings on storage during the planning phase of departmental accommodation projects by ensuring storage decisions are appropriate to the operational needs of departments.

**3.8.228** **Audit did note, however, that large areas of a number of owned properties located in St Andrews Place, East Melbourne are primarily utilised for storage purposes,** as disclosed below:

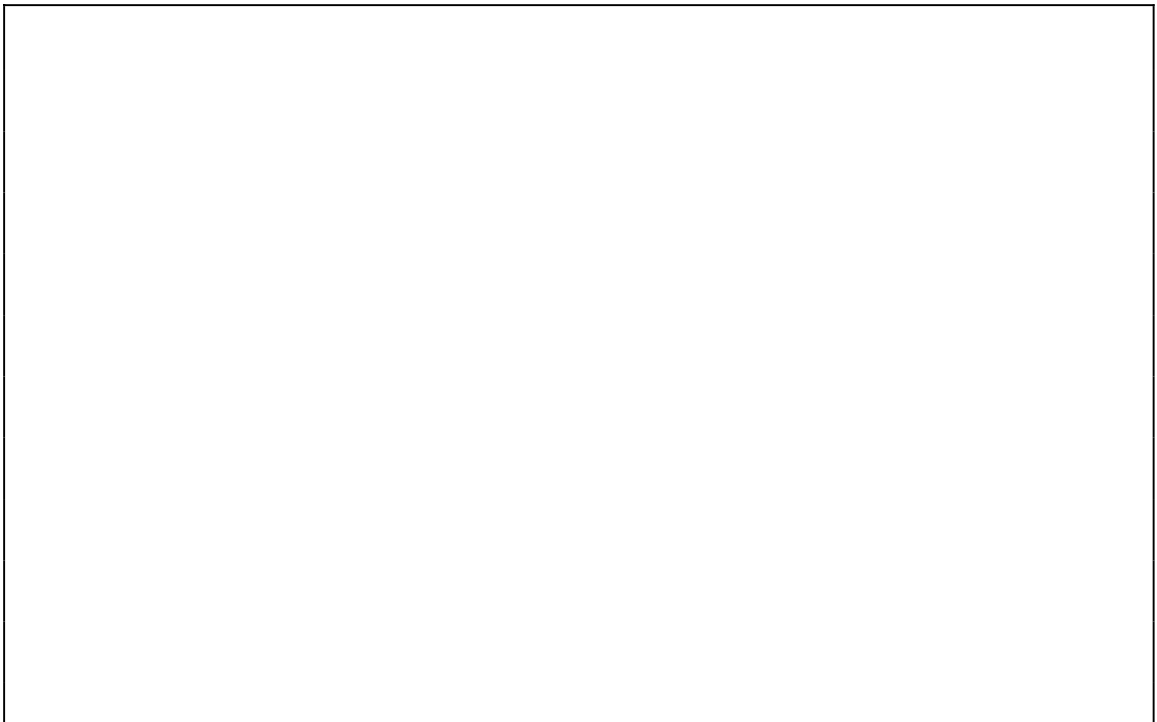
- 17 St Andrews Place - 46 per cent of net floor space is devoted to storage.
- 41 St Andrews Place - 35 per cent of net floor space is devoted to storage.
- 43 St Andrews Place - 50 per cent of net floor space is devoted to storage.



**3.8.229** According to the Property Group, both 41 and 43 St Andrews Place are heritage buildings.



*Ground floor storage of furniture at 43 St Andrews Place, East Melbourne.*



*41 St Andrews Place, vacant space.*



**3.8.230** In addition to the St Andrews Place properties, as already noted previously in this Report, 27 Francis Street, Melbourne is also being used for storage purposes.

**3.8.231** In audit opinion, the continued utilisation of the 3 St Andrews Place properties primarily for storage purposes is inefficient and represents a poor return on the State's capital investment.

*□ RESPONSE provided by Secretary, Department of Treasury and Finance*

*Consideration is being given to whether 43 St Andrews Place and 17 St Andrews Place should be demolished. The property at 41 St Andrews Place is not considered cost-effective for refurbishment to contemporary office accommodation and alternative uses such as storage are being considered.*

*Properties awaiting sale*

**3.8.232** Responsibility for the Government's asset sales program generally rests with the Property Group. The information presented in Table 3.8U was extracted from the Group's information system and illustrates the trend in recent years in the value of those assets awaiting sale.

**TABLE 3.8U  
ASSETS AWAITING SALE,  
TO 14 MARCH 1996**

| Year            | Number<br>of<br>properties | Estimated<br>value (a)<br>(\$m) |
|-----------------|----------------------------|---------------------------------|
| 1993-94         | 988                        | 130.5                           |
| 1994-95         | 919                        | 129.3                           |
| 1995-96 to date | 833                        | 93.6                            |

(a) Estimates are not directly comparable from year to year as assets are recorded at differing values dependent on when a valuation was last undertaken.

**3.8.233** According to the Property Group, various factors have contributed to the high level of assets awaiting sale, including:

- poor quality of many assets within the portfolio;
- low demand for development properties;
- depressed state of the property market;
- unavoidable delays in the preparation of certain property titles and the finalisation of related legal matters; and
- continuing additions to the number of assets awaiting sale as departments identify further surplus assets.

**3.8.234** The length of time that assets have been waiting on the assets sales program is illustrated in Table 3.8V. As the table discloses, the total estimated value of assets awaiting sale at 14 March 1996 was \$93.6 million.

**3.8.235** There is a significant opportunity cost attached to the capital tied up in surplus or underutilised assets. Audit estimated that, based on the Government's



current capital charge rate, the annual opportunity cost of assets awaiting sale under the Property Group's management, based on levels at 14 March 1996, is approximately \$7.5 million.

**3.8.236** The Property Group recently reviewed all of its assets awaiting sale to identify those properties that were considered inappropriate for sale. Reasons for properties being deemed inappropriate for sale included, for example, poor condition, sale costs likely to exceed sale proceeds and legal complications. As a result of this review, approximately 400 properties with a recorded value of some \$38.5 million included in Table 3.8V were classified as inappropriate for sale.

**TABLE 3.8V  
ASSETS AWAITING SALE,  
AS AT 14 MARCH 1996  
(\$million)**

| <i>Year approved for sale</i> | <i>Estimated value</i> |
|-------------------------------|------------------------|
| Prior to 1990-91              | 12.9                   |
| 1990-91                       | 15.5                   |
| 1991-92                       | 13.3                   |
| 1992-93                       | 12.9                   |
| 1993-94                       | 10.4                   |
| 1994-95                       | 19.5                   |
| 1995-96 to date               | 9.1                    |
| <b>Total</b>                  | <b>93.6</b>            |

**3.8.237** It should be noted that the Property Group's records for assets awaiting sale date from when government approval was given for their sale and not from the time they were originally identified as surplus or underutilised. As a consequence, possible unnecessary delays between the identification of surplus or underutilised assets and their subsequent approval for sale have not been identified.

**3.8.238** It is recommended that consideration be given to recording dates when assets are originally identified as surplus or underutilised on the Property Group's information systems. In this way management would be able to identify unreasonable delays incurred, if any, in obtaining approvals for sale and determine measures to eliminate such delays in the future thus limiting opportunity costs associated with assets awaiting sale.



**3.8.239** While the Government's asset sales program was not a major focus of the current audit review, it became apparent that there was a lack of co-ordination of sales activities under the program. Although the Property Group has primary responsibility for the asset sales program, various other agencies undertake asset sales directly, including the Directorate of School Education, the Department of Conservation and Resources (now part of the Department of Natural Resources and the Environment), the Office of Major Projects (now part of the Department of Infrastructure) and the various Transport Authorities. At 30 June 1995, an additional \$75.5 million of assets awaiting sale were under the control of agencies other than the Property Group.

**3.8.240** A major risk associated with an unco-ordinated approach to the sale of government properties is the potential for the property market to become flooded with surplus public sector assets at the one time. In these circumstances it is highly likely that the financial returns achieved on asset sales on behalf of the State will not be maximised.

**3.8.241** During 1996, one agency released some 186 urban and rural property sites onto the market at the same time. Such major releases of properties onto the market underline the importance of ensuring appropriate co-ordination of sales programs occurs to avoid any possibility of conflict with other agencies' asset sales activities, which may reduced overall sales proceeds to the State.

**3.8.242** In light of the substantial value of assets awaiting sale, it is felt that a review of the operations of the assets sales program is warranted. Consideration could be given, as part of this review, to the centralisation of the management and control of the asset sales program under a single agency to ensure that the financial returns to the State from the sale of properties are maximised. Further, implementation of the asset sales program by numerous agencies represents some duplication of effort and a consequential loss of potential economies of scale.

*Lease incentives*

**3.8.243** There has been a trend in recent years with the favourable rental market for landlords to provide public sector agencies with lease incentives to secure their tenancy over long periods. These incentives have taken various forms including rent-free periods, cash payments and free fitouts.

**3.8.244** For some years public sector agencies have entered into rental agreements involving the provision of cash-lease incentives. Three recent cases of rental agreements involving the provision of cash-lease incentives by landlords have occurred since June 1993:

- **The Government entered a lease agreement on 55 Collins Street, Melbourne, in August 1994. According to Property Group records this lease, which is for a 10 year term, involved a \$10 million cash incentive payment to the State, paid in 1995;**



- The State also received a further lease incentive for entering into a 10 year lease agreement commencing in January 1996 for 555 Collins Street, Melbourne from the State Superannuation Board. This lease incentive totalled \$13.5 million consisting of a \$3.5 million rental reduction over the period of fitout and a \$10 million cash payment.
- The Port of Melbourne Authority, as lessor, provided a lease incentive totalling \$26.4 million to the State as consideration for entering into a lease agreement for space within the World Trade Centre, commencing in August 1993. The payment was to contribute to the cost of refurbishment works and the cost of fitout. The lease incentive was received in instalments between August 1993 and February 1995.

**3.8.245 Lease incentives provided by landlords are recovered through subsequent rental payments. Under such arrangements the Government tenant in effect repays the incentive by paying a higher rental.**

*□ RESPONSE provided by Secretary, Department of Treasury and Finance*

*Lease incentives are disappearing from the market and leases are now negotiated on the basis of a genuine effective rent. Funding for fitout of leased premises is now provided through the Government's capital works program.*

**Information systems and performance management**

*Accommodation Management Information System*

**3.8.246** The Auditor-General's 1990 Special Report highlighted a number of information limitations associated with the property management systems utilised by the DPS at that time, including:

- details of occupancy were not systematically updated;
- there was lack of information on the physical condition of buildings;
- there were no details on major works or refurbishments undertaken;
- energy and maintenance costs were not recorded for individual buildings; and
- the useful life expectancy of buildings was not detailed.

**3.8.247** At the time of the 1990 audit review a new multi-user accommodation management information system, referred to as AMIS, was under development. The system was to provide integrated financial and property data.

**3.8.248** Ongoing development work has continued on AMIS up to the present with further system enhancements completed as the nature of the Property Group's operations changed. Key features of AMIS and the timing of their implementation are:

- On-line multi-user property management system became fully operational in July 1992 replacing personal computers and providing occupancy details and creditor payment data for expenditure leases;



- AMIS enhanced in September 1992 to allow charging government tenants rent and outgoings on leased properties, included apportionment of costs, accounts payable and accounts receivable facilities. Government tenants charged rent on owned properties from July 1993 and outgoings from July 1995;
- Revenue (private and non-budget sector) tenants incorporated in AMIS with associated leasing-out facilities implemented in July 1994;
- September 1994 AMIS enhancement to accommodate secondary tenants in owned and leased properties; and
- AMIS interfaced with the Department of Treasury and Finance's financial management system (Oracle) in July 1995 to allow financial data on accounts payable, accounts receivable and general ledger balances for individual properties to be provided through Oracle. The development of profit and loss statements for individual properties is near completion which will allow portfolio-wide and individual property performance monitoring and reporting, including monitoring against Building Owners and Managers Association of Australia's (BOMA) benchmarks and budgets. The BOMA chart of accounts incorporated in AMIS in July 1995 to record details of revenues and outgoings incurred and apportioned for individual properties.

**3.8.249** The development of AMIS has made a significant contribution to the level of information available to the Property Group for performance monitoring and management decision-making purposes. While AMIS has addressed many of the audit concerns raised in the 1990 review, it is felt that further action is required in relation to the following information limitations:

- Details of occupancy continue to be limited to when accommodation arrangements were originally made or renewed. The lack of systematic update of occupancy details limits the usefulness of this information for management purposes. More importantly, as previously discussed in this Report, there is a risk that the savings targets established by the Property Group under the City Precinct Strategic Plan will not be achieved without central monitoring of departmental compliance with accommodation space standards. It is therefore critical that the Property Group utilise the facilities currently available on AMIS to monitor departmental staff numbers against space usage;
- The Property Group's property management systems do not record information on the age, physical condition and useful life expectancy of State buildings. The Victorian Commission of Audit in reviewing agencies' asset information systems concluded that poor management decisions may be made (e.g. buildings retained past their economic life) where the physical condition and useful life expectancy of assets was not recorded and monitored. In keeping with the ongoing monitoring of the physical condition of buildings, the Property Group's systems should detail property inspections and their outcomes;

- While AMIS, a lease management system, records details of expenditure incurred on property minor works, there are no project control systems in place to monitor minor works, refurbishment costs and other costs (including rent incurred during fit outs) against budget and actual work progress against planned timelines. The former DPS's information systems had facilities to monitor and report on rent incurred during the fit out of leased properties and minor works planned commencement/completion against actual times achieved, however, these facilities have been withdrawn;
- At the time of the current audit review, AMIS did not have the capacity to maintain historical property data to allow property occupancy details, payment details or property performance to be monitored over an extended period of time. The Property Group, therefore, has not been in a position to undertake any trend analysis on property performance over time which may have adversely impacted on the management decision-making process and the efficient utilisation of properties. This system limitation has since been addressed with an AMIS update module under development and planned for implementation in July 1996;
- No provision has been made to record and apportion the Property Group's administration costs against individual properties in the profit and loss statements to be produced under AMIS. As a consequence, the Property Group has not been in a position to fully monitor and evaluate the efficiency of their operations against established benchmarks (BOMA) when their own administration costs are not taken into account in the management of individual properties. This would allow the Property Group to compare its performance against established BOMA property administration costs benchmarks; and
- The AMIS system is currently unable to automatically produce dead rent reports for management. Existing dead rent reports are manually prepared using data extracted from the AMIS system.

#### *Standard management reports and performance indicators*

**3.8.250** AMIS has the capacity to produce a wide variety of reports for use by property managers and senior management. A limited number of standard reports are currently received by senior management on a periodic basis, such as dead rent and summary accommodation statistics.

**3.8.251** It is considered that the overall efficiency and effectiveness of the Property Group's operations would be improved if the following reports were produced on a regular basis, in a summarised form, for senior management (audit acknowledges that some of the suggested reports listed below may currently be produced on an ad hoc basis by property and portfolio managers or may otherwise be produced in the future when property profit and loss statements are fully operational):

- cost of the Property Group's operations compared with industry benchmarks;
- trends in property outgoings and comparison against industry benchmarks;
- rental rates incurred or charged above or below market rates or other relevant benchmark levels;
- trend in cost of space (cost per square metre) in the CBD and city fringe;
- average accommodation space per person;



- progress against cost budgets and timelines for major and minor works, refurbishments and fit outs;
- ageing of departmental debtors;
- ageing of properties available for sale;
- portfolio profit and loss reports and actual to budget summary reports;
- summary report on key property usage totals, such as storage;
- summary report on property condition by pre-determined classification; and
- date and overview result of last property inspection.

### Promotion of client services

**3.8.252** The objectives of the Victorian Government Property Group were outlined earlier in this part of the Report. Briefly, the Property Group provides a wide range of services to client agencies including:

- management of owned and leased premises primarily within the CBD and city fringe;
- strategic planning and development of guidelines aimed at assisting departments to better deliver their programs;
- consultancy advice and project management services to facilitate the provision of appropriate and cost efficient accommodation and associated services;
- overseeing project management consultancy services for the planning and construction of office fit outs in owned and leased premises; and
- provision of technical advice and a broad range of property services in leased and owned accommodation including cleaning, security, caretaking, telecommunications, parking, energy management and air-conditioning maintenance.

**3.8.253** In today's environment with increased pressure on agencies to continually enhance performance and provide improved client service, the Property Group needs to become more pro-active in promoting the range of services it offers clients. To this end, it is suggested that the Property Group develop an overall marketing strategy. This would also assist the Group to instil an even greater commercial focus in its operations.

**3.8.254** As part of this process, consideration should be given in the first instance to the publication of promotional literature to current and potential clients detailing all property management services provided together with relevant personnel contact names and telephone numbers.

**3.8.255** Ultimately, it is considered that the Property Group should move towards an even more commercial mode of operation involving full cost recovery and fee-for-service user charges for all property management services provided. This would serve as a discipline on the Property Group and allow meaningful comparison of its performance against other government providers and the private sector.



## FINANCIAL STANDING OF WORKCOVER

**3.8.256** The Victorian WorkCover Authority, the body responsible for the administration of the Victorian workers' compensation scheme, commenced operations on 1 December 1992 as part of the Government's reform agenda. On that date, the Authority acquired the assets and liabilities of the former Accident Compensation Commission, which had \$2 billion of unfunded liabilities relating to its workers' compensation scheme, representing a funding ratio of only 48 per cent, and was projecting a deficit of \$244 million for the 1992-93 financial year.

**3.8.257** The Authority was created as the regulatory body responsible for the management of the new WorkCover scheme as a result of amendments to the *Accident Compensation Act* 1985.

**3.8.258** The key objective of the Government's reform program was to re-orientate the scheme into a socially responsible and financially viable workers' compensation scheme. However, to implement this objective, the Authority faced the difficult task of changing Victoria's "compensation" culture, which was often seen as a "reward" for injury, to a "return to work" culture. The workplace attitudes which had developed under the former scheme were evidenced by Victoria's poor workers' compensation experience.

### Funding position of the WorkCover scheme

**3.8.259** When the Government announced the reforms, it anticipated that the WorkCover scheme would be fully funded within 5 years of its inception, i.e. it would have sufficient funds to fully cover all outstanding liabilities by December 1997. However, this milestone has been achieved by 30 June 1995, some 2½ years ahead of that anticipated. Table 3.8W highlights the financial performance of the scheme for the last 5 financial years.

**TABLE 3.8W**  
**FINANCIAL PERFORMANCE OF THE WORKCOVER SCHEME**  
**FOR THE 5 YEAR PERIOD ENDED 30 JUNE 1995**  
((\$millions))

| <i>Item</i>                                                                         | 1990-91   | 1991-92   | 1992-93    | 1993-94  | 1994-95 |
|-------------------------------------------------------------------------------------|-----------|-----------|------------|----------|---------|
| Operating revenue                                                                   | 1 406.5   | 1 321.3   | 1 356.2    | (a)942.2 | 1 107.1 |
| Operating expenditure (including movement in outstanding claims and abnormal items) | 749.8     | 1,364.1   | (b)(110.0) | 827.5    | 753.9   |
| Net Profit/(Loss)                                                                   | 656.7     | (42.8)    | 1,466.2    | 114.7    | 353.2   |
| Net assets                                                                          | 1 528.0   | 1 721.2   | 1 858.3    | 1 971.1  | 2 582.3 |
| Net outstanding claims liability                                                    | 3 347.0   | 3 583.0   | 2 254.0    | 2 252.0  | 2 510.0 |
| Accumulated surplus(deficit)                                                        | (1 819.0) | (1 861.8) | (395.7)    | (280.9)  | 72.3    |
| Funding ratio                                                                       | 45.7%     | 48%       | 82.4%      | 87.5%    | 102.9%  |

(a) Reduction in operating revenue from the prior year is mainly attributable to a reduction in the average premium rate and a downward revaluation of the market value of investments.

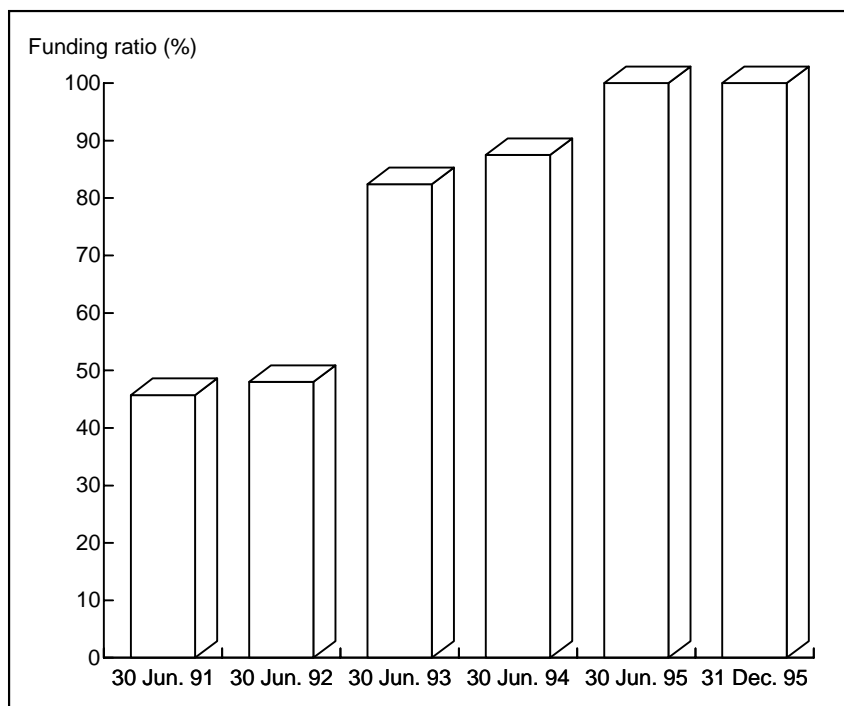
(b) Result affected by a \$1 094 million reduction in outstanding claims liability due to legislative changes.





**3.8.260** The WorkCover scheme's funding ratio (value of scheme's assets compared with the outstanding claims liability), which was only 48 per cent as at 30 June 1992, increased to 102.9 per cent as at 30 June 1995. This ratio has increased further as at 31 December 1995 to 104.4 per cent. Chart 3.8X illustrates the improvement in the Scheme's funding position since the 1990-91 financial year.

**CHART 3.8X  
FUNDING POSITION OF THE SCHEME,  
1 JULY 1990 TO DECEMBER 1995**



**3.8.261** The key reasons for the early achievement of the scheme's fully funded status were:

- The Government's legislative reforms, which provided for:
  - **a change in the entitlement criteria and benefit structure** to compensate claimants for injuries sustained in the workplace, which effectively constrained compensation available to workers and has resulted in a reduction in the number and duration of claims, which in turn led to a reduction in claim payments;
  - **the introduction of premium incentives** to reduce the number and severity of claims; and
  - **a change in the strategic management of the scheme**, including the introduction of competition and the concept of re-insurance.
- **Marketing and education campaigns** to assist in creating safety awareness, preventing injuries and promoting earlier returns to work following absenteeism caused by injuries sustained;

- **Sound performance from the Authority's investment portfolio.** Over the period from 1 July 1992 to 30 June 1995, the Authority earned a return of 9.1 per cent on its investment holdings, which averaged \$2.5 billion over this period. As at 31 December 1995, the Authority's investment holdings was \$3 billion, which generated a return of 7.6 per cent for the 6 month period from 1 July 1995; and
- **The transfer by the Authority of surplus assets of approximately \$260 million from the Supplementation and Guarantee Funds to the WorkCover Fund** during the financial year ended 30 June 1995. These funds were established under previous workers' compensation legislation, with the Authority, as the successor-in-law to the former Accident Compensation Commission and the former Victorian Accident Rehabilitation Council, having responsibility for their management.

### Legislative reforms

**3.8.262** The *Accident Compensation Act* 1985 was substantially amended over a 2 year period from 1992 to 1994, to take account of the Government's reform program for the Victorian workers' compensation scheme. The legislative reforms have brought about a changed culture within the workers' compensation industry. Specifically, the reforms have been aimed at:

- making return to work, rather than the continued payment of weekly compensation, the main objective of the scheme;
- adequately and fairly compensating injured workers;
- reducing the cost of workers' compensation by re-introducing employer liability for the associated costs and requiring employers to insure their liability with private sector licensed insurers;
- introducing an experience-based premium system under which workplace claims performance is a critical factor in determining an employer's premium;
- introducing measures to streamline existing provisions of the Act, especially in critical areas such as claims management; and
- making the Victorian workers' compensation industry consistent with other States and increasing its relative efficiency.

**3.8.263** The Government has indicated that further reforms will occur with the possible privatisation of the scheme, when it has become fully funded and stable.

*Changes to benefits*

**3.8.264** A major focus of the Government's reform program was on employee benefit entitlements. Comments follow on the more significant of these reforms.

*Basis for compensation*

**3.8.265** A number of changes have occurred which have effectively limited entitlements of workers to receive compensation. While in the past, injured workers were entitled to compensation regardless of even the most minor work contribution to the injury, following the reforms, workers are only eligible for benefits if the worker's employment is a "*significant contributing factor*" to the injury.

**3.8.266** In addition, injuries incurred while travelling to and from work, known as journey claims, and claims for stress arising wholly or predominantly from disciplinary or other such action by an employer, are no longer eligible for compensation.

*Benefit levels and duration*

**3.8.267** Under the reform program, weekly benefits were re-focused to provide greater financial support for the more seriously injured workers, with greater incentives for injured workers to return to work at the earliest possible time, through:

- raising the benefit levels from 80 per cent to 95 per cent of pre-injury earnings in the first 26 weeks of incapacity;
- increasing long-term benefits for seriously injured workers from 80 per cent to 90 per cent of pre-injury earnings;
- introducing a scale of benefit levels after a post-injury period of 6 months to reflect varying degrees of incapacity and seriousness of injury; and
- ceasing the payment of weekly benefits to partially incapacitated workers after a period of 2 years. As benefits cease, workers are provided with a financial incentive to return to work, unless they can substantiate that they are seriously injured or totally and permanently incapacitated. Under the previous WorkCare scheme, no such time limit on the payment of benefits was in place.

*Common law eligibility and lump sum payments*

**3.8.268** Thresholds for common law eligibility were introduced through the enactment of legislative amendments effective on 1 December 1992. The Scheme, as a no-fault system, now restricts common law damages to a "*serious injury*" which is defined as "*an injury resulting in a 30 per cent or more impairment to the body*". However, common law damages were extended for seriously injured workers to include loss of earning capacity, where an injury was due to negligence of an employer or another person.

**3.8.269** For injured workers not eligible for common law payments, lump sum benefits are provided under the legislation, based on the medical condition of the injured worker. In addition, the *Table of Maims* incorporated in the legislation, has been expanded and a new lump sum benefit has been introduced specifically for pain and suffering.

.....

### *Rehabilitation*

**3.8.270** Rehabilitation reforms were designed to increase the role of the employer in the return-to-work process by making the employer, or the insurer as the employer's agent, responsible for implementing and managing return-to-work strategies for injured workers, with specific regard to occupational rehabilitation. Where possible, the employer is now required to provide injured workers with suitable employment within the first 12 months of injury or face a monetary penalty. In addition, a *'Return to Work Plan'* must be developed by the employer for injured workers who have not worked for 20 days or more. Previously, occupational rehabilitation services had either been provided or approved by the former Victorian Accident Rehabilitation Council.

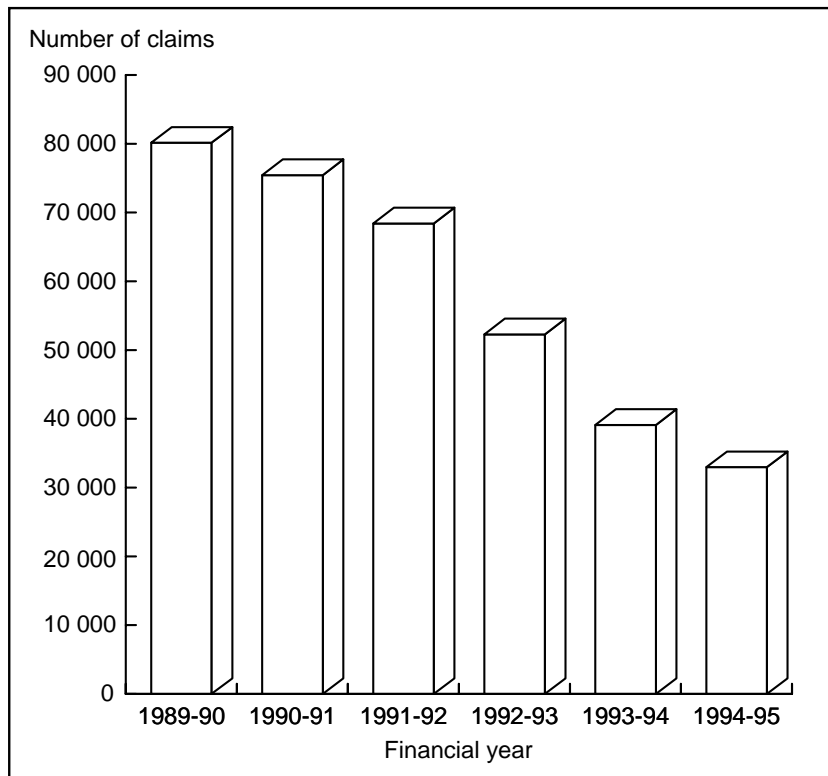
### *Dispute Resolution*

**3.8.271** A conciliation process was introduced as part of the reforms as an avenue for resolving disputes relating to claims. This non-adversarial service offers an informal and free forum for parties to a dispute to try to resolve their differences. Changes to the dispute resolution system have reduced the need for legal representation in the initial stages of the dispute process.

### *Reduction of claims*

**3.8.272** Since the 1989-90 financial year, the number of reported workers' compensation claims has been reduced by almost 60 per cent. As shown in Chart 3.8Y, the highest rates of decline in the number of reported claims occurred following the creation of the new WorkCover scheme during the 1992-93 financial year.

**CHART 3.8Y**  
**NUMBER OF REPORTED CLAIMS,**  
**1989-90 TO 1994-95 (a)**



(a) Represents claims that have been lodged with an authorised insurer (prior to 1 December 1992, known as claims agents) for which the Authority has a liability or against which expenses have been incurred or are expected to be incurred.

**3.8.273** Due to the reduction in reported claims and changes in benefit levels, the Authority experienced a significant decline in the value of claim payments since the implementation of the new scheme. In particular, there has been a reduction of approximately 37 per cent in gross claim payments between the years ended 30 June 1993 and 30 June 1995, with payments reducing from \$1.1 billion to \$684 million, respectively.

**3.8.274** A report by consultants engaged by the Authority concluded that the decline in the number of claims made since the introduction of the WorkCover scheme was due to a combination of the following factors:

- journey claims are no longer compensable under the WorkCover scheme;
- changes in the eligibility criteria for benefits and the associated payment levels for employees; and
- other considerations such as culture changes by employers, workers and health providers.

.....

*Change in management of the scheme*

**3.8.275** The Authority previously performed the role of both regulator and service provider for the workers' compensation scheme. However, the reform program has resulted in a change in its role, with the service provision function now being delivered by authorised private sector insurers. This change has enabled the Authority to focus more closely on the overall regulation of the scheme rather than its administration.

**3.8.276** Under the revised arrangements, in July 1993, licences were granted to 16 authorised private sector insurers to enable them to enter into contracts of insurance with employers, under policies approved and premiums set by the Authority. In addition, the authorised insurers are also required to manage claims, collect premiums and provide occupational rehabilitation and risk management services to Victorian employers and workers.

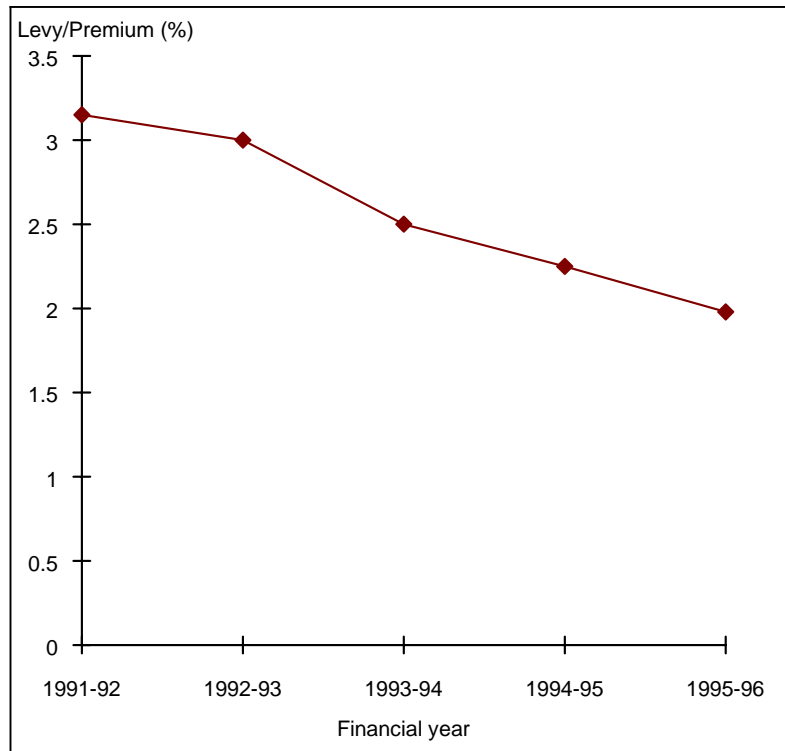
**3.8.277** Employers are required to insure against their workers' compensation liability with an authorised insurer. These insurance contracts are in turn backed by a re-insurance agreement between the Authority and the authorised insurers, which provides for the Authority to reimburse the insurers for claims expense and to receive insurance premiums collected from employers in consideration for re-insurance.

*Premium incentives and surcharge*

**3.8.278** In July 1993, the Government introduced an *experience-based system* for the determination of workers' compensation premiums payable by employers, which effectively abolished the previous levy-based system. The new premium system is designed to offer employers with an incentive to reduce workplace injuries, as the premium is calculated using a number of risk factors including the costs associated with previous injury claims, the total remuneration payable by the employer, and the workplace and industry injury rate. The objective of this reform was to link claim costs to premiums payable.

**3.8.279** Since the 1991-92 financial year, premium rates payable by Victorian employers have declined by 40 per cent, representing an annual saving of around \$600 million to Victorian employers. Chart 3.8Z highlights the decrease in the premium rates payable by employers since the 1991-92 financial year.

**CHART 3.8Z**  
**AVERAGE PREMIUM/LEVY PAYABLE**  
**BY EMPLOYERS AS A PERCENTAGE OF PAYROLL COSTS**



**3.8.280** As a means of reducing the level of unfunded liabilities of the former WorkCare scheme, in July 1993, the Government introduced a 25 per cent surcharge to be levied on employers, in addition to the premium payable to the Scheme. Given the improved financial standing of the Scheme, the Government reduced the surcharge to 10 per cent for the 1995-96 financial year. Subsequently, the Government announced that the surcharge will be completely eliminated from 1 July 1996.

**3.8.281** Due to the structure of the premiums payable by employers, there is a strong incentive to employers to return injured workers to the workplace and also to prevent injuries occurring.

**Marketing campaigns**

**3.8.282** Prevention of work-related injuries is a major focus of the Authority. In this regard, advertising and marketing campaigns have been utilised by the Authority to assist in establishing a culture of safety within Victorian workplaces. The Authority has undertaken a variety of marketing initiatives, comprising television and radio commercials, posters, displays and outdoor advertising, with the aim of communicating messages to the public associated with changes to the WorkCover scheme, reducing the duration of time that injured workers remain away from work and preventing workplace injuries. The major advertising campaigns have included *"WorkCover's working to stop injuries"*, *"Quiet Tragedy"* and *"Safety - think it, talk it, work it"*.

.....

**3.8.283** Marketing expenditure incurred by the Authority in the period 1 July 1992 to 30 June 1995, has amounted to approximately \$14.6 million. It is anticipated by the Authority that it will incur a further \$6 million for the "Return to Work" and "Safety - think it, talk it, work it" campaigns in the 1995-96 financial year.

**3.8.284** A performance audit on the utilisation of marketing campaigns across large government agencies, including the Authority, has been conducted by audit with the results included in *Special Report No. 39: Marketing government services - Are you being served?*, which was presented to the Parliament in May 1995.

**3.8.285** The performance audit has highlighted that the campaigns have been effective, based on performance indicators established by the Authority relating to improvements in return to work rates and the decline in the number and duration of claims. However, the review also found that the Authority was not able to quantify the impact of the "Return to Work" campaign on workplace attitudes, such as whether injured workers feel they are provided with appropriate support systems in the workplace and whether co-workers have positive attitudes to injured employees returning to work. In addition, the impact of other marketing activities such as posters, pamphlets, brochures and community education activities had not been formally measured by the Authority.

#### Future of the scheme

**3.8.286** The next stage of the Government's reform program relates to maximising competition in the workers' compensation industry by privatising the scheme.

**3.8.287** Since the introduction of the reform process, there has been significant improvement in the scheme's financial position. This enhanced performance has resulted in substantial benefits to employers through reduced premiums and the elimination of an additional surcharge that was previously levied to improve the Scheme's poor financial standing.

*□ NO RESPONSE provided to the issues raised.*





**UTILISATION OF CONSULTANTS IN THE PUBLIC SECTOR**

**3.8.288** The Auditor-General's May 1995 *Report on Ministerial Portfolios* outlined the results of an audit review which focused on the identification of the extent to which consultants were utilised in the Victorian public sector and included an assessment of the adequacy of processes established by individual agencies to manage and attain value-for-money from these engagements.

**3.8.289** Specifically, the review found that, based on information provided by public sector agencies, around \$115 million was spent by these agencies on the engagement of consultants during the 1993-94 financial year. However, it also identified that inconsistencies and confusion existed at the agency level in the interpretation of what constitutes "consultancies" as against "contractor services", which caused some uncertainty as to the actual level of expenditure incurred on consultants. Overall, the review concluded that significant value had been added by consultants in improving resource management by enabling the Government to make more informed decisions in key areas of reform.

**Action to improve annual reporting of expenditure on consultants**

**3.8.290** Following the May 1995 Report, the Government commenced action to clarify the distinction between consultancy and contractor services in order to enhance the usefulness of information required to be provided by agencies for annual reporting purposes as to the extent of utilisation of consultancies. In particular, in June 1995, the Government revised the *Guidelines for the Engagement and Management of Consultants* by enhancing the definition of consultancy and contractor services and including examples of such services in the guidelines to assist in the interpretation of the definition by agencies.

**3.8.291** The revised definition and examples of consultancy and contractor services, which were incorporated in the guidelines, were developed through a consultative process involving the Department of the Premier and Cabinet, other agencies and the Victorian Auditor-General's Office. While the revised definition will assist in providing clarification on the distinction between consultancy and contractor services, prior to the revision of the guidelines audit raised certain concerns in relation to one example included in the guidelines which is considered inappropriate and may lead to the understatement of expenditure on consultancy services. The example referred to, which is classified within the guidelines as a contractor service, is as follows:

*"An organisation engaged to implement government decisions to corporatise or privatise a government business enterprise".*

**3.8.292** The guidelines state that expenditure on such services would not meet the definition of a consultancy as the private provider would not be providing expert analysis and advice which facilitates decision-making in such instances. **It is audit's opinion that this example is ambiguous given that private providers could be engaged to implement high level privatisation, corporatisation or other policy decisions, involving the provision of expert advice or analysis of various implementation options etc. In cases involving the provision of expert advice or analysis of options, it is audit's view that this element of the engagements would be more appropriately classified as consultants.**

**3.8.293** In August 1995, the Victorian Government Purchasing Board within the Department of Treasury and Finance assumed policy responsibility for the utilisation and management of consultants. In particular, the Board's responsibilities cover the development, implementation and review of policies and practices relating to the supply of goods and services, only in respect to departments. The Board has incorporated the *Guidelines for the Engagement and Management of Consultants* into its *Supply Policy and Guidelines Manual* which outlines the policies and practices to be followed by departments in relation to the procurement of all goods and services. However, at the date of preparation of this Report, the abovementioned matter remained unresolved.

**3.8.294** To ensure the proper classification of consultancy and contractor services by agencies for annual reporting purposes, consideration needs to be given by the Board to the clarification of the abovementioned illustrative example within the supply guidelines.

### Agency compliance with reporting requirements

**3.8.295** The Government Guidelines and Ministerial Directives issued under the *Financial Management Act 1994* require public sector agencies to observe the following disclosure requirements for consultancy services within their annual reports to the Parliament:

- for consultancies during the year costing in excess of \$50 000, a schedule listing the consultants engaged, particulars of the project involved, the total fees incurred and future commitments in relation to each consultancy; and
- for consultancies during the year costing less than \$50 000, the aggregate number and cost of these engagements.

**3.8.296** An audit review of a sample of budget and non-budget sector agency annual reports found that a small number of these agencies had not observed the reporting requirements for the 1994-95 financial year. In particular, audit identified instances where non-budget sector agencies had either not disclosed within their annual reports any consultancy information, associated expenditure commitments or the number of consultants engaged in the year.

**3.8.297** Given the non-compliance by some agencies with the annual reporting requirements relating to consultancy services, it is important that action be taken by the Department to reinforce the reporting requirements and therefore improve disclosure to the Parliament in future years.



□ **RESPONSE** provided by Secretary, Department of Treasury and Finance

*The Government took steps to clarify the distinction between consultancy and contractor services in order to improve the usefulness of information gathered for annual reporting purposes. The "Guidelines for the Engagement and Management of Consultants" were revised to clarify the definitions of consultant/contractor.*

*The Department of Premier and Cabinet, your Office and several other agencies participated in a consultative process and developed the revised definition, along with illustrative examples. However, it is noted that your Office is concerned with one of the examples which you believe to be inappropriate. You have recommended that consideration be given by the Victorian Government Purchasing Board to clarifying this example in the Board's Supply Policies and Guidelines. That particular example is being re-examined and several options have already been discussed. The Board will convene a meeting of its officers and officers of the Department of Premier and Cabinet and the Victorian Auditor-General's Office to review the example.*

*It should be noted that any change that is made to the example will also need to be reflected in Part 9 of the Directions of the Minister made under the Financial Management Act 1994 which outlines reporting requirements under the Act and includes the definitions and examples of consultant/contractor.*

*With regard to the Supply Policies and Guidelines, you will be aware that the Board is responsible for drafting policies (and any amendments to these policies), with the Minister for Finance having final approval. The Board's responsibilities for supply policy development, implementation and review, are confined to inner-budget departments. However, all public sector agencies are required to follow disclosure requirements for consultancy services under the Government Guidelines and Ministerial Directives in Part 9. This matter raises a broader issue of possible benefits in having the Government extend the application of the Board's Policies and Guidelines to outer-budget agencies. This will be the subject of a separate review within Government.*

*The requirements covering the reporting of consultancy costs incurred by public sector bodies are widely and clearly notified through the Directions of the Minister for Finance under the Financial Management Act 1994. Investigations have been made with the non-compliant bodies to avoid future occurrences. The investigations indicate that they were aware of the reporting requirements with 3 bodies actually disclosing aggregate details.*



## AMENDMENT TO THE CASINO LICENCE

**3.8.298** Following a government decision to allow a casino to operate in Victoria and a subsequent detailed assessment process, the State Government on 19 November 1993 granted a licence to operate a casino in Melbourne to Crown Limited. The licence fee offered and accepted was for \$200 million with additional taxation of \$57.6 million payable over a 3 year period.

**3.8.299** The casino is to be located in a new building complex currently being constructed by Crown on public land at Southbank. The land has been leased from the Government for a 40 year period at a nominal annual rental of \$1.

**3.8.300** While awaiting completion of the new building complex, Crown has operated a casino from temporary facilities at the Galleria which forms part of the World Trade Centre. The casino commenced operations from the temporary facilities on 30 June 1994.

**3.8.301** Since the casino license was originally granted, the licence agreement has undergone a number of amendments, which will enable the complex to be much larger than the one proposed when the original licence was granted. The proposal upon which the original licence was based involved a casino with an associated 361 room hotel, extensive entertainment facilities, a retail precinct and undercover parking for 3 000 cars. By 1995, the project had evolved into a much larger entertainment and retail complex with a 1 000 room hotel and undercover parking for 5 400 cars.

### Overview of events relating to the casino

**3.8.302** An outline of the major events, starting from the announcement of the State Government's intention to issue a casino licence in 1991 through to the most recent amendment to the licence agreement, are detailed below:

#### 1991

- The Victorian Government announced its intention to allow the introduction of casinos into Victoria.
- The *Casino Control Act* 1991 allows for one large casino to be established.
- The Victorian Government Major Projects Unit issued a brief seeking registrations of interest in establishing Melbourne's first casino.

#### 1992

- The Victorian Casino Control Authority (VCCA) was established.
- In response to the State Government's decision to issue a casino licence, 23 expressions of interest were registered.
- A short-list of 3 registrants was selected and invited to apply for the casino licence.
- The Government announces that Southbank would be made available as a potential site for the permanent casino.

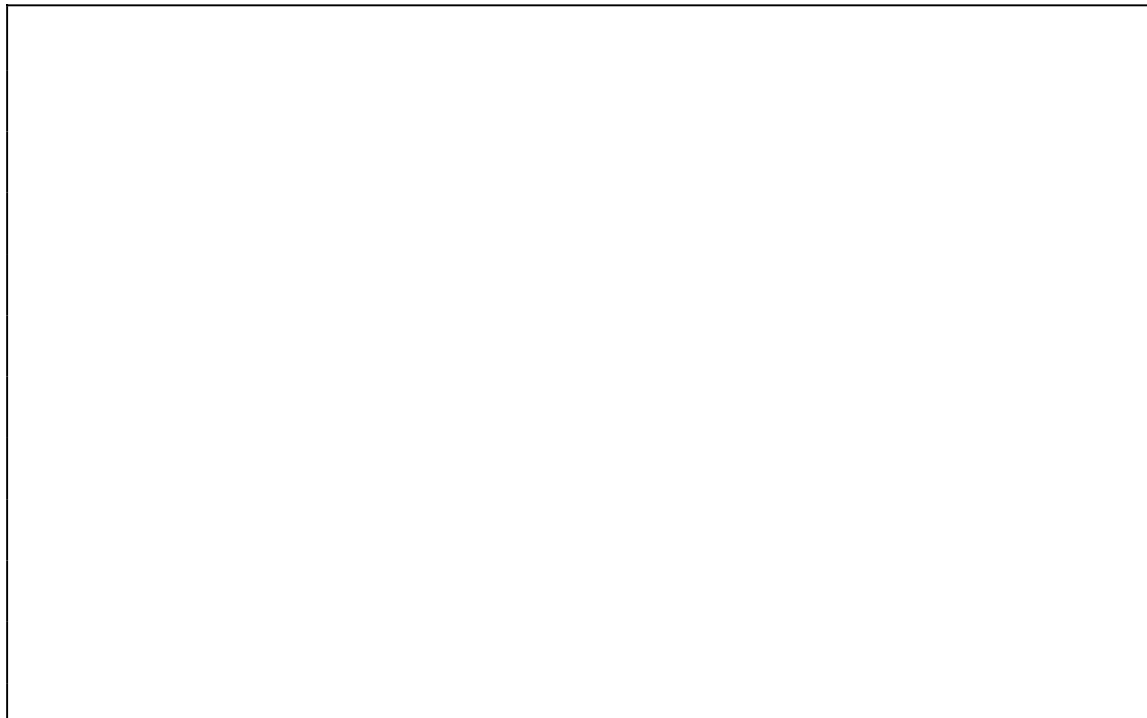


**1993**

- The Galleria area of the World Trade Centre announced as the interim location of the Melbourne casino;
- The VCCA decided unanimously to nominate Crown to Cabinet as the preferred applicant for the licence;
- The *Casino (Management Agreement) Act 1993* enacted on 16 November;
- The casino licence was granted to Crown on 19 November, on payment of a \$200 million fee;
- Crown also agreed to pay:
  - additional casino tax of \$57.6 million;
  - tax of 20 per cent on gross gaming revenue;
  - "super" tax on gross gaming revenue in excess of \$500 million;
  - community benefit levy of 1 per cent on gross gaming revenue; and
  - "supervision charge" of \$5 million a year for 4 years.

**1994**

- The *Gaming and Betting Act 1994* was proclaimed, establishing the Victoria Casino and Gaming Authority (VCGA) as successor to the VCCA;
- The temporary casino opened at the Galleria area of the World Trade Centre.



*Temporary casino operated by Crown Limited at the World Trade Centre, Melbourne.*

## Approval for an increase in Casino gaming tables and machines

**3.8.303** In July 1995, Crown sought approval, pursuant to the provisions of the *Casino Control Act 1991* to:

- increase the number of gaming tables from 200 to 350 and gaming machines from 2 500 to 3 500; and
- amend the tax arrangements in respect of commission-based players.

**3.8.304** Following the receipt of Crown's application and discussions with the Department of Treasury and Finance, the VCGA (which is responsible for approving licence amendments) engaged a consultant to:

- review the revenue projections submitted by Crown relating to the operation of the additional gaming tables and gaming machines and the reasonableness of the assumptions adopted;
- review the likely impact of increased gaming tables and machines on the profitability of the casino operator and the taxation to be raised from the casino; and
- provide a recommendation as to whether there should be a further licence fee and, if so, the range of licence fee payments for different combinations of the number of gaming tables and machines;

**3.8.305** As part of its report on these issues, the consultant concluded that if the request was approved it would provide Crown with increased monopoly rights and that an additional licence payment should be made for those rights.

**3.8.306** Following consideration of the proposal and the consultant's report, the VCGA agreed to increase the maximum number of gaming tables from 200 to 350, on the condition that agreement could be reached between the Government and Crown on appropriate consideration for the additional tables. However, the agreement was conditional upon a number of factors, including the VCGA's assessment that there was sufficient public demand to justify the provision of additional tables and that these tables would further promote tourism in Victoria.

**3.8.307** In relation to the request to increase the maximum number of gaming machines from 2 500 to 3 500, the Authority did not support this element of Crown's application.

### *Additional licence fees*

**3.8.308** In determining the appropriate licence fee for the additional gaming tables, the consultant was of the view that the fee should be determined by reference to the additional incremental profits which could be earned from the resulting increase in the capacity of the casino. **However, the consultant indicated that the additional licence payment was not intended to take into account, with the benefit of hindsight, whether the initial licence payment should have been higher given the better than forecast performance of the casino.**



**3.8.309** As Crown held an exclusive licence for 12 years, the consultant considered it was not in a position to determine a market value for the various combinations of additional gaming tables and machines and that the original licence payment represented the best benchmark. The consultant calculated the ratio that the original licence payment bore to the present value of the original projected earnings. This ratio was then applied to the present value of the projected earnings from the additional tables to determine the recommended range of licence fees.

**3.8.310** The consultant in its report recommended that for an additional 150 gaming tables the licence payment should range from \$51 million to \$69 million.

**3.8.311** If the consultant's recommendation was accepted, it would have resulted in the State receiving 31 per cent of the after-tax earnings generated from the additional tables and Crown receiving 69 per cent.

**3.8.312** Based on these figures, the additional tables were worth between \$166 million and \$223 million to Crown in 1995 dollars or in excess of \$800 million over the term of the agreement. These values were determined after providing for all additional operating and administration costs including a management fee payable to Crown Management Pty Ltd, gaming taxes, a specified rate of return and company tax, but not allowing for additional depreciation, amortisation and interest. Allowance was not made for these expenses, as the physical structure of the casino was unlikely to change significantly as a result of the additional tables.

**3.8.313** **The lower end of the range, outlined above, effectively represented the projected earnings submitted by Crown, while the upper end was determined after adjustment by the consultant of these estimates to take account of, inter alia, lower projected labour costs for operating the additional tables.**

**3.8.314** Under the *Casino Control Act* 1991, the Treasurer is responsible for the determination of the casino licence fees and taxation payments. In order to determine an appropriate licence fee for the additional tables approved by the Authority, the Treasurer sought advice from the Department of Treasury and Finance (the Department).

**3.8.315** The Department, when considering the appropriate additional licence fee, accepted the methodology adopted by the consultant, but prior to determining the appropriate additional licence fee considered the following 4 alternative values:

- adjusting the consultant's recommended fee to take account of capital costs - (valuation ranged from \$86 million to \$96 million);
- estimating the amount Crown was willing to pay for a stream of projected earnings generated from the additional tables - (valuation ranged from \$95 million to \$130 million);

- multiplying the price paid for a table equivalent in the original licence agreement by the number of additional tables (a table equivalent is a gaming table or groups of gaming machines which generate revenue equivalent to a gaming table) - (valuation of \$56 million); and
- using the payment made by TABCORP, for its gaming licence, to estimate a value for the casino's gaming machines, then using this amount to determine the value of an individual gaming table equivalent, which was then multiplied by the number of additional tables - (valuation ranged from \$63 million to \$72 million).

**3.8.316** After examining the various values, the Department recommended to the Treasurer that the additional licence fee should be based on the lower end of the range resulting from estimating the amount Crown was willing to pay for a stream of projected earnings generated from the additional tables (\$194 million). The Department took approximately half of this amount, which was then discounted by \$10 million to arrive at a licence fee of \$85 million. This value assumed a 57 per cent and 43 per cent share of projected **after-tax earnings** from the additional tables by Crown and the State, respectively.

**3.8.317** In addition to the additional licence fee, the consultant estimated that the expansion in table capacity would generate an extra \$30 million a year in ongoing tax revenue for the Government.

**3.8.318** In respect of the changes to the taxation arrangements for commission-based players, the Department agreed to the amendments requested by Crown. As the Department was of the opinion that these changes were unlikely to generate significant monopoly profits, no additional consideration was required from Crown in relation to these changes.

**3.8.319** Based on the Department's recommendation, a once-off non-negotiable offer was made to Crown for the right to operate the additional gaming tables in exchange for an additional licence fee of \$85 million.

#### *Amendment to agreements with Crown*

**3.8.320** Subsequently, an agreement was reached between the Government and Crown in respect of the additional licence fee and tax changes. As a result, the Government's management agreement with Crown was amended on 12 October 1995 to incorporate:

- additional payments of \$100.8 million from Crown for extra gaming tables by way on monthly payments of \$2.8 million for 3 years, commencing 1 January 1996, (\$85 million in present value terms);
- the introduction of a *sliding* scale tax rate ranging from 10 per cent to 22.25 per cent in respect of commission-based players to provide a term rate competitive with overseas and interstate casinos, so that Crown may attract these high net worth patrons to Melbourne;





- Crown contributing \$1 million a year for 5 years from November 1995 to Tourism Victoria to enable it to expand its marketing program for the State and, in particular, Melbourne; and
- an extension of the completion date for the construction of the Casino to 30 November 1996 and a payment to the State of \$5.3 million in relation to liquidated damages by Crown for delays in construction.

*Is the arrangement the most favourable for the State?*

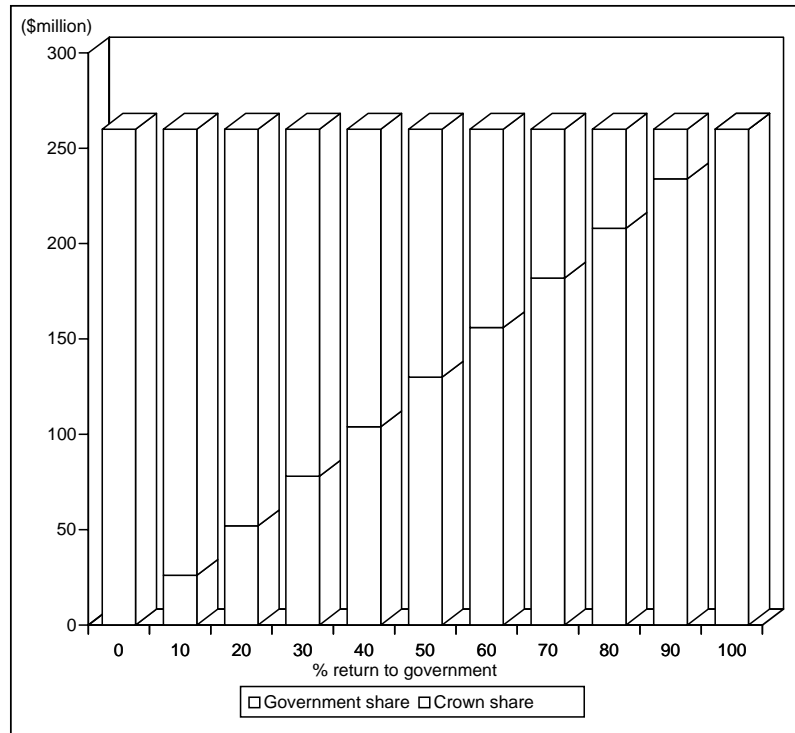
**3.8.321** The Department estimated that the stream of projected earnings to be generated from the additional 150 tables was between \$194 million and \$259 million (in present value terms), after taking account of a rate of return to the owners, consistent with that generated by Crown under the original licence fee. The Department took the view that it was more appropriate to equally share these profits between Crown and the State. Therefore, the Department decided to take half of the lower end of the range in order to establish an appropriate licence fee, prior to discounting by \$10 million.

**3.8.322** In respect of the Department's calculation of the additional licence fee, the following comments are made:

- **The consultant recommended taking the higher end of the licence fee ranges provided, as these amounts were based on more accurate estimates of the revenues and expenses likely to be generated from the additional tables. Based on the Department's calculation this would have been \$259 million;**
- **As the estimated profits were calculated after providing for a return to the owner, they represent monopoly profits. However, there was inadequate support, provided to audit, for the Department's decision for Crown to retain any of the monopoly profits generated from the licence; and**
- **The Department discounted its estimated licence fee value by \$10 million, as a result of the uncertainties associated with the licence fee calculations and its recognition that the Government wanted to make a one-off non-negotiable offer to Crown. However, inadequate support was provided to audit for the discount and why a strategy was adopted involving a one-off non-negotiable offer.**

**3.8.323** Chart 3.8ZA highlights the options available for the sharing of monopoly profits.

**CHART 3.8ZA  
OPTIONS AVAILABLE FOR SHARING MONOPOLY PROFIT**



**3.8.324** The above chart highlights the returns that were available to the Government compared with the return achieved through the additional licence fee of \$85 million.

**□ RESPONSE** provided by Secretary, Department of Treasury and Finance

*The Department of Treasury and Finance (DTF) does not believe that there is a uniquely correct method for determining the value of the additional tables in the casino.*

*The approach used by Coopers and Lybrand is based on the ratio of the original licence fee payment to the present value of the original projected earnings. This is a defensible basis for the calculation of the additional licence fee, as this ratio was determined during a market bidding process. The consultants argue that this provided the best objective benchmark available for replicating a competitive bid situation.*

*While not necessarily rejecting the consultant's methodology, DTF decided to test it by using 4 alternative approaches. As your Report points out, 2 of these methodologies suggested valuations consistent with the consultants' suggested range of \$51 million to \$69 million. Two alternative methodologies, however, suggested higher values.*



□ *RESPONSE provided by Secretary, Department of Treasury and Finance - continued*

*The main reason for the difference relates to the treatment of capital costs. The lower valuation methodologies implicitly assume that, in the expansion, Crown would bear capital costs roughly proportional to the capital costs related to the original casino. The higher valuation methodologies, on the other hand, allow for little, if any, additional capital costs associated with the extra tables. The Auditor-General's Report assumes that the higher valuation methodology is the appropriate methodology to use. It also assumes that all of the revenue flows using this measure (discounted) are "monopoly profits", and could have been appropriated by the Government. This conclusion:*

- Assumes that the rate of return used in this calculation represents a "normal" rate of return in the casino industry and that all returns above this rate are "monopoly profits". This assumption is based on the consultants' estimate of the weighted average cost of capital for Crown in 1993. The calculation of monopoly profits is quite sensitive to the chosen rate of discount: for example, a one per cent change in the rate of return would reduce the valuation of future earnings by \$14 million;*
- Assumes that if the Government had appropriated the whole of the "monopoly profit" calculated using this methodology that Crown would nevertheless have decided to proceed with the expansion. DTF believes that such an outcome would have been most unlikely;*
- Mistakenly assumes that it is correct to make no allowance for the opportunity cost of the space allocated to the extra tables, which would have been alternative uses if the Government had refused Crown's request. Hence, when it was assessing the amount it was willing to pay for the extra tables, Crown would have subtracted this opportunity cost from the present value of the EBDAIT that would be generated by the additional tables; and*
- ignores the fact that Crown's proposal to expand the number of tables was part of a broader proposal, involving, among other things, expansions to the size and changes to the nature of the hotel. It is arguable that some of this expenditure could be seen as part of the tables expansion project.*

*DTF also took into account the fact that the expansion in the number of tables would, on Crown's projections, have generated \$30 million per annum of ongoing taxation revenue (although the actual amount might have been less than this after allowing for the substitution of gambling within the casino for other forms of gambling). Seeking an excessive licence fee payment could have placed this ongoing, large, revenue stream at risk.*

*Given these considerations, and the existence of an independent valuation which was lower than the valuation which Treasury recommended, DTF believes that its valuation has generated an appropriate return for the State.*

.....

**SCHEDULE A**  
**STATUS OF MATTERS RAISED IN PREVIOUS REPORTS**

| <i>Report</i>                                        | <i>Subject</i>                                                                                                                                                                                                                                                                                                                                                                                     | <i>Status at date of preparation of this Report</i>                                                                                                                                                                                                                                                                                             |
|------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>MATTERS RESOLVED OR ACTION COMMENCED</b>          |                                                                                                                                                                                                                                                                                                                                                                                                    |                                                                                                                                                                                                                                                                                                                                                 |
| <b>GAS AND FUEL CORPORATION OF VICTORIA</b>          |                                                                                                                                                                                                                                                                                                                                                                                                    |                                                                                                                                                                                                                                                                                                                                                 |
| <i>Ministerial Portfolios, May 1995, pp. 24-7.</i>   | At 30 June 1994, the Corporation had a substantial financial exposure, estimated at \$74.6 million, for the remediation of certain properties which had become contaminated in the process of production and/or storage of gas.                                                                                                                                                                    | With the abolition of the Corporation on 20 June 1995, the responsibility for the remediation was transferred partly to GASCOR, the successor entity in law to the Gas and Fuel Corporation of Victoria, and partly to the State Electricity Commission of Victoria. For further comments, refer to paragraphs 3.8.26 to 3.8.27 of this Report. |
| <i>Ministerial Portfolios, May 1994, pp. 189-91.</i> | After protracted negotiations extending over 4 years to determine the most suitable building for its head office requirements, the Corporation repudiated the agreement to lease entered into with Gleem Pty Ltd.                                                                                                                                                                                  | Legal proceedings are continuing. For further comments, refer to paragraphs 3.8.18 to 3.8.20 of this Report                                                                                                                                                                                                                                     |
| <i>Ministerial Portfolios, May 1995, pp. 27-9.</i>   | This resulted in the issue of Supreme Court proceedings against the Corporation claiming damages totalling \$107 million.                                                                                                                                                                                                                                                                          |                                                                                                                                                                                                                                                                                                                                                 |
| <b>STATE ELECTRICITY COMMISSION OF VICTORIA</b>      |                                                                                                                                                                                                                                                                                                                                                                                                    |                                                                                                                                                                                                                                                                                                                                                 |
| <i>Ministerial Portfolios, May 1994, pp. 229-31.</i> | In May 1991, the State Electricity Commission of Victoria (SECV) entered into a 20 year lease for a new 40 000 square metre head office building to be constructed by a developer. Due to the restructuring of the electricity industry and the decline of SECV staff numbers located within the Melbourne central business district, uncertainty surrounded the future occupancy of the building. | The building is now fully leased. The SECV intends to dispose of the building at an appropriate time.                                                                                                                                                                                                                                           |
| <i>Ministerial Portfolios, May 1995, pp. 29-31.</i>  |                                                                                                                                                                                                                                                                                                                                                                                                    |                                                                                                                                                                                                                                                                                                                                                 |
| <b>GASCOR</b>                                        |                                                                                                                                                                                                                                                                                                                                                                                                    |                                                                                                                                                                                                                                                                                                                                                 |
| <i>Ministerial Portfolios, May 1995, pp. 31-4.</i>   | Over the life of the current gas supply pricing arrangements, GASCOR and Generation Victoria have an estimated gross exposure for petroleum rent resource tax of \$1 billion (net present value \$897 million) if a court ruling was made entirely in favour of the gas suppliers, ESSO and BHP.                                                                                                   | Legal proceeding to resolve the issue are continuing. For further comments, refer to paragraphs 3.8.21 to 3.8.25 of this Report.                                                                                                                                                                                                                |

**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                  | <i>Financial<br/>year ended</i>    | <i>Reporting to Parliament</i>                                                           | <i>Financial<br/>statements<br/>signed by<br/>entity</i> | <i>Auditor-<br/>General's<br/>report<br/>signed</i> |
|------------------------------------------------|------------------------------------|------------------------------------------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------------|
| <b>COMPLETED AUDITS</b>                        |                                    |                                                                                          |                                                          |                                                     |
| Department of Treasury and Finance             | 30 June 1995                       | 31 Oct. <i>Financial Management Act 1994</i> , s.45.                                     | 4 Oct. 1995                                              | 5 Oct. 1995                                         |
| <b>FINANCE</b>                                 |                                    |                                                                                          |                                                          |                                                     |
| Coal Mine Workers' Pensions Fund               | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46. Extension granted to 31 Oct. 1995. | 20 Oct. 1995                                             | 30 Oct. 1995                                        |
| Emergency Services Superannuation Scheme       | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46.                                    | 27 Sept. 1995                                            | 27 Sept. 1995                                       |
| Government Employee Housing Authority          | Period 1 July 1994 to 29 Feb. 1996 | " "                                                                                      | 29 Feb. 1996                                             | 1 March 1996 (a)                                    |
| Holmesglen Constructions Superannuation Plan   | 30 June 1995                       | " "                                                                                      | 19 Sept. 1995                                            | 19 Sept. 1995                                       |
| Hospitals Superannuation Board                 | 30 June 1995                       | " "                                                                                      | 27 Sept. 1995                                            | 29 Sept. 1995                                       |
| Local Authorities Superannuation Board         | 30 June 1995                       | " "                                                                                      | 29 Sept. 1995                                            | 29 Sept. 1995                                       |
| Parliamentary Contributory Superannuation Fund | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46. Extension granted to 31 Oct. 1995. | 25 Oct. 1995                                             | 30 Oct. 1995                                        |
| Port of Geelong Authority Superannuation Fund  | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46.                                    | 30 Aug. 1995                                             | 22 Sept. 1995                                       |
| Regulator-General, Office of the               | 30 June 1995                       | 31 Oct. <i>Financial Management Act 1994</i> , s.45.                                     | 22 Sept. 1995                                            | 26 Sept. 1995                                       |
| State Casual Employees Superannuation Fund     | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46.                                    | 19 Sept. 1995                                            | 19 Sept. 1995                                       |
| State Employees Retirement Benefits Fund       | 30 June 1995                       | " "                                                                                      | 19 Sept. 1995                                            | 19 Sept. 1995                                       |
| State Superannuation Fund                      | 30 June 1995                       | " "                                                                                      | 19 Sept. 1995                                            | 19 Sept. 1995                                       |
| Transport Superannuation Fund                  | 30 June 1995                       | " "                                                                                      | 19 Sept. 1995                                            | 19 Sept. 1995                                       |

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**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                          | <i>Financial<br/>year ended</i>    | <i>Reporting to Parliament</i>                          | <i>Financial<br/>statements<br/>signed by<br/>entity</i> | <i>Auditor-<br/>General's<br/>report<br/>signed</i> |
|----------------------------------------|------------------------------------|---------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------------|
| <b>COMPLETED AUDITS - continued</b>    |                                    |                                                         |                                                          |                                                     |
| <b>FINANCE - continued</b>             |                                    |                                                         |                                                          |                                                     |
| Victorian Superannuation Board         | 30 June 1995                       | 31 Oct. <i>Financial Management Act 1994</i> , s.46.    | 19 Sept. 1995                                            | 19 Sept. 1995                                       |
| Victorian Superannuation Fund          | 30 June 1995                       | " "                                                     | 19 Sept. 1995                                            | 19 Sept. 1995                                       |
| Victorian WorkCover Authority          | 30 June 1995                       | " "                                                     | 15 Sept. 1995                                            | 29 Sept. 1995                                       |
| <b>GAMING</b>                          |                                    |                                                         |                                                          |                                                     |
| Tattersall Gaming Machine Division     | 30 June 1995                       | 31 Oct. <i>Gaming Machine Control Act 1991</i> , s.132. | 20 Oct. 1995                                             | 24 Oct. 1995                                        |
| Tattersall Sweep Consultation          | 30 June 1995                       | <i>Tattersall Sweep Consultation Act 1958</i> .         | 20 Oct. 1995                                             | 24 Oct. 1995                                        |
| Tattersall's Club Keno                 | 30 June 1995                       | 31 Oct. <i>Club Keno Act 1993</i> , s.10.               | 20 Oct. 1995                                             | 24 Oct. 1995                                        |
| Victorian Casino and Gaming Authority  | 3 June 1994 to 30 June 1995        | 31 Oct. <i>Financial Management Act 1994</i> , s.46.    | 11 Oct. 1995                                             | 11 Oct. 1995                                        |
| <b>TREASURER</b>                       |                                    |                                                         |                                                          |                                                     |
| Aluminium Smelters of Victoria Pty Ltd | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46.   | 14 Sept. 1995                                            | 20 Oct. 1995                                        |
| Citipower Limited                      | Period 11 May 1994 to 30 June 1995 | 31 Oct. <i>Financial Management Act 1994</i> , s.53A.   | 3 Oct. 1995                                              | 5 Oct. 1995                                         |
| Coal Corporation of Victoria           | Period 1 July 1994 to 20 June 1995 | 30 Sept. <i>Financial Management Act 1994</i> , s.46.   | 20 Sept. 1995                                            | 22 Sept. 1995 (b)                                   |
| Eastern Energy Ltd                     | Period 11 May 1994 to 30 June 1995 | 31 Oct. <i>Financial Management Act 1994</i> , s.53A.   | 21 Sept. 1995                                            | 26 Sept. 1995 (c)                                   |
| Ecogen Energy Ltd                      | 30 June 1995                       | " "                                                     | 27 Sept. 1995                                            | 28 Sept. 1995                                       |
| Electricity Services Victoria          | 30 June 1995                       | 30 Sept. <i>Financial Management Act 1994</i> , s.46.   | 27 Sept. 1995                                            | 27 Sept. 1995                                       |

**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                | <i>Financial year ended</i>         | <i>Reporting to Parliament</i>                                                                   | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|----------------------------------------------|-------------------------------------|--------------------------------------------------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS</b>                      |                                     |                                                                                                  |                                              |                                        |
| <b>TREASURER - continued</b>                 |                                     |                                                                                                  |                                              |                                        |
| Energy Brix Australia Corporation            | 30 June 1995                        | 30 Sept. <i>Financial Management Act 1994</i> , s.46.                                            | 21 Sept. 1995                                | 29 Sept. 1995                          |
| Energy Business Centre Pty Ltd               | Period 10 June 1994 to 30 June 1995 | 31 Oct. <i>Financial Management Act 1994</i> , s.53A.                                            | 5 Oct. 1995                                  | 13 Oct. 1995                           |
| Everton Dell Pty Ltd                         | 30 June 1995                        | " "                                                                                              | 28 Sept. 1995                                | 28 Sept. 1995                          |
| Gas and Fuel Corporation of Victoria         | Period 1 July 1994 to 21 June 1995  | 30 Sept. <i>Financial Management Act 1994</i> , s.46.                                            | 30 June 1995                                 | 30 June 1995 (d)                       |
| Gas and Fuel Corporation Superannuation Fund | 30 June 1995                        | " "                                                                                              | 24 Oct. 1995                                 | 30 Oct. 1995                           |
| GASCOR                                       | 30 June 1995                        | " "                                                                                              | 24 Aug. 1995                                 | 7 Sept. 1995                           |
| Gas Transmission Corporation                 | 30 June 1995                        | " "                                                                                              | 25 Aug. 1995                                 | 25 Aug. 1995                           |
| Generation Victoria                          | 30 June 1995                        | 30 Sept. <i>Financial Management Act 1994</i> , s.46. Extension of time granted to 10 Nov. 1995. | 9 Nov. 1995                                  | 9 Nov. 1995                            |
| GFE Resources Ltd                            | 30 June 1995                        | 31 Oct. <i>Financial Management Act 1994</i> , s.53A.                                            | 11 Oct. 1995                                 | 16 Oct. 1995 (e)                       |
| Hazelwood Power Corporation Ltd              | 30 June 1995                        | " "                                                                                              | 8 Sept. 1995                                 | 29 Sept. 1995                          |
| Loy Yang B Power Station Pty Ltd             | 30 June 1995                        | " "                                                                                              | 25 Aug. 1995                                 | 29 Aug. 1995                           |
| Loy Yang Power Ltd                           | 30 June 1995                        | " "                                                                                              | 6 Sept. 1995                                 | 6 Sept. 1995                           |
| National Electricity Pty Ltd                 | 30 June 1995                        | " "                                                                                              | 18 Sept. 1995                                | 21 Sept. 1995                          |

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**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                            | <i>Financial year ended</i>                    | <i>Reporting to Parliament</i>                             | <i>Financial statements signed by entity</i> | <i>Auditor-General's report signed</i> |
|------------------------------------------|------------------------------------------------|------------------------------------------------------------|----------------------------------------------|----------------------------------------|
| <b>COMPLETED AUDITS - continued</b>      |                                                |                                                            |                                              |                                        |
| <b>TREASURER - continued</b>             |                                                |                                                            |                                              |                                        |
| Powercor Australia Ltd                   | Period<br>11 May<br>1994 to<br>30 June<br>1995 | 31 Oct. <i>Financial Management Act 1994</i> ,<br>s.53A.   | 3 Oct.<br>1995                               | 3 Oct.<br>1995                         |
| PowerNet Victoria                        | 30 June<br>1995                                | 30 Sept. <i>Financial Management Act 1994</i> ,<br>s.46.   | 24 Aug.<br>1995                              | 8 Sept.<br>1995                        |
| Powerworks Pty Ltd                       | 30 June<br>1995                                | 31 Oct. <i>Financial Management Act 1994</i> ,<br>s.53A.   | 21 Nov.<br>1995                              | 23 Nov.<br>1995                        |
| Renewable Energy Authority of Victoria   | 30 June<br>1995                                | 30 Sept. <i>Financial Management Act 1994</i> ,<br>s.46.   | 8 Sept.<br>1995                              | 11 Sept.<br>1995                       |
| Rural Finance Corporation                | 30 June<br>1995                                | " "                                                        | 13 Sept.<br>1995                             | 13 Sept.<br>1995                       |
| Securities Finance Corporation Ltd       | 31 Dec.<br>1995                                | 30 April. <i>Financial Management Act 1994</i> ,<br>s.53A. | 6 Mar.<br>1996                               | 6 Mar.<br>1996                         |
| SECV International Pty Ltd               | 30 June<br>1995                                | 31 Oct. <i>Financial Management Act 1994</i> ,<br>s.53A.   | 2 Aug.<br>1995                               | 9 Aug.<br>1995 (e)                     |
| Solaris Power Ltd                        | Period<br>11 May<br>1994 to<br>30 June<br>1995 | " "                                                        | 14 Sept.<br>1995                             | 14 Sept.<br>1995                       |
| Southern Hydro Ltd                       | 30 June<br>1995                                | " "                                                        | 14 Sept.<br>1995                             | 14 Sept.<br>1995                       |
| State Electricity Commission of Victoria | 30 June<br>1995                                | 30 Sept. <i>Financial Management Act 1994</i> ,<br>s.46.   | 29 Sept.<br>1995                             | 29 Sept.<br>1995                       |
| State Insurance Office                   | 30 June<br>1995                                | " "                                                        | 15 Sept.<br>1995                             | 29 Sept.<br>1995                       |
| State Trust Corporation of Victoria      | 30 June<br>1995                                | " "                                                        | 14 Sept.<br>1995                             | 18 Sept.<br>1995                       |
| The Albury Gas Company Ltd               | 30 June<br>1995                                | 31 Oct. <i>Financial Management Act 1994</i> ,<br>s.53A.   | 10 Aug.<br>1995                              | 16 Aug.<br>1995                        |
| Transport Accident Commission            | 30 June<br>1995                                | 30 Sept. <i>Financial Management Act 1994</i> ,<br>s.46.   | 12 Sept.<br>1995                             | 12 Sept.<br>1995                       |



**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                      | <i>Financial<br/>year<br/>ended</i> | <i>Reporting to Parliament</i>                        | <i>Financial<br/>statements<br/>signed by<br/>entity</i> | <i>Auditor-<br/>General's<br/>report<br/>signed</i> |
|----------------------------------------------------|-------------------------------------|-------------------------------------------------------|----------------------------------------------------------|-----------------------------------------------------|
| <b>COMPLETED AUDITS - continued</b>                |                                     |                                                       |                                                          |                                                     |
| <b>TREASURER - continued</b>                       |                                     |                                                       |                                                          |                                                     |
| Treasury Corporation of Victoria                   | 30 June 1995                        | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 8 Sept. 1995                                             | 8 Sept. 1995                                        |
| Tricontinental Australia Ltd                       | 31 Dec. 1995                        | 31 Mar. <i>Financial Management Act 1994</i> , s.53A. | 6 Mar. 1996                                              | 6 Mar. 1996                                         |
| Tricontinental Corporations Ltd                    | 31 Dec. 1995                        | " "                                                   | 6 Mar. 1996                                              | 6 Mar. 1996                                         |
| Tricontinental Holdings Ltd                        | 31 Dec. 1995                        | " "                                                   | 6 Mar. 1996                                              | 6 Mar. 1996                                         |
| Twin Waters Resorts Pty Ltd                        | 31 Dec. 1995                        | " "                                                   | 6 Mar. 1996                                              | 6 Mar. 1996                                         |
| United Energy Ltd                                  | Period 11 May 1994 to 30 June 1995  | 31 Oct. <i>Financial Management Act 1994</i> , s.53A. | 7 Dec. 1995                                              | 9 Feb. 1996 (c)(e)                                  |
| Utilities Insurance Company Pty Ltd                | 30 June 1995                        | " "                                                   | 19 Sept. 1995                                            | 28 Sept. 1995                                       |
| V.E.I. Super Pty Ltd                               | 30 June 1995                        | " "                                                   | 19 Oct. 1995                                             | 19 Oct. 1995                                        |
| Vicfleet Pty Ltd                                   | 30 June 1995                        | " "                                                   | 25 Oct. 1995                                             | 30 Oct. 1995                                        |
| Victorian Debt Retirement Fund                     | 30 June 1995                        | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 27 Sept. 1995                                            | 27 Sept. 1995                                       |
| Victorian Electricity Industry Superannuation Fund | 30 June 1995                        | " "                                                   | 19 Oct. 1995                                             | 19 Oct. 1995                                        |
| Victorian Funds Management Corporation             | 30 June 1995                        | " "                                                   | 10 Aug. 1995                                             | 12 Sept. 1995                                       |
| Victorian Power Exchange                           | 30 June 1995                        | 30 Sept. <i>Financial Management Act 1994</i> , s.46. | 24 Aug. 1995                                             | 31 Aug. 1995                                        |
| Vistel Ltd                                         | 30 June 1995                        | 31 Oct. <i>Financial Management Act 1994</i> , s.53A. | 26 Oct. 1995                                             | 26 Oct. 1995                                        |
| Yallourn Energy Ltd                                | 30 June 1995                        | " "                                                   | 25 Aug. 1995                                             | 7 Sept. 1995                                        |

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**SCHEDULE B**  
**COMPLETED/INCOMPLETE AUDITS - continued**

| <i>Entity</i>                                             | <i>Financial<br/>year<br/>ended</i>   | <i>Reporting to Parliament</i>                             | <i>Financial<br/>statements<br/>signed by<br/>entity</i>                                                                         | <i>Auditor-<br/>General's<br/>report<br/>signed</i> |
|-----------------------------------------------------------|---------------------------------------|------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------|
| <b>INCOMPLETED AUDITS</b>                                 |                                       |                                                            |                                                                                                                                  |                                                     |
| <b>GAMING</b>                                             |                                       |                                                            |                                                                                                                                  |                                                     |
| Tabcorp Manager Pty Ltd<br>Gaming Business<br>Segment (f) | 15 Aug.<br>1994 to<br>30 June<br>1995 | 31 Oct. <i>Gaming Machine<br/>Control Act</i> 1991, s.132. | Doubt exists as to<br>whether financial<br>statements meet<br>requirements of the<br><i>Gaming Machine Control<br/>Act</i> 1991. |                                                     |
| Tabcorp Holdings Limited<br>Club Keno Business<br>Segment | 15 Aug.<br>1994 to<br>30 June<br>1995 | 31 Oct. <i>Club Keno Act</i><br>1993, s.10.                | Awaiting signed set of<br>statements.                                                                                            |                                                     |
| Totalizator Agency Board                                  | 1 Aug. 1994<br>to 2 June<br>1995      | 31 Oct. <i>Financial<br/>Management Act</i> 1994,<br>s.46. | Statements not provided<br>until March 1996.                                                                                     |                                                     |

(a) Abolished on 29 February 1996.

(b) Abolished on 20 June 1995.

(c) Qualified audit report issued.

(d) Abolished on 21 June 1995.

(e) Sold to a private sector entity as at 30 June 1995.

(f) TABCORP Manager Pty Ltd is the operator of the Gaming Licence issued to TABCORP Holdings Ltd.

# Part 4



## Broad Scope Issues



# Part 4.1

## Women in Public Office

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### KEY FINDINGS

- While it is essential that selection processes be equitable and based on merit, there is scope for a higher representation of women on Boards of Management and in Chief Executive Officer (CEO) positions within public sector agencies.  
*Para 4.1.1*
- The recent trend for increased representation of women at the parliamentary level has not been mirrored in the bureaucracy.  
*Paras 4.1.1, 4.1.18 to 4.1.21*
- The composition of public sector Boards of Management tended to be dominated by men across all industry groups in 1995, with women comprising 25 per cent of members (1991, around 24 per cent).  
*Para 4.1.9*
- Of the agencies examined, 32 agencies (or 12 per cent) did not have a woman on their Board of Management.  
*Para 4.1.11*
- The proportion of CEO positions held by women increased from 5.2 per cent in 1991 to 9.6 per cent in 1995.  
*Para 4.1.13*
- Of 271 CEO positions examined in 1995, only 26 were occupied by women.  
*Para 4.1.13*
- In general, CEO appointments tended to be located in smaller agencies which are in perceived traditional areas for women.  
*Para 4.1.14*



**WOMEN IN PUBLIC OFFICE**

**OVERALL AUDIT CONCLUSION**

**4.1.1** Overall, the audit concluded that there is scope for a higher representation of women on Boards of Management and in Chief Executive Officer positions within public sector agencies. The audit disclosed that the representation of women on Boards of Management (25 per cent) and serving as Chief Executive Officers (10 per cent) is well below their representation in the population (50 per cent). The recent trend for increased representation of women at the parliamentary level has not been mirrored in the bureaucracy.

**Introduction**

**4.1.2** In May 1995, the Auditor-General's *Special Report No. 35 Equality in the Workplace: Women in Management* was tabled in the Parliament and examined the representation of women in the day-to-day operational management of agencies in the Victorian public sector.

**4.1.3** Given that women represented 50 per cent of the population in Australia and 42 per cent of the total Australian labour force, but occupied only 25 per cent of managerial positions in the Victorian public sector (i.e. job categories attracting an annual salary in excess of \$44 200), there was clearly scope for further improvement in the representation of women in the managerial ranks of government agencies. As many of the services provided by the Government are in fact received by women, the significant involvement of women in decision-making may lead to improved resource allocation and service delivery. Around two-thirds of current employees in the public sector held the view that women bring different managerial qualities to the operation of an organisation. In this regard, despite women increasingly obtaining similar technical skills and abilities as men, the most common perception in relation to other qualities attributed to women related to greater people skills and more caring of individuals. Other opinions expressed included:

- a willingness to listen, discuss matters, negotiate and adopt a flexible approach;
- more efficient and organised;
- broader thinking and practical; and
- more approachable and understanding.

**4.1.4** To build on this theme, audit has now examined the representation of women in the higher leadership and decision making roles attached to public office by analysing the representation of women on Boards of Management and in positions as Chief Executive Officers of agencies in the Victorian public sector. Audit comment on the increased participation of women in the Parliament is included for comparative purposes.

□ **RESPONSE** provided by Public Service Commissioner.

*The introduction compares women's under-representation in management positions with their representation in the population and labour force. I believe it is more meaningful to compare the representation of women in feeder groups with Executive Officer (EO) levels, as your Report focuses on senior management positions. In the Victorian Public Service, women represent 28 per cent of the feeder group to, and 20 per cent of, EO positions.*

**Government initiatives and commitments**

**4.1.5** Some of the initiatives introduced by the Government, which will have an impact in addressing women's issues in this regard, are outlined below:

- Disclosure in the Victoria's Women's Budget by the Office of Women's Affairs of the representation of men and women on public sector Boards and Committees and in the Executive Service, together with associated policies and strategies for women;
- The commencement of the *Executive Officer Leadership Program* for Band 2 Executives (22 per cent of participants are women who comprise 11 per cent of the Band 2 executive level) and the *Leadership 21 Development Program* for Band 3 Executives (women comprise 36 per cent of participants compared with 23 per cent of the Band 3 executive level) in December 1995 and early 1996, respectively. These programs aim to strengthen leadership and management skills and also prepare those officers aspiring to be future Chief Executive Officers for their ultimate role as heads of their respective agencies;
- The conduct of a women-only Public Sector Management Course in 1995-96 with the specific aim to provide women, who have yet to gain middle management experience, with competencies that would enable them to be successful as managers;
- The release by the Public Service Commissioner in late 1995 of *Draft Flexible Work Options* and *Interim Guidelines for Telecommuting* for use by agencies in the development of their own policies in order to assist employees to meet work, family, health, study and other responsibilities;
- The release by the Public Service Commissioner to agencies in 1996 of a guide entitled *A Managing Diversity Approach to Merit and Equity*, which has a primary focus on achieving excellence in managing a diverse workforce with an aim of facilitating better productivity and service delivery; and
- The finalisation in 1996 of a *Ministerial Review of Employment Equity for Women in Education* which includes a series of recommendations in relation to providing an environment that supports women, and ensures that employment opportunities and training are available to enable women to reach their career potential.

**4.1.6** In order to enhance the effectiveness of the above measures, it is important that all decision-makers within government agencies show a strong commitment to, and be accountable for, the above initiatives.



**4.1.7** In March 1996, the Government released a series of election policies relating to women. These policies, which address a wide range of topics, include coverage of issues relating to the participation of women in public decision-making. With a view to increasing the involvement of women at all levels of decision-making to ensure government policy addresses the needs and views of women, the Government has indicated a commitment to:

- reviewing the reporting structure in all departments and government-funded bodies to ensure accountability for the appointment of women;
- ensuring that there is an increased representation of women on boards and committees and in decision-making positions within government departments by encouraging the expansion and use of the Victorian Women's Register (a database of approximately 500 women who are senior in their field and are interested in serving on government boards and committees);
- providing women with opportunities to develop skills to become involved in public decision-making;
- considering options for extending work-based child care facilities to enable care to be more readily accessible in locations where parents are working;
- introducing a legislative framework for children's services to enable the provision of high quality and affordable child care facilities; and
- encouraging women into politics by education and promotion.

**Women on Boards of Management**

**4.1.8** Boards of Management of public sector agencies play a vital role in the formulation of high level policy and strategic decision-making connected with the delivery of government programs to the community, many of which are delivered to women. With this in mind, considerable benefits could be achieved by a greater involvement of women on Boards of Management.

**4.1.9** The audit disclosed that, in 1995, 25 per cent of members of public sector boards examined by audit were women (1991, around 24 per cent). While the composition of Boards tended to be dominated by men across all industry groups, the education and health sectors had the highest representation of women involved in the affairs of the agencies at the Board level.

**4.1.10** Of the 260 agencies examined by audit, the following agencies identified in Table 4.1A had the highest representation of women on their Boards of Management in 1995.

**TABLE 4.1A  
AGENCIES WITH THE  
HIGHEST COMPOSITION OF WOMEN ON THEIR BOARDS**

| <i>Agency</i>                                | <i>Representation<br/>of women</i> | <i>Number<br/>of women</i> |
|----------------------------------------------|------------------------------------|----------------------------|
|                                              | (%)                                |                            |
| Queen Victoria Women's Centre Trust          | 100                                | 12                         |
| Nurses Board of Victoria                     | 75                                 | 9                          |
| Board of Studies                             | 64                                 | 7                          |
| O'Connell Family Centre (Grey Sisters) Inc   | 62                                 | 5                          |
| Liquor Licensing Commission                  | 60                                 | 3                          |
| Victorian Relief Committee                   | 56                                 | 5                          |
| Timboon and District Hospital                | 55                                 | 6                          |
| Adult, Community and Further Education Board | 50                                 | 7                          |
| Estate Agents Council                        | 50                                 | 4                          |
| Hospitals' Superannuation Board              | 50                                 | 3                          |
| Maryborough and District Health Service      | 50                                 | 6                          |
| Otway Health and Community Services          | 50                                 | 5                          |
| Physiotherapists' Registration Board         | 50                                 | 3                          |
| State Film Centre of Victoria Council        | 50                                 | 4                          |
| Tweddle Child and Family Health Service      | 50                                 | 6                          |
| William Angliss College                      | 50                                 | 6                          |

**4.1.11** In contrast, 32 agencies, representing 12 per cent of the agencies examined, did not have a woman on their Boards.

**4.1.12** To build on the current developments and proposed directions of the Government, the involvement of women on Boards of Management and decision-making could be improved by gradually increasing the number of women appointed to Boards which currently have a poor representation of women.



**Women holding the position of Chief Executive Officer**

**4.1.13** The proportion of Chief Executive Officer (CEO) positions held by women in the public sector increased from 5.2 per cent in 1991 to 9.6 per cent in 1995. In 1995, out of 271 CEO positions examined by audit across large, medium and small government agencies, only 26 were occupied by women. These women held the position of CEO in the following agencies:

**Public Bodies**

Department of Premier and Cabinet  
Australian Grand Prix Corporation  
Film Victoria  
Mental Health Review Board  
Nurses Board of Victoria  
Psychosurgery Review Board  
Victorian Health Promotion Foundation

**Educational Institutions**

Broadmeadows College of TAFE  
Hawthorn Institute of Education Ltd  
Melbourne College of Textiles  
Wangaratta College of TAFE  
William Angliss College  
Wimmera Community College of TAFE

**Health Institutions**

Burwood and District Community Hospital  
Hampton Rehabilitation Hospital  
Kingston Centre  
Kyneton District Hospital  
Lorne Community Hospital  
Maffra District Hospital  
Mordialloc-Cheltenham Community Hospital  
Mt Alexander Hospital  
North West Hospital  
O'Connell Family Centre (Grey Sisters) Inc.  
Tweddle Child and Family Health Service  
Williamstown Hospital

**Water and Sewerage Authorities**

Avoca River Management Board

**4.1.14** The audit revealed that from 1991 to 1995, while the education and health sectors showed the largest increase in the appointment of women to CEO positions, in general, appointments tended to be located in smaller agencies which are in perceived traditional areas for women. Exceptions were:

- the position of Secretary, Department of Premier and Cabinet, the most senior position in the Victorian Public Service;
- the CEO for the Australian Grand Prix Corporation, a high profile project undertaken in Victoria; and
- CEOs appointed to a number of areas that could be considered to be in the non-traditional domain for women, e.g. some TAFE colleges with trade activities such as industrial and aerospace courses.

**4.1.15** CEOs have a prime role as leaders of organisations in the context of policy development, business planning, human resource management and promoting the efficiency and effectiveness of service delivery to the public. Large numbers of women are employed by government agencies at an operational level to deliver key services. Many government programs provide services that are used by women in the community.

**4.1.16** In audit opinion, various avenues that could be considered in order to provide a greater number of women leaders of government agencies are listed below:

- continuing the practice of encouraging suitable women to attend leadership courses and providing women with the opportunity to work on various high profile projects in order to gain the necessary skills and qualifications to undertake the responsibilities of a CEO;



- developing policies to ensure women have access to all relevant information in regard to career advancement in their agency to assist in overcoming the exclusionary effects of perceived male networks;
- fostering long-term career path planning for women in senior executive levels;
- targeting recruitment strategies at women who have the potential to be future leaders;
- identifying personal development needs and the timely use of training for performance enhancement in line with the requirements of business plans;
- enhancing family friendly policies to men and women in the workforce, such as access to child care facilities and elder care, which would assist a greater number of women to reach senior management and CEO positions within their agencies; and
- developing improved reporting procedures in line with the Government's policy commitment to enable the Government to monitor the progress of women in relation to their involvement in all levels of decision-making throughout the public sector.

□ **RESPONSE** provided by Public Service Commissioner.

*The Office of the Public Service Commissioner promotes a managing diversity approach which highlights the need for managers to focus on systematic, people management policies and practices that address the needs of a diverse workforce. Such a focus will help improve women's opportunities at all levels.*

□ **RESPONSE** provided by Secretary, Department of Justice

*The Department of Justice welcomes the Auditor-General's analysis of Women in Public Office which provides an appropriate and timely sequel to the Auditor-General's Special Report in 1995 on "Equality in the Workplace: Women in Management".*

*The avenues the Auditor-General recommends to achieve an increased number of women leaders in government are supported, particularly those which aim to address cultural barriers in the workplace and improve organisational practice in relation to human resource management.*

*The Auditor-General's analysis in 1995 demonstrated that women in the feeder group for management are at least as well-qualified and experienced as their male counterparts. This fact suggests that the answer to low representation of women in decision-making does not lie in those strategies designed to address any perceived deficits in women themselves.*

*Rather, as promoted by the Office of the Public Service Commissioner in the managing diversity approach, organisations and decision-makers need to employ practices which challenge the prevailing culture and particularly, those assumptions about women's capacity to successfully combine work and family responsibilities and organisational practices which impede women and men, to sensibly balance work and home.*

**Women in Parliament**

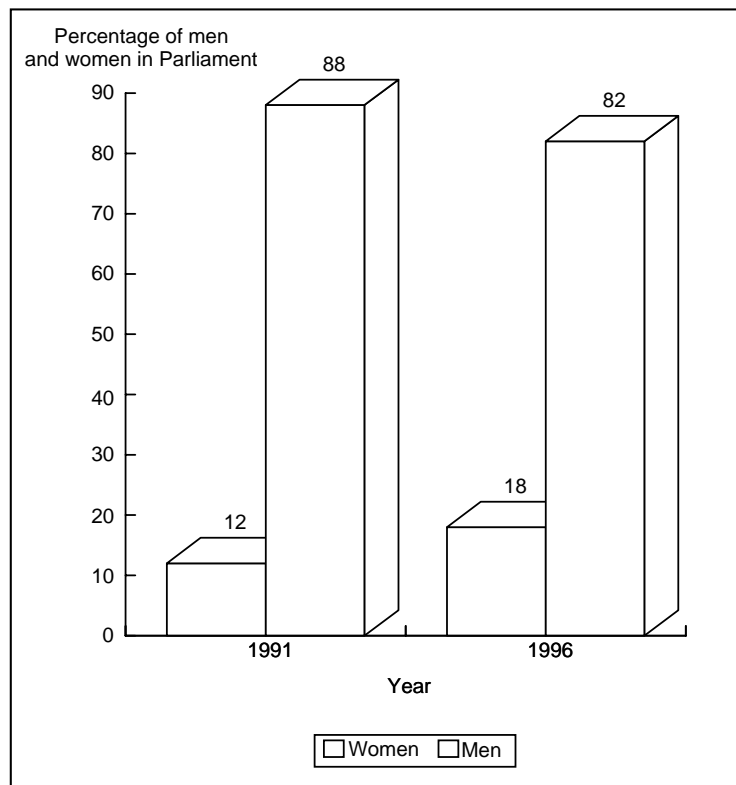
**4.1.17** Members of Parliament are generally responsible for answering queries from constituents in their electorate, fulfilling party duties and contributing to parliamentary debates, asking questions in the Parliament and introducing bills from time to time on issues which affect the community.

**4.1.18** According to information released by the Parliament of Victoria in relation to women in parliament, recognition of the contributions that women could make in Government has been a feature of Victoria's recent parliamentary history. A commentary by audit on the representation of women in the Parliament follows.

**4.1.19** In recent times women parliamentarians in Victoria have made significant progress in increasing the role they play in government. In the previous term of the Victorian Government, the Cabinet of 21 ministers included 2 women, each with major portfolio responsibilities, as well as a female Parliamentary Secretary of the Cabinet. In its current term, the Ministry has been reduced to 18 but the number of women increased to 4. Portfolios held by women ministers include that of Attorney-General as well as Fair Trading; Small Business and Tourism; Conservation and Land Management; and Housing. In addition, 2 of the 10 Parliamentary Secretaries are women.

**4.1.20** The representation of men and women in the Victorian Parliament in 1991 compared with 1996 is shown in Chart 4.1B.

**CHART 4.1B  
REPRESENTATION OF MEN AND WOMEN  
IN THE VICTORIAN PARLIAMENT**

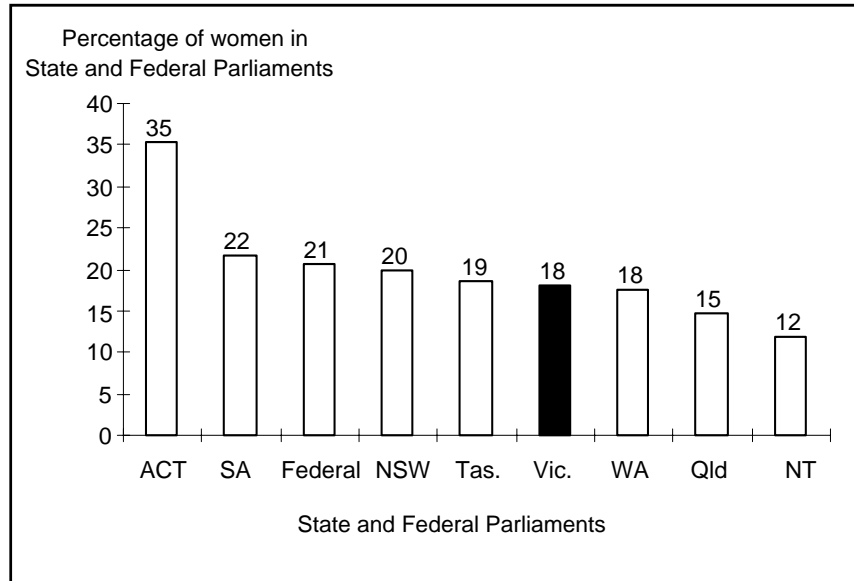


Source: Victorian Parliamentary Hansard, 1991.  
Information provided by the Victorian State Parliament in 1996.

**4.1.21** Chart 4.1C indicates that from 1991 to 1996, the representation of women in the Victorian Parliament increased from 12 per cent to 18 per cent.

**4.1.22** A comparison of the representation of women in Parliament across the various Australian State jurisdictions and at the Federal level is illustrated in Chart 4.1C.

**CHART 4.1C  
REPRESENTATION OF WOMEN IN BOTH STATE AND  
FEDERAL PARLIAMENTS IN AUSTRALIA, APRIL 1996**



Source: Information provided by individual Parliaments.

**4.1.23** The above chart shows that, with the exception of the situation in the Australian Capital Territory and the Northern Territory, the proportion of female parliamentarians in the Victorian Parliament is similar to that of the other political jurisdictions.

**4.1.24** In terms of the aggregate representation of women in Parliament at a State and Federal level, women were elected to 161 seats (19 per cent) out of a total of 842 seats. The number of seats held by women according to each particular jurisdiction follows:

- Australian Capital Territory, 6
- South Australia, 15
- Federal, 46
- New South Wales, 28
- Tasmania, 10
- **Victoria, 24**
- Western Australia, 16
- Queensland, 13
- Northern Territory, 3.

# Part 4.2

## Outsourcing Information Technology

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### KEY FINDINGS

- A formal business case to justify the decision to outsource the information technology (IT) functions of VicRoads and the Public Transport Corporation (PTC) was not prepared.  
*Paras 4.2.25 to 4.2.30*
- The request for proposals was open to interpretation by the respondents and inhibited the evaluation process.  
*Paras 4.2.45 to 4.2.53*
- The timeframes for the project did not take into consideration the enormity and complexity of the project.  
*Paras 4.2.58 to 4.2.63*
- The PTC paid the outsourcer approximately \$2.2 million in the first year of the contract for services that were not required.  
*Paras 4.2.100 to 4.2.101*



**OUTSOURCING INFORMATION TECHNOLOGY**

**Introduction**

**4.2.1** Outsourcing involves an arrangement whereby an external provider assumes responsibility for performing agency functions at a pre-determined price and according to pre-defined performance criteria. Although outsourcing changes the means of delivering services, it does not change an organisation's accountability for ensuring that the services are delivered. Under outsourcing, an organisation's focus shifts from managing the inputs of service provision to managing the outcomes. It becomes a contract manager rather than a resource manager.

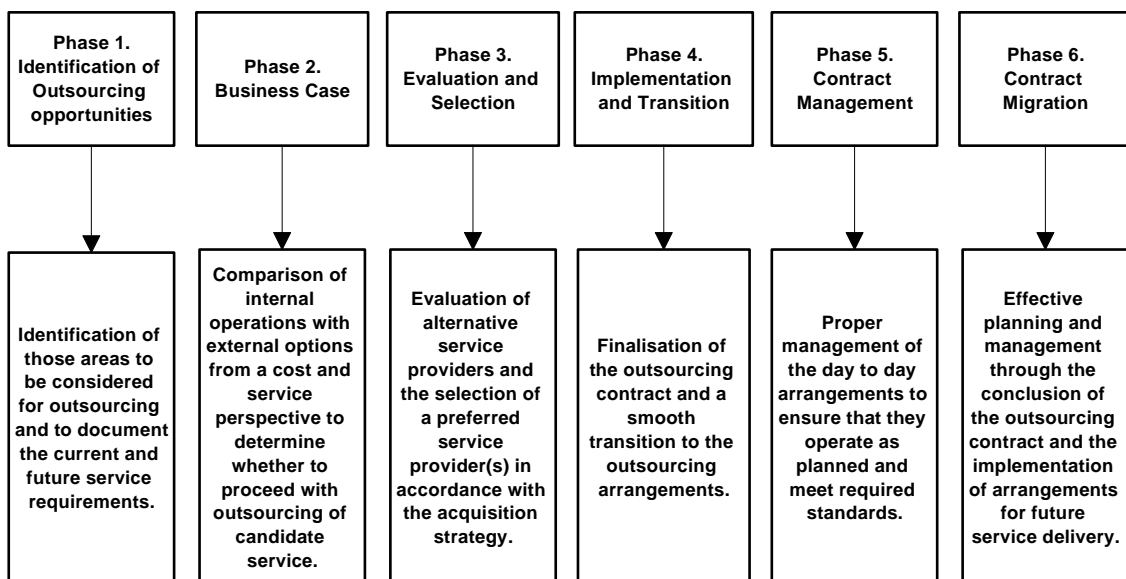
**4.2.2** The audit examination of outsourcing, which has formed part of an ongoing work program of my Office over recent years, has included coverage of the:

- Outsourcing of the information technology services of Melbourne Water in order to assess the management control framework designed to protect its strategic and operational interests arising from the establishment of a private company (Melbourne Information Technology Services Ltd). This company was formed to provide all existing information technology services and to be sole supplier to Melbourne Water of new information technology developments and acquisitions. The key lesson to be learnt from this audit was the failure to ensure adequate provision for competitive forces. Where practical problems arise in terms of the application of competitive influences to particular elements of IT services, audit considered that agreement between the parties should be reached on externally-derived evaluative benchmarks for progressively assessing costs and quality of services.
- The State Electricity Commission of Victoria's outsourcing program from the period February 1991 to December 1993 involving contracts of \$554 million. The aim of this audit was to determine whether the management of outsourcing activities had been conducted in an economic, efficient and effective manner. Audit findings included:
  - the SECV Board's involvement in the outsourcing process was limited, notwithstanding the magnitude of the outsourcing arrangements entered into and the fact that the SECV was the pioneer in Victoria in entering into such extensive contractual arrangements;
  - the majority of the businesses involved were not adequately analysed, therefore audit was unable to determine whether the decisions were soundly based;
  - the groups did not formally document quantifiable objectives and targets to enable the performance of contractors to be measured;

- in some instances the best possible outsourcing arrangements may not have been obtained, particularly where insufficient time was given to prospective contractors to submit Registrations of Interest and tenders, or the open market was not accessed;
- contractual arrangements entered into had, on occasions, provided substantial financial incentives to the contractors, such as payment for future voluntary departure packages, compensation for idle resources, provision of minimum work guarantees and payments for mobilisation and demobilisation costs, to ensure that the outsourcing process was not jeopardised; and
- systems and procedures had not been established to monitor the outcome of various outsourcing arrangements and to report on these arrangements.

**4.2.3** The Government is committed to outsourcing and contracting-out as part of its objective to create a more competitive customer focused service across government. There is extensive outsourcing activity across the Victorian public sector supporting service improvement and cost reduction, separation of policy making and regulatory functions from service provision functions and fostering of competition between potential supplier organisations. In support of the objectives, the Department of Treasury and Finance has established an Outsourcing and Contract Management Unit which provides advice and consultancy support on outsourcing strategies, techniques and specific applications.

**4.2.4** In December 1995, the Outsourcing and Contract Management Unit in conjunction with a chartered accounting firm developed an Outsourcing and Contract Management Guide which provides guidance on outsourcing and contract management. The guidelines expand on the broad guidance material previously issued by the Office of State Owned Enterprises and are aimed at assisting management in preparing requests for proposals, establishing selection criteria, evaluating proposals, formulating contract documentation and implementing effective contract management arrangements. The guidelines segment the phases of an outsourcing project into the following:





**4.2.5** As part of the ongoing review of outsourcing measures, in February 1996, my Office commenced an examination of the outsourcing of information technology at the Public Transport Corporation and the Roads Corporation. This audit assessed:

- the efficiency and effectiveness of outsourcing in meeting agency objectives;
- whether the processes followed to select the outsourcer were appropriate; and
- whether appropriate monitoring procedures to assess the performance of the outsourcer were implemented.

## BACKGROUND

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**4.2.6** The Public Transport Corporation (PTC) provides metropolitan, country and intrastate transport services. Roads Corporation (VicRoads) manages Victoria's road system through planning, designing, constructing and maintaining roads, managing road use through registered vehicles, licensing drivers and traffic management and providing information and road-user services. Both organisations extensively use information systems to support management and users.

**4.2.7** In late 1989, the PTC began examining the possibilities of the rationalisation of its IT operations by the sharing of a data centre. To ascertain the viability of such an action, a number of selected vendors were invited, in July 1990, to propose solutions for the rationalisation of the computer processing functions. Other information technology (IT) functions, including application development and maintenance, end user support and network facilities were not considered as part of this initiative.

**4.2.8** During September 1990, VicRoads and the PTC proposed the provision of a merged data centre by a selected vendor. While the principle of a merged data centre was supported by the Government, it rejected the process of selective tendering on the basis that it did not incorporate public tendering. In November 1991, the preparation of a Request for Tender for the provision of a merged data centre was commenced.

**4.2.9** During July 1992, the then Government required that the Request for Tender be amended to extend the scope of IT services to be outsourced beyond the provision of a data centre, to encompass any IT functions that prospective respondents may wish to provide. In addition, the Request for Tender had to incorporate the option for the outsourcer to be based at Ballarat.

**4.2.10** The purpose in outsourcing the Corporations' IT services was to:

- provide for the ongoing delivery of information technology services which meet the PTC's and VicRoads' current and future needs, consistent with other government requirements; and
- receive those services at costs significantly below those currently experienced by the Corporations.





**4.2.11** The outsourcing of these services was part of an extensive government program designed to increase information technology outsourcing by public sector agencies from the level which existed at that time (approximately 30 per cent) to around 70 per cent by December 1994, subject to value-for-money, agency efficiency and public policy considerations. The Government's information technology industry development objectives and commitment to increase employment in Ballarat was a key consideration when outsourcing the information technology functions of the PTC and VicRoads.

**4.2.12** In November 1992, the newly elected government endorsed the previous government's decision to locate the outsourced facilities at Ballarat.

**4.2.13** During December 1992, the Department of Transport, which had responsibility for managing the project, advertised for Expressions of Interest to provide IT services to the PTC and VicRoads. Responses were received by April 1993, from 9 vendor groups.

**4.2.14** A project team led by an external management consultant and including staff seconded from the PTC and VicRoads was established by the Department of Transport to evaluate these responses. In July 1993, a recommendation was made that 5 of the respondents should be invited to participate in the subsequent tender process. Request for Proposals were issued in October 1993.

**4.2.15** Under a direction from the Premier in late October 1993, the Minister for Finance who was responsible for Statewide outsourcing took over responsibility for the PTC and VicRoads outsourcing project. Responsibility for its management was transferred from the Department of Transport (DOT) to the Department of Finance (now known as the Department of Treasury and Finance - DOTF).

**4.2.16** After responses had been received, a chartered accountancy firm was appointed to establish an evaluation criteria to assess responses to the Request for Proposal. In April 1994, a Steering Committee, managed by Department of Finance, with representatives from Department of Transport, VicRoads, the PTC, the Department of Premier and Cabinet, and Department of Business and Employment (DBE) analysed the responses and short-listed 2 applicants. The 2 tenderers selected were given the opportunity to provide "best and final cost proposals" before the Steering Committee made its recommendation to Cabinet in late June 1994. In July 1994 Cabinet gave approval subject to, inter alia:

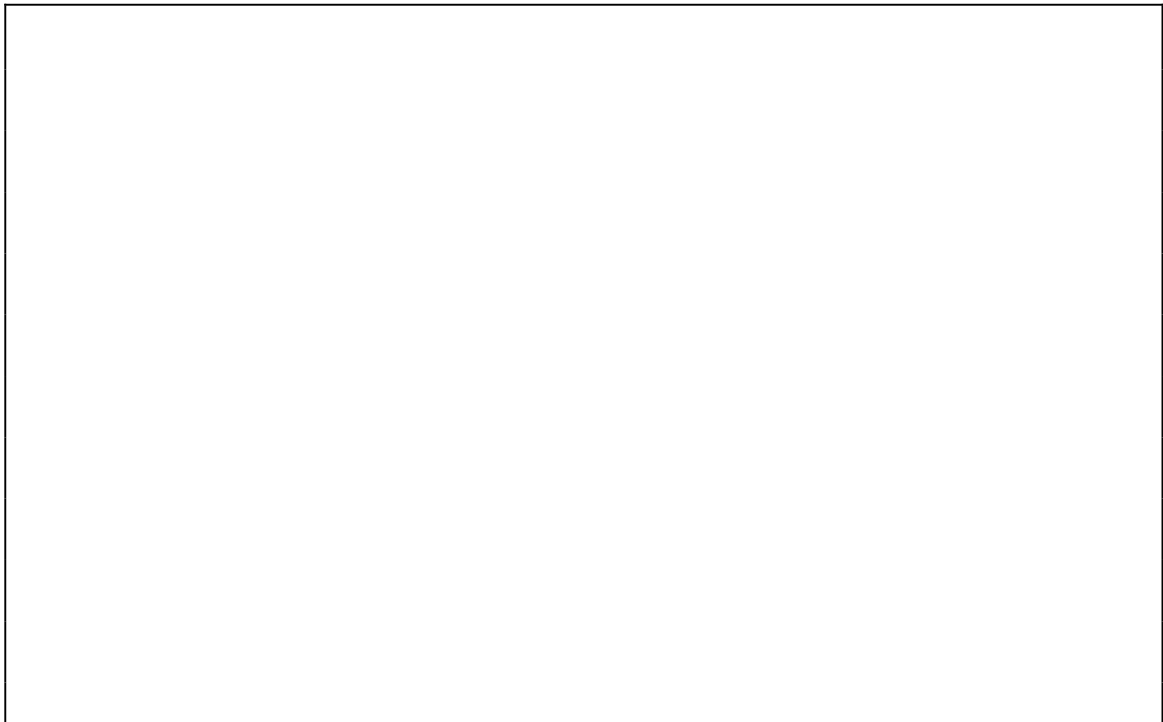
- PTC and VicRoads entering into due diligence and contract negotiations with the preferred tenderer; and
- a determination by the Treasurer and the Minister for Public Transport and the Minister for Roads and Ports of the funding sources for the marginal cost of providing the services from Ballarat compared with providing them from Melbourne.



**4.2.17** On 14 November 1994, the Premier announced that the 2 transport corporations and the preferred tenderer had agreed on the terms and conditions of proposed contractual arrangements for the delivery of information technology services from Ballarat.

**4.2.18** On 16 November 1994, separate contracts were entered into by the PTC, VicRoads and the preferred tenderer for the provision of IT services. The 4 main service areas included in the contract were end-user services, network services, application maintenance and enhancement and computer processing services.

**4.2.19** VicRoads and the PTC personnel retain responsibility for the development and implementation of the information system's strategy and ensuring all users including external service providers comply with established policies and standards. They remain responsible for the monitoring and evaluation of the performance of the outsourcer and ensuring the services provided meet the needs of management and users.



*PTC and VicRoads Data Centre located at Ballarat.*



## OVERALL CONCLUSION

**4.2.20** Faced with the need to update the IT facilities at the PTC and the prospect of efficiency savings from the rationalisation of services with VicRoads, the transport authorities embarked on an outsourcing program designed to reduce costs and improve efficiency.

**4.2.21** The program has been extensive in size and has been undertaken in a relatively short timeframe.

**4.2.22** Both the PTC and VicRoads consider that overall, the outsourcing arrangements have been successful and achieved the major objective of delivering a timely and efficient IT service which satisfies the operational, business and management needs of both organisations in accordance with quality, performance and functional requirements.

**4.2.23** The audit review has, in some respects, confirmed the views of the PTC and VicRoads that the benefits from outsourcing have been realised. There is little doubt that significant gains have been achieved in the quality of the services provided. In addition, the outsourcing arrangements addressed the regional development objectives of government, in particular the proposed location of the facilities at Ballarat.

**4.2.24** The examination of the outsourcing arrangements undertaken during the project identified areas where the processes could have been improved. Specifically, audit found that:

- there was no formal business case developed to support the decision to outsource the IT facilities of the PTC and VicRoads;
- not all costs were included in the cost comparisons between the outsourcer and internal agency costs;
- the timeframes for the project failed to take into consideration the enormity and complexity of the project;
- the request for proposal document was open to interpretation by the tenderers and inhibited the evaluation processes; and
- the PTC's service requirements for the first year of the contract were over-estimated and as a result the PTC paid approximately \$2.2 million for services that were not required.

IDENTIFICATION OF  
**OUTSOURCING OPPORTUNITIES - THE BUSINESS CASE**

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**4.2.25** The Office of State Owned Enterprises' outsourcing guidelines require that any outsourcing opportunities must be fully evaluated to justify whether functions or activities should be performed internally or outsourced. The scope of the activity to be outsourced needs to be defined and involves identifying the current and excess service levels, possible improvements and expected benefits. This high level evaluation requires that consideration be given to:

- short and long-term analysis of the business;
- identification of internal and external threats;
- determination of the impact of outsourcing on key elements of the operating environment including industrial relations, human resources and government initiatives;
- determining the current and projected utilisation of the function or service to be outsourced; and
- evaluation of the available options including an assessment of the costs.

**4.2.26** After performing these tasks, a documented "case" should be prepared and approved by the relevant staff, which recommends either outsourcing or in-house supply of those services.

**4.2.27** The outsourcing project commenced with an advertisement for Expressions of Interest to be submitted by interested parties and the evaluation of responses resulted in a recommendation to limit further negotiations to 5 of the 9 respondents. Subsequently, a request for proposals document was prepared by the DOT and responses were evaluated in detail and compared against both each other and in-house costings. Two potential tenderers were selected to undergo further evaluation and subsequently a preferred tenderer was selected.

**4.2.28** As the decision had been made by the Government to outsource the IT functions of the PTC and VicRoads, the evaluation process undertaken by the Steering Committee short-circuited the strategic business evaluation and a formal business case to justify the decision to outsource was not prepared.

**4.2.29** The method used by DOT to outsource IT services to the PTC and VicRoads risked wasting significant resources in the event that provision of IT services in-house had proven to be the most economical alternative. (Evaluation of prospective tenderers was undertaken between April 1993 and July 1994, by senior staff at the PTC, VicRoads, DOT, DOTF and DBE, with expert assistance from a chartered accountancy firm.)

**4.2.30** To utilise resources in the most efficient manner, there is a need for comprehensive strategic business analyses, which take into account all options available, including the development of a business case comparing internal operations with external options, from a cost and service perspective, to ensure that future decisions to outsource are justified and soundly based. These decisions should be clearly and comprehensively documented.

**Cost comparisons**

**4.2.31** In addition to undertaking a strategic business analysis it is essential to clearly define objectives that are supported by quantifiable benefits and savings. In accomplishing an effective cost comparison:

- all IT costs which cannot be transferred to the service provider should be identified and eliminated from the comparison;
- costs associated with any inefficiencies in current operations should be eliminated, so that vendor prices are compared to internally provided, efficient services;
- costs associated with implementing the outsourcing arrangements, e.g. preparation of specifications, evaluation of tenderers, legal and consultancy costs should be identified;
- costs associated with monitoring the service provider should be identified; and
- overhead costs which can be transferred to the service provider should be identified.

**4.2.32** Generally throughout the IT industry, cost savings are not a major outcome of outsourcing. Improvement in service and the ability to concentrate on core activities are some of the more likely benefits to arise.

**4.2.33** The PTC and VicRoads were required by the Steering Committee to develop internal cost estimates for provision of those IT services being considered for outsourcing, over a 5 year period. It was estimated that the outsourcer could provide the services over a 5 year period at a cost approximately \$24.4 million less than the PTC and VicRoads in a shared facility. The costing information highlighted that for the PTC the selected tenderer could supply three of the 4 service areas at a lower price while for VicRoads only one of the services (computer processing) could be provided at a lower cost externally.

**4.2.34** The Steering Committee did not consider the alternative of retaining those services which were most cost efficient in-house and outsourcing only those services which could be performed more cost-effectively by the selected tenderer.

**4.2.35** In addition, the costs associated with managing the outsourcing project, including preparation of specifications, evaluation of tenderers, legal and consultancy cost arrangements were not estimated, monitored or included in any cost comparisons of internal versus externally supplied IT services. Audit has been unable to ascertain the magnitude of these cost or their impact on the outsourcing decision. Further, the costs associated with the PTC and VicRoads ongoing monitoring of the outsourcer after implementation were not included in cost comparisons.

**4.2.36** The PTC and VicRoads may have been able to achieve greater cost-savings if outsourcing of the 4 IT services under consideration had been evaluated individually against the preferred tenderer and internal costs, instead of as a package.



**4.2.37** Estimated cost savings associated with outsourcing were lower than calculated by the steering committee because transition and monitoring costs were never included as part of the cost of outsourcing. Therefore, cost comparisons used to assist in the outsourcing decision were incomplete.

**4.2.38** When performing a cost comparison of internally versus outsourcer provided services, all costs outlined above should be considered. To maximise cost savings associated with outsourcing, all IT services which are potentially suitable should be considered individually, unless they are inextricably linked.

□ *RESPONSE provided by the Department of Infrastructure*

*The Government made a decision in principle to outsource the IT functions of the PTC and VicRoads. The process undertaken by the Steering Committee during 1993 through the evaluation of the Request for Tender (RFT) was to determine whether prima facie case for outsourcing existed and the scope of the services to be outsourced. As alluded to in paragraph 4.2.33, the final decision to outsource was taken only after a thorough comparative evaluation of all the options, including the 5 commercial proposals received, the proposals of the agencies acting independently, the proposals of the agencies acting collectively and the proposals of the agencies acting collectively with the services to be outsourced from Ballarat.*

*A thorough comparative evaluation of the economic advantages of the option to provide the services in-house was undertaken.*

*The separation of computer processing from data network and end user services (help desk) would have created extreme difficulties in determining accountabilities and clear lines of responsibilities. All bidders were invited to submit prices for all services as a whole and in separate parts.*

**EVALUATION AND SELECTION**

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**4.2.39** The selection of a contractor to undertake the function to be outsourced consists of the following distinct phases:

- advertising for Expressions of Interest - a public invitation to firms to register their interest in performing the function;
- issuing a Request for Proposal - a public or selective invitation to firms to tender for a function;
- evaluation of the tenders received; and
- awarding the contract after obtaining the required approvals.

**Expressions of Interest**

**4.2.40** In December 1992, an advertisement was placed by the DOT requesting Expressions of Interest to provide for the outsourcing of IT services for the PTC and VicRoads. During discussions with senior management of the PTC and VicRoads, audit was advised that neither VicRoads nor the PTC had been approached in regard to the content of the advertisement.



**4.2.41** The advertisement was general in that it did not outline those specific IT services being considered for outsourcing and as a result responses received varied greatly in the information and detail provided, e.g. the types of IT services offered and costing information. The project team responsible for assessing responses had, therefore, to evaluate the potential tenderers using information which was not comparable.

**4.2.42** The *IT Outsourcing Expressions of Interest Review Report* prepared by the chartered accounting firm stated that "... In applying the criteria the team were hampered by the generality of the Expressions of Interest responses and the lack of detail provided, particularly in the area of financial data. This was a result of the open-ended nature of the Expressions of Interest specification, briefing inconsistencies and commercial reticence on the part of the tenderers. While further detail was requested and some provided it was not sufficient to enable a satisfactory financial analysis to be undertaken".

**4.2.43** The Expressions of Interest received were not directly comparable and provided insufficient financial information, however, they were used to eliminate 4 of the 9 respondents from any further negotiations. Their use in reducing the prospective tenderers may have resulted in prematurely eliminating respondents who may have provided IT services directly competitive with the other submissions.

**4.2.44** While it is appreciated that a request for Expressions of Interest need not be as particular in its requirements as the Request for Proposals document, it is important that information requested is specific enough to ensure that responses received will be comparable for the purpose of later evaluation.

*□ RESPONSE provided by the Department of Infrastructure*

*Comprehensive information packages were prepared by the agencies and provided to interested parties. In January 1993, a public presentation of the proposal was conducted at the Kew offices of VicRoads. This presentation was widely advertised and very well attended by the computer industry. In the weeks following the presentation, unlimited opportunity was given to prospective respondents to query aspects of the proposal and the range and scope of existing IT services.*

*It was by intention that the advertisement was general. Its general nature was to elicit creative responses and suggestions from the computer industry in order to assist and enable the project team in its task of preparing a case for outsourcing and determining the scope and services to be outsourced.*

**The Request for Proposals document**

**4.2.45** The Request for Proposals document should cover a number of areas, including:

- the organisation's business requirements;
- functional and service requirements for IT delivery;
- contractual and management requirements;
- payment terms and requirements;
- staff and asset strategies and options; and
- the evaluation methodology and selection criteria.



**4.2.46** The Request for Proposals document, issued by the DOT in early October 1993, was a comprehensive document which required the selected tenderers to provide information on all topics outlined above.

**4.2.47** In order to respond to the Request for Proposals document, each of the tenderers had to complete detailed costing schedules, including 7 different variations in service load for both the PTC and VicRoads, for each of the 4 IT services selected for outsourcing. Despite the above requirement, the Steering Committee when assessing each of the tenders against the "Financial Impact" criteria only evaluated 2 of the 7 costings being those service loads most likely to eventuate. During discussions with senior management audit was advised that due to time constraints it was not feasible for the Steering Committee to consider all 7 costings provided.

**4.2.48** As some of the information required by the Request for Proposal was not useful to the subsequent evaluation of the tenderer, the respondents invested a large amount of time and resources gathering data unnecessarily. After receiving the responses, the project team invested resources in determining what information was useful in the evaluation process rather than undertaking the assessment against predetermined criteria.

**4.2.49** **When preparing the Request for Proposals document, it is important that the information required for subsequent assessment be clearly established to ensure that only relevant information is requested from tenderers and responses are received in a timely manner.**

**4.2.50** When preparing their proposal document, the tenderers were required to submit queries regarding the Request for Proposal in writing to the DOTF. Three hundred and sixty queries were received from 5 tenderers, the majority of which focused upon clarifying pricing information.

**4.2.51** Some requirements specified in the Request for Proposal were open to different interpretations by the tenderers. During the evaluation stage, one of the tenderer's had incorrectly interpreted a Request for Proposal requirement of 99.97 per cent network availability to mean that all points of the network had to be available for that percentage of time. As a result their initial costing submitted was higher than other respondents as they had provided for duplication of the network. By contrast, one of the other tenderer's had correctly interpreted that the network, as a whole, had to be operational 99.97 per cent of the time and not every individual component. After discussions with the first mentioned tenderer, their misinterpretation of the requirements was recognised and they were subsequently able to amend their costings and submit a lower tender price during the final evaluation stage of the tenders.

**4.2.52** As specifications included in the Request for Proposal were unclear or ambiguous, numerous queries had to be answered by the Project Manager and it is possible that the tenderers may have submitted costings based on misinterpreted system specifications. Table 4.2B provides an indication of the number of queries directed to the Project Manager by the respective tenderers.



TABLE 4.2B

| <i>Tenderer</i> | <i>Number of queries</i> |
|-----------------|--------------------------|
| A               | 92                       |
| B               | 51                       |
| C               | 36                       |
| D               | 106                      |
| E               | 75                       |
| <b>Total</b>    | <b>360</b>               |

**4.2.53 Ambiguity in the Request for Proposal should be minimised to ensure that competing proposals have been prepared and evaluated on a common basis.**

*□ RESPONSE provided by the Department of Infrastructure*

*The proposal to outsource the IT services of the PTC and VicRoads broke new ground in complexity and magnitude in the introduction of IT outsourcing in Australia, for either a government or commercial undertaking. The RFP documents were most comprehensive in their description of the requirements. Notwithstanding the extent of detail provided in the documents, it was anticipated that some matters would require clarification. Every opportunity was given to all tenderers to clarify their concerns to obviate misinterpretation of system specifications. The tenderers submitted many queries to the project manager and were thankful for the opportunity to clarify issues.*

**Process to evaluate Proposals**

**4.2.54** A detailed evaluation of responses to the Request for Proposal should be conducted, in accordance with pre-determined criteria and address the following areas:

- capability of the tenderer, including relevant experience and qualifications of key personnel;
- technical assessment to ensure specification requirements have been met;
- contractual assessment to determine whether any contractual qualifications and variations are acceptable; and
- financial assessment to assess the net present values of competing bids.

**4.2.55** The chartered accounting firm engaged to assist with the management of the project developed a formal methodology for the evaluation of tenders which was approved by the Steering Committee.

**4.2.56** Upon completion of the Initial Assessment, the Project team recommended that one of the 4 bids be eliminated from consideration, as a non-compliant bid had been submitted. The relevant tenderer had not met the requirement that the outsourcing of the Corporations' information technology functions "result in an employment increase in Ballarat by more than 100 jobs". The steering committee ignored this recommendation and the submission was fully evaluated along with the other 3 tenders.



**4.2.57** While the methodology followed in the evaluation of the tenderers helped ensure that an objective assessment, which considered all relevant factors, was undertaken, it was not adhered to in that non-compliant bids were not eliminated from detailed evaluation. **Accordingly, significant resources were used in evaluating a response which did not comply with Request for Proposals requirements and was highly unlikely to be successful.**

**Project completion dates**

**4.2.58** To effectively manage an outsourcing project, it is important that separate stages of the task be identified and progress should be monitored against established deadlines.

**4.2.59** The DOT prepared early targeted completion dates for the major phases involved in the project. These targets proved to be inaccurate and were revised by the DOT in late August 1993. Completion dates are outlined in Table 4.2C.

**TABLE 4.2C**

| <i>Phase</i>                                                          | <i>Revised completion dates</i> | <i>Actual completion</i> |
|-----------------------------------------------------------------------|---------------------------------|--------------------------|
| Phase 1 - Preparation and Release of Request for Proposal             | 20/09/93                        | 11/10/93                 |
| Phase 2 - Outsourcer Selection                                        | 31/12/93                        | 13/07/94                 |
| Phase 3 - Implementation - (Finalise contracts and manage transition) | 30/03/94                        | 28/11/94                 |

**4.2.60** From discussions with senior management involved in managing the outsourcing project, the major reason provided for the difference between targeted and actual completion dates was a lack of experience in managing an outsourcing project of this magnitude and underestimation of the complexity and effort required to undertake the project.

**4.2.61** The phase which caused the greatest delay was selection of the outsourcer, which took 5½ months longer than anticipated. While responses to the Request for Proposal had been received by 26 November 1993, the development of a methodology to evaluate the proposals did not commence until mid-December, following the appointment of a chartered accounting firm to assist in the process. The evaluation strategy was approved by the Steering Committee in early February 1994. During this period the tender documents were held by the Tender Board in escrow.

**4.2.62** As the early timeframes, prepared by DOT, failed to take into consideration the enormity and complexity of the project and in particular the time required to establish a selection criteria, the outsourcing project was implemented 8 months after the anticipated date.



**4.2.63** To avoid significant increases in the estimated cost and time involved to complete an outsourcing project, management need to consider in detail the tasks required in each phase. Government policies and guidelines and experience of organisations who have undertaken IT outsourcing should be used to assist in this task.

**Use of specialist consultants**

**4.2.64** In December 1993, a firm of chartered accountants was engaged to undertake a consultancy assignment for the evaluation phase of the project. The principal requirement of the consultancy was to undertake the following:

- design and develop an appropriate framework for the evaluation of the responses to the Request for Proposals including the development of specific criteria for subsequent endorsement and approval of the steering committee;
- evaluate the responses to the Request for Proposals and the preparation of evaluation reports detailing each response in accordance with the previously agreed/approved criteria; and
- the presentation of a final evaluation report containing recommendations on the preferred tenderer by the steering committee.

**4.2.65** During the period December 1993 to April 1994, the consultants discharged their responsibilities and provided valuable input into the project. At the steering committee's April meeting the consultant's detailed analysis report was considered and its recommendations adopted.

**4.2.66** In early June 1994 the same firm of chartered accountants was invited, in conjunction with a number of other firms, to submit a proposal to be the management consultants for the implementation phase of the project. After due evaluation and consideration of the complexities of the assignment, the skills and previous experience needed for the successful completion of the project the same firm was appointed in early July.

**4.2.67** From discussions with senior management of the PTC and VicRoads and review of appropriate documentation it is clear that the specialist consultant provided significant input into the project and the knowledge, skills and experience, displayed by the consultant, were of great benefit to all parties involved and a major contributing factor to the final outcome of the project.

**4.2.68** The benefits to be derived from engaging a consultant with the appropriate level of knowledge, skills and experience in IT outsourcing projects are significant and should be given serious consideration when future projects of this type are entered into.

**The steering committee**

**4.2.69** A steering committee was established subsequent to the advertisement for Expressions of Interest and it had an important, ongoing role in managing the outsourcing project. It included an external consultant (chairperson), the Chief Executive Officers of the PTC and VicRoads (who had responsibility for ensuring the business objectives of the Corporations were met), the Secretary of the Department of Transport and senior representatives from the Departments of Treasury and Finance, Premier and Cabinet and Business and Employment.

**4.2.70** The principal responsibilities of the steering committee were to:

- supervise the outsourcing evaluation project;
- review and approve the project charter, project workplan, evaluation mechanism and decisions to eliminate tenderers from consideration; and
- review the evaluation and recommendations of specialist contractors engaged and to determine the preferred tenderers.

**4.2.71** The steering committee met regularly throughout the project to discuss important issues, consider recommendations presented by the project teams and external consultants and assumed day-to-day responsibility for making decisions. Important decisions were referred by the steering committee to the Minister for Finance for ratification. From discussions with senior representatives from the Transport authorities and review of relevant documentation, the steering committee discharged its responsibilities in a competent manner and made a significant contribution to the project.

**4.2.72** Audit is of the view that it was appropriate that responsibility for managing the outsourcing project be removed from those organisations directly affected and vested with the Minister for Finance and co-ordinated by an independent steering committee. These arrangements ensured an objective, unbiased approach to the project.

**4.2.73** To help ensure that future major outsourcing projects are effectively managed, it would be of benefit to establish an independent steering committee, with a chairperson independent of the organisation(s) engaging in the outsourcing activities. In addition, representatives from the outsourcing unit at DOTF should be actively involved and if regional issues arise then DBE should be consulted.

**IMPLEMENTATION AND TRANSITION**

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**4.2.74** In July 1994 a chartered accounting firm was appointed to manage the implementation of the project. The terms of reference for this consultancy included:

- development of an implementation plan;
- negotiations with the tenderers;
- preparation for, and execution of, transition; and
- establishment of guidelines for the contract management phase.

**4.2.75** By late July an implementation plan had been developed and approved by the steering committee. The plan was comprehensive and involved a thorough process by which the PTC and VicRoads were well placed to outsource their IT facilities.

**Contractual arrangements**

**4.2.76** The tender process not only forms the basis for selecting a contractor, but outlines the principal terms and conditions to be included in the ensuing contracts. A contract should:

- include standard contract terms and conditions to ensure consistency with similar contracts;
- provide the contractor with adequate incentive to operate efficiently and effectively
- ensure the interests of the organisations are protected by:
  - setting qualitative and quantitative performance targets and guarantees;
  - including appropriate default, penalty and insurance clauses in the event of poor performance;
  - provide for a reasonable sharing of the risks; and
  - excluding any guarantees or incentives that could impact adversely on outsourcing benefits.

**4.2.77** Between July and November 1994 the implementation phase included the preparation and negotiation with the preferred tenderer on contracts and due diligence examinations by both the outsourcer and the PTC and VicRoads.

**4.2.78** Legal advice and guidance was provided from a firm of solicitors, engaged in June 1994. In addition, an Implementation and Transition Committee (comprising representatives from the outsourcer, the chartered accounting firm, the PTC and VicRoads, DOT and DOTF) met throughout the period July to November to ensure the implementation progressed as planned.

**4.2.79** It is pleasing to note that the contractual negotiations, due diligence processes and, in general, the implementation and transition followed the plans as developed by the chartered accounting firm.

**4.2.80** On 16 November, contracts were executed and exchanged between the outsourcer and the 2 transport organisations. The contract specified that the outsourcer was to provide the 2 transport corporations with computer processing, data networking, end-user services and applications maintenance and enhancement services.

**4.2.81** On 28 November the project's status changed from implementation to Contract management with all responsibilities being assumed by the PTC and VicRoads.

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**CONTRACT MANAGEMENT**

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**4.2.82** To determine whether the objectives anticipated from outsourcing have been achieved, appropriate policies, systems and procedures must be developed to enable management to monitor the performance against the contract. Performance indicators should be developed which are realistic, meaningful and subjected to regular review with all identified variances actioned. The audit review addressed a number of issues which revealed that the management of the contract has scope for improvement. Comments are provided in the following paragraphs.

**Partnering arrangements**

**4.2.83** VicRoads and the outsourcer have entered into a partnering arrangement whereby the common values and objectives of both the outsourcer and VicRoads in achieving the most effective IT service have been established.

**4.2.84** Each month, both parties rate the services provided by the outsourcer against the established values and objectives. The ratings are discussed at monthly meetings providing the forum for both parties to openly discuss any problems, resolve issues and to build upon benefits.

**4.2.85** **The partnering arrangement is a positive initiative which ensures that the contract is approached as a partnership with benefits derived by both parties.**

**4.2.86** In contrast with VicRoads, the PTC does not have a partnering arrangement. On the basis that the PTC already had, through regular meetings with the outsourcer, established a good working relationship, it did not consider a partnering arrangement would add additional benefits.

**International benchmarking**

**4.2.87** Essentially, benchmarking is a comparison of an organisation's business practices to those of other similar organisations to generate ideas on how to make improvements. It provides a criteria to measure the service delivery provided by the outsourcer. Prior to outsourcing the IT functions, VicRoads actively engaged in benchmarking its IT services against international benchmarks.

**4.2.88** The contract provides that the outsourcer will complete and present annually, internationally recognised benchmark metrics on the quality and cost of service delivery to VicRoads and the PTC and to incorporate the results in performance reviews. In November 1995, the outsourcer with the assistance of an external consultant produced a Comparative Benchmark Evaluation Report for only one of the outsourced services, namely, application maintenance and enhancement. A report on this outsourced service compared to the benchmark in respect to the PTC has been finalised whereas the report for VicRoads is in draft and awaiting their comments.

**4.2.89** The benchmarking exercise for the remaining 3 outsourced services, namely, computer processing services, data network services and end-user services which should also have been completed by November 1995 has not been undertaken. Accordingly, the outsourcer has not, at this stage, fully complied with the contractual obligations.



**4.2.90** Until such time as internationally recognised benchmarks are established for all of the outsourced services, neither VicRoads nor PTC are in a position to know if the standard of services provided are appropriate.

*□ RESPONSE provided by the Department of Infrastructure*

*VicRoads has responded to the benchmark of the Applications Maintenance and Enhancement services on 17 April 1996. The response accepts the Report.*

**Performance monitoring and reporting**

**4.2.91** To measure performance, the contract needs to have clearly established objectives and quantifiable criteria. Performance indicators should then be developed which are realistic, meaningful and subjected to regular review with all identified variances actioned.

**4.2.92** Both VicRoads and the PTC require the outsourcer to provide, on a timely basis, performance reports. The data contained in these performance reports is used to calculate credit adjustments against the monthly service payments to the outsourcer. Credit adjustments occur where the service levels provided by the outsourcer are less than the service levels specified in the contract.

**4.2.93** VicRoads receive monthly service reports from the outsourcer, however, they have not developed validation processes other than for computer processing services. Although the validation exercise requires extensive experience to undertake audit found that the procedures are not formally documented .

**4.2.94** There are no procedures in place within the PTC to ensure the validity of the data provided by the outsourcer in the monthly service reports. The PTC indicated that the contract was established on the basis of an honour system, with both the outsourcer and the PTC having the opportunity to audit and review items reported if required.

**4.2.95** The PTC have not retained staff with the skills necessary to engage in the analysis and review of performance data and as a result would need to rely upon external sources to conduct any assessment to ascertain the validity of information contained within the service reports.

**4.2.96** As the information provided to VicRoads and PTC in the service reports is not validated, it is possible that the information included may not be a true indicator of the outsourcer's performance and service charge adjustments may not be correct.

**4.2.97 Both the PTC and VicRoads need to establish procedure which will enable validation of computer processing data and provide staff training in those procedures**

**4.2.98** Aligned with the performance monitoring of the outsourcer are the annual adjustments to the contract fee agreed to by the outsourcer and both VicRoads and the PTC.



**4.2.99** VicRoads contract fee for year 2 has been based on the actual service levels provided in year one, the annual assessment of the future growth in transaction processing and the additional cost of new services that were included in the contract in December 1995. As a result, the monthly contract service cost for VicRoads has increased by approximately \$34 000. This supports the view that VicRoads original estimates of present and future service levels were reasonably accurate.

**4.2.100** The first year's payments to the outsourcer by the PTC were based on an estimated quantity of service. The actual services required were far less than the contracted service levels and consequently, the PTC paid approximately \$2.2 million for services that were not required. The PTC and the outsourcer have agreed that the service levels for the second year of the contract will be based on the actual service levels provided in year one and, accordingly, the monthly contract service cost for PTC has decreased by approximately \$181 700.

**4.2.101** With the experiences gained in the first 12 months of the contract, VicRoads and the PTC should be well positioned to determine the service levels required and ensure that appropriate adjustments are made to contract payments.

**□ RESPONSE** *provided by the Department of Infrastructure*

*The year one charges were based on the outsourcer's estimates of quantities of services to be provided, including once off items associated with applications conversion and network relocation. The year one charges were fixed. The outsourcer bore the risk that he might underestimate requirements, including conversion and relocation costs. The PTC had the protection that the costs were realistic and commercially competitive, as determined by a most thorough evaluation of a highly competitive RFP process.*

*In determining year 2 service levels, the actual service levels provided in year one and the estimates of growth in requirements in year two have been taken into account. The monthly contract cost has decreased in year 2 because of the absence of the year one once off items and a prospective decline in demand for some services in year 2 by comparison to year one.*

*This is a quality assured contract and therefore does not depend on continuous audit of detail data. VicRoads has authorised the conduct of 3 audits of the outsourcer by internal audit and its adherence to the contract deliverables and controls.*

**Master Quality Plan**

**4.2.102** The outsourcer has a contractual obligation to prepare a Master Quality Plan for review within 3 months of the contract commencement date. The master quality plan set out the widely accepted and recognised IT standards to be applied by the outsourcer in discharging the contract. It includes procedures and methodologies for areas such as change management, security and project management.

**4.2.103** The outsourcer prepared the Plan for both VicRoads and the PTC within the specified period.





**4.2.104** The master quality plan prepared for VicRoads has been approved and finalised in line with the contractual requirements. However, the draft plan for the PTC was reviewed during the months of March to September 1995 and concerns were expressed regarding the application maintenance and enhancement quality plan and as a result the plan is still not finalised.

**4.2.105** **Until the plan is agreed to then the PTC cannot ensure the ongoing quality of the service delivery by the outsourcer.**

**IT strategy**

**4.2.106** It is important that organisations considering outsourcing fully understand the business needs, challenges and opportunities, the management implications of IT and to assume effective management control of business applications planning, technology strategy and technical performance and quality.

**4.2.107** Each organisation should have a strategic plan and know where IT fits within that plan. If an organisation does not know where it wants to be and how IT is going to help it get there, it is harder to make good corporate decisions and achieve objectives. A soundly-developed IT strategy will help an organisation determine how to access those services, i.e. internally or through outsourcing. Outsourcing is not a substitute for an IT strategy and does not absolve management from the responsibility for IT services.

**4.2.108** Prior to commencement of the outsourcing project, VicRoads had a well-developed IT strategy which favourably positioned it in the consideration of outsourcing. By contrast, the PTC did not have an IT strategy prior to outsourcing and as a result would not have been as effective in establishing those IT services which were candidates for outsourcing. Since outsourcing, the PTC has focused upon the co-ordination of central infrastructure, with business units responsible for its own IT planning. Further, with the Government's plan to disaggregate the PTC, the development of an IT Strategy is still pending.

**4.2.109** **It is important that all organisations have, in place, soundly-developed IT strategies which support the business directions and corporate goals regardless of the resourcing of the IT services.**

**Disaster recovery planning**

**4.2.110** Effective business contingency planning ensures that critical business functions are able to continue to operate in the event of a loss of IT facilities and to recover those facilities. A contingency plan should document detailed recovery procedures to quickly and smoothly restore the organisation's processing capabilities in the event the computer or communications facility becomes inoperable or inaccessible.

**4.2.111** The outsourcer has a contractual obligation to have finalised the disaster recovery plan in respect of critical applications (to be specified by VicRoads and the PTC) within 6 months of the contract commencement date and in respect of all other applications within 12 months of the commencement date.



**4.2.112** The audit review revealed the following positive steps:

- Within 6 months of the contract commencement date, VicRoads and the PTC had determined the critical applications and the recovery response times;
- A "mock" disaster recovery test was successfully completed by the outsourcer for VicRoads. Applications/systems were recovered from Ballarat to the outsourcer's site in Melbourne; and
- PTC has documented responsibilities and procedures for critical applications.

**4.2.113** Notwithstanding the above, there is currently no formally documented disaster recovery plan in place between the outsourcer and VicRoads. Further, the PTC, while possessing a documented disaster plan, has not tested the documented procedures and formal test plans have not been developed or agreed upon.

**4.2.114** Management has advised audit that processes are in progress to devise a comprehensive disaster recovery plan for VicRoads and a disaster recovery test plan for the PTC. The 2 tasks have been allocated a high priority to ensure the disaster recovery plans are in place, regularly tested and updated with changes.

## CONTRACT MIGRATION

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**4.2.115** With the contract in its second of 5 years it is understandable that no action has been initiated to date. The new outsourcing guidelines provide clear direction on the action required including the effective planning and management through the conclusion of the outsourcing contract and the implementation of arrangements for future service delivery. It is important that the PTC and VicRoads undertake an evaluation of all options, namely;

- retention of existing outsourcer;
- selection of alternative service provider; and
- migration to in-house services

## FUTURE DIRECTIONS

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**4.2.116** At this stage it is my intention that after a sufficient lead time has elapsed, my Office will conduct a major Statewide audit of the management of outsourcing across the public sector utilising the Government's Outsourcing and Contract Management Guidelines as a major reference.

# Part 4.3

## Financial accountability in the Victorian public sector

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### KEY FINDINGS

#### Implementation of accrual accounting in departments

- It is the aim of the Government that departments have in place integrated financial management information systems which will accommodate both cash and accrual recording and reporting requirements. This will enable departments to prepare both year-end financial statements and internal management reports on an accrual basis and enable meaningful financial analysis to be undertaken on a regular basis which will enhance the financial management and accountability of departments.

*Paras 4.3.11 to 4.3.13 and Para. 4.3.18*

- In the case of the former Department of Conservation and Natural Resources, and the Department of Education, the valuation of significant levels of non-current physical assets has yet to be finalised which will impact upon their capacity to comprehensively report on an accrual basis for the 1995-96 financial year.

*Paras 4.3.4 to 4.3.6 and Para. 4.3.19*

#### Valuation of assets

- The timely finalisation of asset valuations will assist in ensuring that the benefits of introducing accrual accounting are realised, particularly in relation to effective asset management.

*Paras 4.3.20 to 4.3.29*



**KEY FINDINGS - continued**

**Financial reporting issues**

- From a public accountability perspective, consideration needs to be given to enhancing the current reporting requirements to require reporting entities to provide greater disclosure of revenues and expenditures within their financial statements.  
*Paras 4.3.32 to 4.3.34*
- Agencies now have an option as to the method of disclosure to be used for government contributions utilised for capital acquisitions which could lead to inconsistencies in financial reporting and may hinder inter-period and inter-agency comparisons.  
*Paras 4.3.39 to 4.3.42*
- To ensure a uniform approach to the recognition in financial statements of government contributions utilised for asset acquisitions, it is audit's view that either the Parliament should specify the amounts made available for capital purposes or an appropriate administrative framework should be developed for this purpose.  
*Para. 4.3.43*
- The recent changes to the *Financial Management Act* 1994, should result in more timely reporting of audited financial statements to the Parliament.  
*Paras 4.3.45 to 4.3.46*

**Audit committees in the Victorian public sector**

- It is desirable that audit committees within departments consist of a majority of external representatives in order to maintain a reasonable degree of independence and separation from management influence.  
*Paras 4.3.51 to 4.3.53*
- Given that most major public bodies and State-owned companies have now established audit committees, guidance should be issued to all other entities in the Victorian public sector espousing the merits of establishing independent audit committees.  
*Paras 4.3.54 to 4.3.55*





**IMPLEMENTATION OF ACCRUAL ACCOUNTING IN DEPARTMENTS**

**4.3.1** Traditionally, departments prepared their financial statements on a cash accounting basis. While this approach was relatively straight forward, the financial performance of departments could not be adequately evaluated, given that the full cost of services and revenues raised was not readily ascertainable from the cash-based information. In addition, the financial position of these administrative units could not be determined as complete information was not available on the value of assets held, and the liabilities and the other financial commitments outstanding.

**4.3.2** In more recent years, accrual accounting has become the generally accepted method of presenting financial information, given its greater commercial orientation and its advantages over cash accounting in enabling a more accurate determination of each entity's operating performance and financial position, through the recognition of all transactions and balances in the relevant financial period.

**4.3.3** Auditor-General's Reports to the Parliament over a number of years have commented upon the progress that has been made in the adoption of accrual accounting by departments and the role played by the Department of Treasury and Finance in the co-ordination and implementation of accrual accounting.

**Implementation program**

**4.3.4** Given the advantages of accrual accounting, in October 1991, the Department of Treasury and Finance commenced the implementation of accrual accounting for departments within the Victorian public sector. Six departments were initially selected as part of this implementation program and were required to prepare a statement of financial position (balance sheet) for the period ended 30 June 1992. Following an assessment of the outcomes of this pilot program, the Department of Treasury and Finance established a 3 year staged program which provided for all departments to be in a position to prepare accrual financial statements by the 1995-96 financial year, in accordance with the reporting requirements of the *Financial Management Act 1994*, which would be subject to audit.

**4.3.5** The Australian accounting profession has also given recognition to the benefits of accrual accounting for departments by the issue of Australian Accounting Standard AAS 29 *Financial Reporting by Government Departments*. This standard requires that all departments prepare an operating statement, a statement of financial position and a statement of cash flows with accompanying notes by 31 December 1996. The Government has mandated compliance with AAS 29 for all departments.



**4.3.6** For the financial year ended 30 June 1995, all but 3 departments tabled in the Parliament audited accrual-based financial statements. The remaining departments, namely, the former Departments of Business and Employment, and Conservation and Natural Resources, and the Department of Education, with the approval of the Minister for Finance continued to report on a cash basis, but also included **unaudited supplementary accrual financial statements** in their annual reports to the Parliament. **All departments will be required, for the 1995-96 financial year, to prepare accrual financial statements and to have their financial statements audited by my Office.**

**Role played by Department of Treasury and Finance**

**4.3.7** The Department of Treasury and Finance has played an important role in facilitating the introduction of accrual accounting in the Victorian public sector. This has been evidenced by its efforts in providing training and guidance materials to the relevant administrative units and its role in the development of integrated financial management information systems for departments.

*Provision of training and guidance materials*

**4.3.8** The *Accrual Accounting Manual*, which was originally issued in May 1994, was revised in February 1995 to address the concerns relating to compliance with AAS 29 requirements. Audit found that most departments have referred to this manual extensively for guidance in the preparation of their accrual-based financial statements.

**4.3.9** To assist with the ongoing implementation of accrual accounting, the Department of Treasury and Finance has also co-ordinated a series of training courses for staff from other departments during the 1994-95 financial year. Individual departments have now assumed the responsibility for, and have conducted, further ongoing training which has generally been provided by an external consultant.

**4.3.10** The emphasis of training provided by the Department of Treasury and Finance has now shifted to internal management reporting. Over recent months, workshops have been conducted by the Department which have dealt with issues arising from the development of integrated accrual recording and reporting systems and the use of these systems to monitor departmental performance.

*Implementation of accrual-based integrated financial management information systems*

**4.3.11** The major focus to date by departments, in relation to the accrual accounting process, has been to comply with statutory reporting requirements under the Financial Management Act and applicable Accounting Standards. However, internal management reporting continued to be undertaken on a cash basis, and was generally restricted to a comparison of actual receipts and payments against budget projections.



**4.3.12** In the review conducted by audit of the processes adopted by departments for the preparation of accrual-based financial statements for the 1994-95 financial year, it was found that the financial information was generally compiled from spreadsheets devised independently of the financial management information system which continued to be cash-based. In audit view, such a position was unsatisfactory as the full benefit expected from management's use of accrual-based information was not being achieved. Clearly, the introduction of integrated accrual-based management information systems, which provide for regular and comprehensive reporting, would assist in the achievement of this objective.

**4.3.13** In recognition of the above shortcoming, departments are in the process of introducing enhanced management information systems. The former Department of Planning and Development, and the Departments of Justice, Treasury and Finance, and Education (Directorate of School Education) have implemented common integrated information systems. A number of other departments are in the process of implementing similar systems in 1996. It is vital that progress towards full implementation of these systems be achieved as soon as possible, to attain the full benefits to management of accrual accounting.

*Accounting skills*

**4.3.14** In the review of the preparation of the accrual-based financial statements for the 1994-95 financial year, audit found that, in certain cases, accounting staff within departments experienced some difficulties in the preparation of those statements, mainly in relation to:

- recognition and valuation of non-current physical assets;
- distinguishing between transactions which are the responsibility of departments and those which are undertaken on behalf of the Government;
- accounting for employee leave entitlements; and
- accounting to trust funds.

**4.3.15** A survey on the implementation of accrual accounting by departments was conducted by the Department of Treasury and Finance in mid-1995. The results of the survey revealed that, while senior and middle level accounting positions within departments were occupied by qualified accountants, many of these staff have only had experience with cash recording and reporting, and minimal exposure to accrual accounting.

**4.3.16** The survey highlighted the need for the Department of Treasury and Finance to provide guidance and assistance to departments. To this end, workshops and meetings co-ordinated by the Department of Treasury and Finance have provided a forum for staff from the participating departments to discuss issues and raise matters of concern which relate to the accrual accounting process. In addition, the Department of Treasury and Finance has introduced a number of other initiatives directed at providing technical and other support to departments, including the conduct of regular finance manager meetings and the enhancement of graduate recruitment and training.



**4.3.17** Clearly, the role of financial staff within the public sector has substantially changed from purely financial recording and reporting to a range of inter-related functions encompassing budgetary control, financial analysis, performance measurement and management accounting activities. Therefore, training is important to ensure that these staff obtain the required skills and knowledge to perform their expected roles.

**What are the future challenges?**

**4.3.18** It is the aim of the Government that departments have in place integrated financial management information systems which will accommodate both cash and accrual recording and reporting requirements. This will enable departments to prepare both year-end financial statements and internal management reports on an accrual basis and enable meaningful financial analysis to be undertaken on a regular basis which will enhance the financial management and accountability of departments.

**4.3.19** In the case of the former Department of Conservation and Natural Resources, and the Department of Education, the valuation of significant levels of non-current physical assets has yet to be finalised. The ability of these departments to complete independent valuations of their non-current physical assets will impact upon their capacity to comprehensively report on an accrual basis for the 1995-96 financial year.

*□ RESPONSE provided by Deputy Secretary, Accounting and Financial Reporting, Department of Treasury and Finance*

*The implementation of accrual financial reporting in departments has proceeded as planned, with all departments to prepare accrual financial statements for audit as at 30 June 1996. The next step for departments will be to ensure that this form of reporting translates into accrual management reporting, via the implementation of appropriate financial management systems.*

**VALUATION OF ASSETS**

**4.3.20** Previous Auditor-General's Reports to the Parliament, have highlighted the deficiencies which existed in physical asset recording, valuation and management practices in budget sector agencies and recommended that the Department of Treasury and Finance issue comprehensive guidelines in this area.

**4.3.21** Following the introduction of a number of initiatives by the Department, improvement has occurred in this area over the past year. In January 1995, the Department issued a guidance paper entitled *Recognition and Valuation of Non-Current Assets*, which required agencies to undertake valuations of their physical assets by 30 June 1996 and provided direction in relation to the valuation of physical assets for external reporting and insurance purposes.





**4.3.22** Another initiative which complements the above guidance paper was the issue by the Government in November 1995 of a manual entitled *Asset Management Series* which outlines the purpose and fundamental principles of effective asset management in agencies, and provides the strategic framework to implement such principles. This manual also deals with a number of asset management issues, including those relating to the recording, valuation and reporting of physical assets.

**4.3.23** In addition, the Department has also progressed the development of a central asset register covering all departments and budget sector agencies and is seeking to directly link, during the 1996-97 financial year, the register with the recording systems maintained by these agencies. Once established, this interface should enhance the capacity of the Department of Treasury and Finance from a central agency perspective, to maintain up-to-date, relevant and reliable financial information on asset holdings.

**Progress in asset valuations**

**4.3.24** In recent years, action has been taken by individual agencies to address past audit concerns regarding the valuation of their physical assets. Prior to the introduction of the *Financial Management Act 1994*, departments were not accountable for the assets that they controlled. However, with the recent introduction of accrual accounting, departments have taken steps to identify these assets and have them valued. Comments follow on the status of valuations for a number of significant asset groups.

*Arts collections*

**4.3.25** The former Department of Arts, Sport and Tourism provided funding to a number of agencies within its portfolio to enable the valuation of their extensive collections. The agencies to which the funding was made available included the National Gallery of Victoria, the Museum of Victoria, the State Library of Victoria, the Public Records Office, the State Film Centre of Victoria and the Victorian Arts Centre (Performing Arts Museum). These agencies have commenced to value their collections and are expected to complete the task by 30 June 1997.

*Conservation and natural resources*

**4.3.26** During the 1994-95 financial year, the former Department of Conservation and Natural Resources developed various policy documents relating to the valuation of its major asset holdings, including Crown land held for conservation, forestry and recreational purposes. The valuation of these assets is in progress and is expected to be completed by 30 June 1996.

*Primary and secondary schools*

**4.3.27** The Department of Education, through its Directorate of School Education, has responsibility for in excess of 1 700 primary and secondary schools. In its 1994-95 supplementary accrual financial statements, which were not subject to audit, the Department included land and associated school buildings at an estimated written-down value of \$4.3 billion. During the current financial year, the Department has sought to value these assets for inclusion in its 1995-96 accrual-based financial statements, which will be subject to audit. However, at the date of preparation of this Report, independent valuations of these assets had not been completed.

*Road infrastructure*

**4.3.28** Over a number of years, the Roads Corporation of Victoria has been obtaining values for its road infrastructure, covering roads, bridges and traffic facilities, and has included estimates of their value as supplementary information in its annual report. The Corporation intends to finalise the valuation of these assets and include their value in its 1995-96 financial statements.

**4.3.29** As indicated previously, the timely finalisation of asset valuations will assist in ensuring that the benefits of introducing accrual accounting are realised, particularly in relation to effective asset management.

□ *RESPONSE* provided by Deputy Secretary, Accounting and Financial Reporting, Department of Treasury and Finance

*The importance of all departments identifying and appropriately valuing their physical assets, not only for reporting purposes but also for insurance and asset management purposes, is acknowledged.*

**FINANCIAL REPORTING ISSUES**

**4.3.30** Prior to 30 June 1994, financial reporting requirements within the Victorian public sector were prescribed in the *Annual Reporting Act* 1983 and the associated regulations which specifically outlined the form and content of financial statements applicable to the various segments of the public sector.

**4.3.31** The introduction of the *Financial Management Act* 1994 in the 1994-95 financial year represented a fundamental change to the Government's financial reporting framework. In particular, the Ministerial Directions which underpin the Act now only provide general guidance on disclosures to be made in financial statements. These Directions are supplemented by a series of accounting policy bulletins issued by the Department of Treasury and Finance which provide additional guidance on a number of accounting matters, including accounting for employee entitlements, government contributions, unfunded superannuation liabilities and disclosure requirements relating to related party transactions.

**Disclosure requirements**

**4.3.32** Under the *Financial Management Act 1994*, the Ministerial Directions require that the financial statements of departments and public bodies, *inter alia*, to:

- be prepared on an accrual basis;
- comply with Australian Accounting Standards and other relevant professional pronouncements; and
- comply with accounting policy bulletins released from time-to-time by the Department of Treasury and Finance.

**4.3.33** While agencies have continued to prepare their financial statements in a form consistent with that required by the former regulations under the *Annual Reporting Act 1983*, due to the reduced disclosure requirements under the Ministerial Directions, much less detail may be provided in financial statements in the future which could lead to a diminished level of accountability to the Parliament. The major area of concern is in relation to the level of disclosure in agency operating statements. By way of example, under the former regulations, major categories of expenditure were required to be disclosed in detail, whereas, under the current reporting requirements, only certain specific expense items such as financing costs, depreciation charges, bad and doubtful debts, audit fees and board members' emoluments are required to be disclosed in the notes to the financial statements.

**4.3.34** From a public accountability perspective, consideration needs to be given to enhancing the current reporting requirements to require reporting entities to provide greater disclosure of revenues and expenditures within their financial statements.

**Issues arising in 1994-95**

*Related party transactions*

**4.3.35** In the May 1994 Auditor-General's *Report on Ministerial Portfolios*, comment was made on the need for major public sector entities to disclose related party transactions, in a similar fashion to the corporate sector. It is pleasing to note that the Ministerial Directions under the *Financial Management Act 1994* now require various disclosures within financial reports of departments and public bodies in respect of related party transactions.

*Unfunded superannuation liabilities*

**4.3.36** In relation to accounting for superannuation in the financial statements of employing agencies, audit has consistently held the view that it is appropriate for such agencies to recognise the full extent of the liability which has accrued in respect of their employees. This view has been based on the principle that, as the benefits derived from employees' services are realised by the employer agencies, the progressive increment in the liability for superannuation entitlements resulting from the services rendered should be recognised in the financial statements of employing agencies.

**4.3.37** In previous years, individual budget sector agencies generally disclosed in the notes to their financial statements their portion of the unfunded superannuation liability as determined by the respective superannuation funds.



**4.3.38** However, for the 1994-95 financial year, the Department of Treasury and Finance recognised in its financial statements the aggregate unfunded superannuation liability for certain superannuation funds. These funds included the State Superannuation Fund, Emergency Superannuation Fund, State Employees Retirement Benefits Fund, Parliamentary Contributory Superannuation Fund, Hospitals Superannuation Fund and Transport Superannuation Fund. As a consequence, individual agencies generally did not disclose their portion of the unfunded liability in the notes to their financial statements.

*Accounting for government capital contributions*

**4.3.39** The issue of accounting for government contributions used for capital acquisitions has generated debate over a number of years. It has been audit's consistent view that such contributions should be disclosed as contributed capital, on the basis that these amounts represent the State's equity in the public bodies receiving the contributions.

**4.3.40** Prior to 30 June 1994, the regulations under the Annual Reporting Act required that any government contributions which were applied for capital purposes were required to be disclosed as contributed capital in the balance sheet of the recipient entity.

**4.3.41** During the 1994-95 financial year, the Department of Treasury and Finance changed the reporting requirements and required agencies to account for government contributions used for asset acquisitions as revenue in the agencies' operating statements. However, agencies are permitted to disclose these contributions as contributed capital if approval is obtained from the Minister responsible for the agency after consultation with the Minister for Finance.

**4.3.42** **Audit has expressed concern to the Department of Treasury and Finance in relation to its required approach which could lead to inconsistent disclosures between individual financial periods and agencies, and may hinder inter-period and inter-agency comparisons.** The impact of the changed reporting requirements is illustrated by the following example:

*During the 1994-95 financial year, the Public Transport Corporation showed an operating deficit before abnormal items of \$62.5 million, compared with \$204.7 million in the previous year. While the Corporation's financial statements appear to indicate an improved operating result for the 1994-95 financial year, this result was determined after recognising \$173.2 million of government contributions utilised for capital purposes as revenue. Had this amount been treated in a consistent manner to that of the previous year, the financial statements would have disclosed an operating deficit before abnormal items of \$235.7 million, representing a deterioration in the operating result from the previous year.*



**4.3.43** Given that agencies now have an option as to the method of disclosure to be used for such contributions which could lead to inconsistencies in financial reporting, it is my view that either the Parliament should specify the amounts made available for capital purposes or an administrative framework should be developed which will result in a uniform approach to the recognition in financial statements of government contributions utilised for asset acquisitions.

*Qualified audit reports*

**4.3.44** Over a number of years, the Auditor-General's Reports to the Parliament have made reference to the proliferation of audit qualifications issued in respect of the financial statements of various public sector entities. In the past, the majority of audit qualifications had been issued as a result of inadequacies associated with asset recording and valuation as well as other related issues. **It is pleasing to report that the number of audit qualifications in this area has significantly diminished over the last 2 years.**

**Expected improvements in the timeliness of financial reporting**

**4.3.45** Under the former *Annual Reporting Act 1983*, public sector agencies were provided with a period of up to 4 months after their balance date in which to finalise their financial reports.

**4.3.46** With the recent changes to the *Financial Management Act 1994*, the timetable has changed markedly. In particular, all entities reporting under the Act are required, in respect of financial years ending on 30 June 1996 and thereafter, to submit financial statements to audit within 8 weeks after balance date. In turn, my Office is required to provide an opinion on those financial statements within 4 weeks of their receipt. **This initiative should result in more timely reporting of audited financial statements to the Parliament.**

*□ RESPONSE provided by Deputy Secretary, Accounting and Financial Reporting, Department of Treasury and Finance*

*The policy of the current Government is to adopt commercial principles. Accordingly, the Financial Management Act 1994, has been established upon a commercial reporting basis, with less emphasis on prescription than its predecessor, the Annual Reporting Act 1983.*

*Whereas the previous legislation was somewhat "bureaucratic" in relation to disclosure requirements, the current legislation allows, and indeed requires, preparers of public sector financial statements to exercise professional judgement regarding the need for separate disclosure of most individual items of revenue and expense.*

*The Department of Treasury and Finance is endeavouring to develop an appropriate solution to accounting for government capital contributions, balanced between the 2 extreme views which exist on this issue.*





## AUDIT COMMITTEES IN THE VICTORIAN PUBLIC SECTOR

**4.3.47** The Auditor-General's May 1994 *Report on Ministerial Portfolios* commented upon the initiatives taken by the Government to recognise the importance of the role and function of audit committees within the Victorian public sector. At the time of that Report, most major public bodies had been pro-active in establishing audit committees and the Government had mandated the establishment of audit committees in departments.

**4.3.48** It is readily accepted, in both the private and public sectors, that audit committees play an important role in enhancing financial accountability and in monitoring the performance of entities. Ideally, audit committees should consist mainly of non-executive and external members, and be capable of providing high level objective advice on the adequacy of internal control systems, internal audit matters and external reporting issues. More specifically, audit committees assist boards of management fulfil their responsibilities by providing them with a mechanism to better consider accounting and auditing issues, promote improved communication with external auditors, and strengthen the credibility of financial information.

### Extent to which audit committees have been established in the Victorian public sector

**4.3.49** A review of the role and composition of audit committees within government departments, major public bodies and State-owned companies revealed that:

- all government departments and most major public bodies had established audit committees within the past 5 years;
- audit committees generally comprise 3 to 5 members, with meetings held on a regular basis;
- there were very few external representatives on audit committees established by departments;
- membership of audit committees established by major public bodies and State-owned companies consisted mainly of non-executive or external members;
- there was a range of skills and knowledge held by audit committee members, primarily in the fields of general business, accounting and auditing; and
- most audit committees functioned in accordance with formally approved charters, which outlined their duties and responsibilities.

**4.3.50** Audit found that many smaller public bodies and State-owned companies had not established separate audit committees, with many of the functions of an audit committee being directly performed by the board of management. In some cases, where a specific audit committee has not been established, the overview function had been combined with the responsibilities of a finance committee.

**Need to enhance independence of departmental audit committees**

**4.3.51** The *Ministerial Directions* supporting the *Financial Management Act 1994* require the accountable officer of a government department to maintain "...an audit committee to oversee and advise him or her on matters of accountability and internal control affecting the operations of the department...". The Directions indicate that the appointment of external experts to the audit committee of a department is considered to be advantageous and that non-departmental persons are highly desirable as members of such committees as they are not involved in the day-to-day operations of the department and bring to the committee additional skills, an independent viewpoint and the ability to ask objective and incisive questions.

**4.3.52** The review found that, while all departments have complied with the requirement to establish audit committees, they predominantly comprised the executive management of the department, with only minimal representation by appropriately qualified external persons. This position contrasts with the practice in the private sector, and with most major public bodies, where membership of audit committees consists predominantly of independent non-executive and external persons.

**4.3.53** **It is desirable that audit committees within departments consist of a majority of external representatives in order to maintain a reasonable degree of independence and separation from management influence.**

**Requirement for public bodies and State-owned companies to establish audit committees**

**4.3.54** While there is a requirement, under the *Ministerial Directions* supporting the *Financial Management Act 1994*, for departments to establish audit committees, no such legislative requirement exists for public bodies and State-owned companies.

**4.3.55** Given that most major public bodies and State-owned companies have now established audit committees, the advantages of these committees should be brought to the attention of all other entities in the Victorian public sector. **It is therefore desirable that further guidance be provided to entities espousing the merits of establishing independent audit committees.**

*□ RESPONSE provided by Deputy Secretary, Accounting and Financial Reporting, Department of Treasury and Finance*

*The need to promote and maintain the independence of audit committees is acknowledged.*

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