

VICTORIA

Auditor-General
of Victoria

**REPORT ON
MINISTERIAL
PORTFOLIOS
MAY 1998**

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May 1998

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.

This Report completes the cycle of my auditing activities in relation to the 1996-97 financial year.

Yours faithfully

C.A. BARAGWANATH
Auditor-General

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Foreword

A diverse range of public interest issues identified from the annual financial audit process of the numerous public sector agencies which come under my responsibility are subjected to additional audit work culminating in this annual Report to the Parliament on Ministerial Portfolios.

As a result of the enactment of the *Audit (Amendment) Act 1997*, I am required to appoint “authorised persons”, following a process of contestability, to assist me in my financial audit responsibilities. As I remain the principal auditor of all Victorian public sector agencies, which total around 520, my Office will be required to undertake quality assurance reviews of the work undertaken by appointed “authorised persons”, in order to comply with Australian Auditing Standards, before I issue the audit opinions on agencies’ financial statements and issue the related audit reports.

Under the new legislation, my Office will continue to be responsible for undertaking the additional audit work required to enable the preparation of my 2 annual audit reports to the Parliament, namely, the *Report on Ministerial Portfolios* and the *Report on the Government’s Annual Financial Statement*.

I am currently finalising the determination of the appropriate resources to enable me to fulfil these responsibilities which emanate from the financial audit process, together with the resources to fulfil my performance audit responsibilities.

The effectiveness of the new audit regime will be largely dependent on the quality of the input received from the various audit service providers, including Audit Victoria. The challenge for my Office will be to ensure that the public interest continues to be protected through the ongoing issue of high quality Auditor-General’s Reports to the Parliament and the community.

C.A. BARAGWANATH
Auditor-General

May 1998

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Legislative Council
Parliament House
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Part 1



Executive Summary



Part 1.1

Major findings

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.

EDUCATION	Page 19
Maintenance backlog at schools	
<ul style="list-style-type: none">• The most recent assessment of the level of maintenance backlog in schools across the State indicates the need for expenditure of \$275.4 million over a 5 year period. Audit examination identified certain instances where maintenance requirements were underestimated indicating a need to critically reassess the maintenance requirements of schools and the associated funding implications. <i>Paras 3.1.4 to 3.1.5 and Paras 3.1.29 to 3.1.37</i>• In relation to the Williamstown North Primary School, maintenance requirements were significantly underestimated as the School was closed on account of health and safety factors, including unsafe classrooms and significant structural damage, within a year of its maintenance requirements being assessed at only \$512 000. <i>Paras 3.1.32 to 3.1.37</i>• The Department of Education has currently allocated, through school global budgets, funding which will only meet 55 per cent of the identified maintenance rated as urgent and required to be undertaken in the 1997-98 financial year. <i>Paras 3.1.9 to 3.1.14</i>• Seventy-nine per cent of schools surveyed by audit supplemented the funding received from the Department with locally-raised funds or locally-provided labour to undertake urgent and ongoing maintenance. <i>Paras 3.1.15 to 3.1.20</i>	



EDUCATION - <i>continued</i>	Page 19
Capital expenditure and asset management at Swinburne University of Technology	
<ul style="list-style-type: none">• The University's Mooroolbark campus commenced operations in 1992 and continued until 1996 when its Lilydale campus was opened. The full financial impact of the University's decision to invest in the Mooroolbark campus at a cost of around \$5.2 million, which was only utilised for 5 years, will not be determined until the property is sold. <i>Paras 3.1.57 to 3.1.70</i>	
Development of university IT systems - The CASMAC project	
<ul style="list-style-type: none">• Universities across Australia in 1991 agreed to develop administrative computing systems (CASMAC). However, in February 1997, a computer application forming part of the project developed by a third party repeatedly failed acceptance testing resulting in the termination of the associated contract and as a consequence the commencement of legal action. <i>Paras 3.1.71 to 3.1.78</i>	

HUMAN SERVICES	Page 51
Department of Human Services tendering procedures	
<ul style="list-style-type: none">• Departmental procedures do not require that a business case be developed when considering the outsourcing of functions or activities and therefore the Department is not in a position to determine whether the most cost-efficient and effective option has been selected for the provision of services. <i>Paras 3.2.14 to 3.2.15</i>• Audit examination identified instances where there was no documentary evidence to substantiate whether goods and services had been provided in accordance with the contract specifications nor was there any analysis of the quality of service provision by contractors. <i>Paras 3.2.18 to 3.2.22</i>	
Management of Residents' Amenities Funds	
<ul style="list-style-type: none">• Audit identified that Residents' Amenities Funds were not only used to acquire goods and services for the use of residents but were also used to fund the normal operating activities of institutions. <i>Paras 3.2.30 to 3.2.31</i>	



INFRASTRUCTURE**Page 75****Privatisation of bus services**

- The Government's Service Agreement with the National Bus Company was extended for more than 6 years without being subject to competitive tendering and is likely to result in a decrease in future savings to be achieved by the arrangement.

Paras 3.3.18 to 3.3.27

- The Department of Infrastructure advised that it now considers the punctuality target level to be unreasonable and intends amending the private bus Service Agreement to lower the target levels.

*Paras 3.3.28 to 3.3.30***Public transport revenue and patronage levels**

- An analysis of metropolitan rail patronage levels which assists in monitoring fare evasion was not possible due to the removal of passenger counters pending the installation and operation of the automated ticketing system.

*Paras 3.3.35 to 3.3.40***Docklands redevelopment arrangements**

- During December 1997, the Mirvac Group was announced as the successful developer for the Yarra Waters precinct of the Docklands redevelopment. However, the Mirvac Group has the option of not proceeding with individual stages of the Development where there is insufficient market demand, or it is not viable to do so.

Paras 3.3.52 to 3.3.54 and Paras.3.3.87 to 3.3.89

- In determining the preferred developers, the Docklands Authority decided not to assign any weighting to its evaluation criteria to signify the relative importance of the various criteria which would have provided greater objectivity and transparency in the evaluation process.

*Paras 3.3.70 to 3.3.73***Operation of audit committees and internal audit within the local government sector**

- The use of audit committees and internal audit has not been universally adopted across the local government sector and, as a consequence, corporate governance within the sector has not achieved best practice.

*Paras 3.3.110 to 3.3.123***Management of municipal business undertakings**

- Of the \$1.4 billion of municipal services subjected to market testing, approximately one-third are provided by council in-house provider teams.

Paras 3.3.124 to 3.3.128



Management of municipal business undertakings - continued

- In response to an audit survey, 12 councils with contract expenditure in excess of \$68 million were unable to identify the surpluses or losses generated during the 1996-97 financial year from their business unit operations. This management deficiency may expose ratepayer's funds to risk, particularly where such units provide services external to the council.

Paras 3.3.136 to 3.3.141

- Fifty per cent of councils who responded to an audit survey indicated that profits of council business units were shared with employees.

Paras 3.3.145 to 3.3.149

Poor tender specifications

- The Macedon Ranges Shire Council awarded a contract relating to road maintenance services valued at \$5.2 million to a third party, commencing from January 1997. However, the terms and conditions of the contract have been subjected to differing interpretations by the contractor and the Council due to a lack of clarity of the contractual obligations of both parties.

Paras 3.3.152 to 3.3.173

- During February 1998, a Deed of Amendment was entered into by the parties clarifying various provisions of the initial contract and incorporating a variation to the contract totalling \$620 000 to enhance the level of service provided for unsealed roads.

Paras 3.3.155 to 3.3.176

Competitive tendering arrangements at the City of Greater Dandenong

- Notwithstanding the City of Greater Dandenong's tender evaluation panel's recommendation to award the contracts for maintenance of horticultural, parks and sports facilities to an external provider, councillors formally resolved to award the contracts to the in-house provider.

Paras 3.3.177 to 3.3.189

- In December 1997, a writ was lodged in the Victorian Supreme Court on behalf of the external provider seeking damages against the Council in excess of \$1.5 million.

Paras 3.3.177 to 3.3.191



Community-based orders by courts

- There was 6 000 community correction orders during 1996-97 representing a 3 per cent increase over the previous financial year. However, 27 per cent of these orders were revoked or breached.

Paras 3.4.10 to 3.4.12 and Paras 3.4.22 to 3.4.24

- The effectiveness of the administration of community correction orders could be improved by greater care being taken to ensure that assessments to support the allocation of offenders to appropriate projects are adequately documented and there is effective monitoring of offenders' progress in meeting the requirements of the orders.

Paras 3.4.13 to 3.4.21

Management of infant investment trust accounts by courts

- An important element of the responsibilities of the respective judiciaries is the management of funds paid into the courts as a result of legal judgements and held in trust on behalf of persons under the age of 18 years or those who have a legal disability. At 30 June 1997, around \$318 million was held in trust funds by the State's major judicial institutions.

Paras 3.4.30 to 3.4.34

- Investment system enhancements should be implemented at the County Court and the Victims of Crime Assistance Tribunal to enable the regular production of transaction statements to trust fund beneficiaries.

Paras 3.4.35 to 3.4.39

Collection of fines and fees

- At 30 June 1997, \$324.5 million of fines, which were legally payable, were outstanding representing an increase of \$53.5 million (20 per cent) since the 1994-95 financial year.

Paras 3.4.40 to 3.4.47 and Paras 3.4.60 to 3.4.63

- The *Magistrates Court (Amendment) Act* 1996 was passed by the Parliament which resulted in debts of \$112 million no longer being legally collectable.

Paras 3.4.66 to 3.4.69

Charging for police services

- The Police (Charges) Regulations 1992 provide the legislative authority for Victoria Police to charge for services provided at sporting and other events, however the Regulations currently inhibit the recovery of the full cost of providing these services.

Paras 3.4.81 to 3.4.88

- Audit found significant delays in the raising of accounts for Police services at a substantial number of events and identified delays in the approval of applications for the waiving of Police charges for certain events.

Paras 3.4.89 to 3.4.90 and Paras 3.4.77 to 3.4.80

Restructuring of water authorities

- Only 57 per cent of the population supplied by non-metropolitan water authorities received water that met the guidelines for microbiological quality. Of particular concern was that one-third of water that was treated did not meet the guidelines.

Paras 3.5.32 to 3.5.37

- The estimated cost associated with raising the quality of water to a standard consistent with the guidelines was in the order of \$288 million.

Paras 3.5.32 to 3.5.37

- Only 13 per cent of wastewater treatment plants operated by non-metropolitan water authorities fully met the Environment Protection Authority (EPA) Standards outlined in their licence agreements for the discharge of treated wastewater into waterways.

Paras 3.5.41 to 3.5.47

- The cost of upgrading non-metropolitan water authorities wastewater treatment plants to comply with their licensing agreements with the EPA has been estimated to be in the order of \$167 million.

Paras 3.5.41 to 3.5.47

Victorian Dairy Industry Authority Chinese joint venture

- The Victorian Dairy Industry Authority's share of the estimated losses in a joint venture in China to 30 June 1998 is expected to be \$564 000, with the joint venture costing the Authority in excess of \$1.2 million.

Paras 3.5.51 to 3.5.58

- The Authority did not incorporate a provision within the agreement to ensure that a pre-determined percentage of Victoria market milk and dairy products would be exported to China for utilisation by the joint venture. As a result, the Authority created the potential for its participation in the joint venture to be ultra vires.

Paras 3.5.62 to 3.5.67

Milk marketing

- The establishment of Australian Milk Marketing Pty Ltd (AMM) has created the situation where the Victorian Dairy Industry Authority has effectively relinquished control over its marketing function. The Authority's actions in forgoing its interest in AMM for nil consideration has resulted in a loss to the Authority of at least \$285 000.

Paras 3.5.68 to 3.5.80

PREMIER AND CABINET**Page 203****Administration of the Community Support Fund**

- Aggregate revenue from the commencement of the Community Support Fund in July 1992 to February 1998 totalled \$326 million, with weekly revenue of the Fund from gaming activities now reaching around \$1.8 million. *Para. 3.6.8*
- As at February 1998, distributions from the Fund totalling \$322 million had been approved, with actual cash payments totalling \$169 million. *Paras 3.6.9 to 3.6.10*

STATE DEVELOPMENT**Page 213****The year 2000 Issue - The Millennium Bug**

- None of the entities examined by audit are currently year 2000 compliant. As certain entities examined were yet to begin replacing or converting non-compliant systems and other equipment, these entities face the risk that their businesses may be detrimentally affected by non-compliant systems. *Paras 3.7.11 to 3.7.14*

TREASURY AND FINANCE**Page 235****Clearance of Yallourn Power Station site**

- The potential cost to the State for the clearance of the Yallourn Power Station site is estimated at \$44.5 million, but the overall cost may increase by an additional amount of up to \$25.9 million as a result of a statement of claim lodged by the original contractor which was subject to litigation in the Supreme Court. However, a counter claim amounting to \$10.7 million has been lodged by the SECV. *Paras 3.8.39 to 3.8.40*

Trends in performance of public sector superannuation funds

- The State's unfunded superannuation liabilities which totalled \$15.6 billion as at 30 June 1997 represent the largest component of the State's liabilities after State debt. *Paras 3.8.47 to 3.8.53*
- An important element of the Government superannuation reforms was the modification of benefits available to employees with the closure of defined benefits schemes to new entrants and the establishment of accumulation schemes. Notwithstanding the Government reforms, defined benefit schemes have been retained for operational emergency services employees, judges, senior law officers and parliamentarians. *Paras 3.8.63 to 3.8.67*



Local Authority Superannuation Board unfunded superannuation liability

- While the Local Authorities Superannuation Board's (LASB) unfunded superannuation liability increased significantly during the 1995-96 financial year, the liability slightly declined during the 1996-97 financial year due to unusually high investment returns achieved during the year as a result of the favourable prevailing investment market.
Paras 3.8.82 to 3.8.83 and 3.8.90

Financial standing of WorkCover

- The percentage of the WorkCover Scheme's net assets in relation to its outstanding claims liability has decreased from 102.9 per cent at 30 June 1995 to 92.4 per cent (deficit of \$292 million) at 31 December 1997.
Para. 3.8.95
- The key factors contributing to the reduced funding level of the WorkCover Scheme as at 31 December 1997 was a cumulative increase of \$1.2 billion, or 50 per cent, in the Scheme's outstanding claims liability since 30 June 1995 without the same corresponding increase in net assets.
Para. 3.8.96

Utilisation of government property

- The average space allocation per public servant remains excessive based on the target established by the Government.
Paras 3.8.128 to 3.8.131
- There has been a significant improvement in the level of dead rent which is estimated at \$6.8 million for the 18 month period to December 1997 compared with \$12 million for the same period to December 1995.
Paras 3.8.136 to 3.8.137

Victorian electricity industry privatisation

- PowerNet Victoria's revenues are substantially secured, with the company currently deriving in excess of 95 per cent of its total revenues from its regulated transmission business.
Paras 3.8.146 to 3.8.147
- The total proceeds of \$2.7 billion received from the sale of PowerNet Victoria compared favourably with valuations obtained prior to the sale and was \$1.2 billion in excess of the book value of the business.
Paras 3.8.159 to 3.8.161
- The State obtained total proceeds of \$400 million in relation to the sale of Southern Hydro Ltd which compared favourably with valuations obtained prior to the sale and was \$115 million in excess of the book value of the business.
Paras 3.8.182 to 3.8.184
- It is estimated that the State will derive annual net savings of approximately \$760 million during the 1997-98 financial year from the electricity privatisations which have generated proceeds of \$21.7 billion to date.
Paras 3.8.204 to 3.8.206

Part 2



Parliament of Victoria



Part 2.1

Parliament of Victoria

KEY FINDING
<ul style="list-style-type: none">• 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>
COMPLETED AUDITS				
Parliament of Victoria	30 June 1997	No reporting requirements.	15 Sept. 1997	15 Sept. 1997

Part 3



Audit of Ministerial Portfolios



Part 3.1

Education

KEY FINDINGS

Maintenance backlog at schools

- The most recent assessment of the level of maintenance backlog in schools across the State indicates the need for expenditure of \$275.4 million over a 5 year period. *Paras 3.1.4 to 3.1.5*
- Audit examination identified certain instances where maintenance requirements were underestimated and as a consequence the maintenance backlog estimate appears conservative indicating a need to critically reassess the maintenance requirements of schools and the associated funding implications. *Paras 3.1.29 to 3.1.37*
- In relation to the Williamstown North Primary School, maintenance requirements were significantly underestimated as the School was closed on account of health and safety factors, including unsafe classrooms and significant structural damage, within a year of its maintenance requirements being assessed at only \$512 000. *Paras 3.1.32 to 3.1.37*
- For the 1997-98 financial year, the level of funds appropriated to the Department of Education for works and services purposes at schools declined by \$35 million (17 per cent) since the previous financial year. *Paras 3.1.7 to 3.1.8*
- The Department has currently allocated, through school global budgets, funding which will only meet 55 per cent of the identified maintenance rated as urgent and required to be undertaken in the 1997-98 financial year. *Paras 3.1.9 to 3.1.14*





KEY FINDINGS - continued

Maintenance backlog at schools - continued

- Seventy-nine per cent of schools surveyed by audit supplemented the funding received from the Department with locally-raised funds or locally-provided labour to undertake urgent and on-going maintenance.

Paras 3.1.15 to 3.1.20

- Thirty-six per cent of schools surveyed by audit indicated that urgent works accounted for the majority of maintenance money allocated, thereby not providing sufficient funding for preventative or minor maintenance.

Paras 3.1.15 to 3.1.20

Capital expenditure and asset management at Swinburne University of Technology

- Swinburne University's car park and student residence complex at its Hawthorn campus, which was completed in late 1996, has experienced significantly lower operating surpluses than originally projected.

Paras 3.1.50 to 3.1.56

- The University's Mooroolbark campus commenced operations in 1992 and continued until 1996 when its Lilydale campus was opened. The full financial impact of the University's decision to invest in the Mooroolbark campus at a cost of around \$5.2 million, which was only utilised for 5 years, will not be determined until the property is sold.

Paras 3.1.57 to 3.1.70

Development of university IT systems - The CASMAC project

- Universities across Australia in 1991 agreed to develop administrative computing systems (CASMAC) that individual universities could tailor to meet local needs and meet the cost, estimated to be approximately \$11 million for software development and licence fees, and to provide resources in the form of staff time and expertise.

Paras 3.1.71 to 3.1.75

- In February 1997, a computer application forming part of the CASMAC project developed by a third party repeatedly failed acceptance testing resulting in the termination of the associated contract and as a consequence the commencement of legal action in the New South Wales Supreme Court.

Paras 3.1.76 to 3.1.78

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 1996-97.

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

<i>Ministerial portfolio</i>	<i>Entities subject to audit</i>
Education	Board of Studies Telematics Course Development Fund Trust
Tertiary Education and Training	Adult, Community and Further Education Board Council of Adult Education International Training Australia Pty Ltd Post-secondary education institutions - Universities (8) and associated companies, trusts and foundations (48) Colleges/institutes of technical and further education (22) and associated company State Training Board Victorian Tertiary Admission Centre

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 below.

MAINTENANCE BACKLOG AT SCHOOLS

3.1.4 In 1993, the Victorian Commission of Audit identified that there was a significant backlog of maintenance required to school buildings. In particular, the Commission reported that, based on the figures provided by the Department of Education, at least \$620 million of maintenance works were required at government schools. However, this data was outdated and an urgent review to ascertain the actual level of expenditure required for this purpose was recommended.

3.1.5 The Department commenced a review to ascertain the actual level of maintenance backlog in schools in 1994. The most recent assessments of the level of the maintenance backlog indicate the need for expenditure of \$275.4 million over a 5 year period for this purpose.

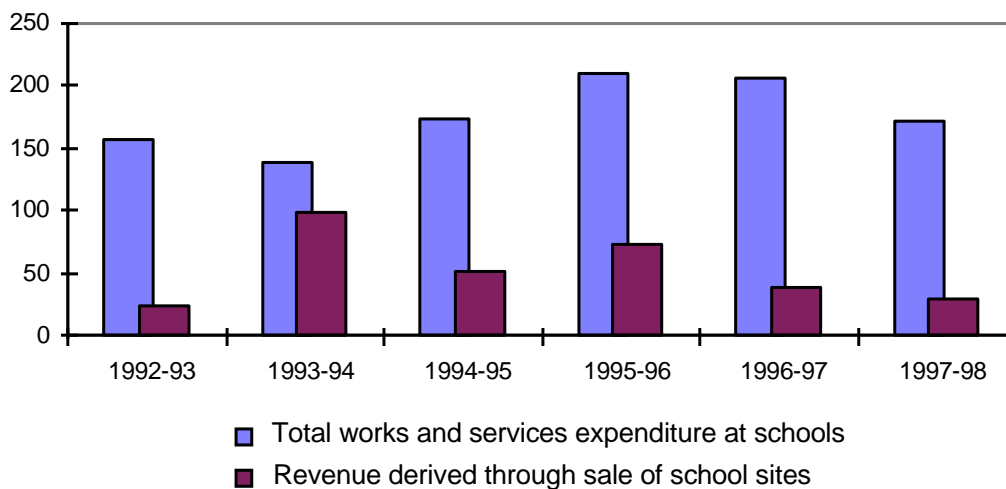


3.1.6 The reduction in the level of the maintenance backlog at schools since 1993 can be attributed in part to:

- a decrease in the number of school sites from approximately 2 000 in 1993 to 1 660 in 1998, with the sale of former school sites netting \$288 million since the 1992-93 financial year; and
- the provision of annual funding to schools by the Department of Education for maintenance and minor works through School Global Budgets and the departmental maintenance program.

3.1.7 Under an agreement between the Department of Treasury and Finance and the Department of Education, the funding generated from the sale of schools’ sites has been made available to the Department of Education through appropriations in the financial year following the sales. This arrangement has contributed to an increase in the total works and services funding made available to schools to undertake major maintenance and upgrades and to fund the establishment of new schools. Chart 3.1B highlights the total works and services funding made available for schools compared with the total level of funding generated from the sale of school sites for the financial years 1992-93 to 1997-98.

CHART 3.1B
WORKS AND SERVICES EXPENDITURE AND REVENUE
FROM THE SALE OF SCHOOL SITES
 (\$million)



3.1.8 The chart indicates that the level of expenditure for works and services purposes at schools has progressively increased up until the 1995-96 financial year and totalled \$207 million in the 1996-97 financial year. **However, for the 1997-98 financial year, the level of funds appropriated to the Department for works and services purposes at schools declined to \$171.6 million, representing a \$35 million (17 per cent) reduction since the previous financial year.** The key reasons provided by the Department for this reduction were:

- timing differences between approval for major projects and actual cash expenditure;
- changing priorities of the Government; and
- decrease in asset sales.

Departmental review of maintenance requirements

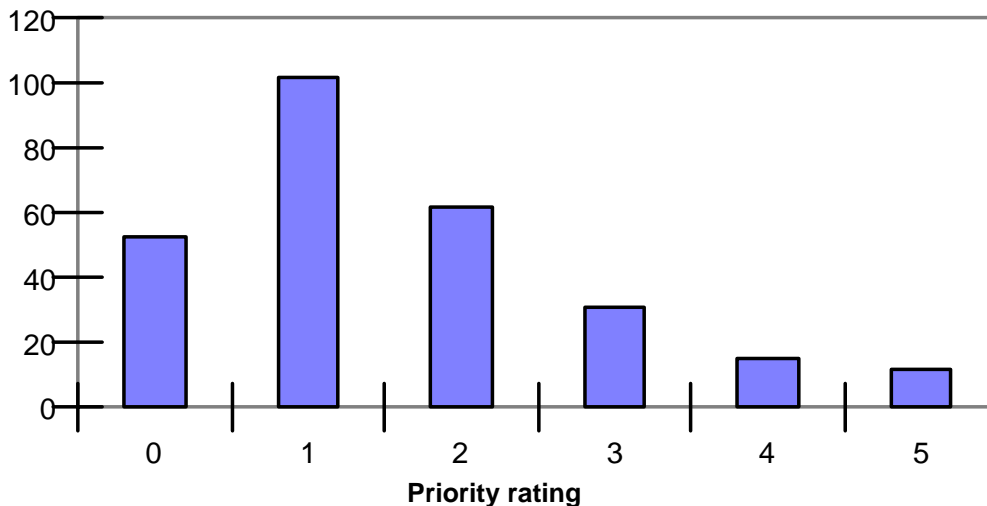
3.1.9 During 1997, independent consultants were engaged by the Department to perform maintenance audits at all schools throughout the State, with the primary objective of establishing a database of information on the condition of all building stock and developing reliable estimates of the current maintenance backlog.

3.1.10 The maintenance audits involved the classification of each room at individual schools. Each component of a room, such as walls, painting, roofs, windows, floor coverings and light fittings, was allocated a rating according to the following scale:

- 0 - Urgent and/or potential health and safety issue requiring immediate attention;
- 1 - Requires attention within 1 year;
- 2 - Requires attention within 2 years;
- 3 - Requires attention within 3 years;
- 4 - Requires attention within 4 years; and
- 5 - Requires attention within 5 years.

3.1.11 This departmental audit process identified aggregate maintenance requirements for schools across the State of \$275.4 million. Chart 3.1C highlights the timing and value of maintenance requirements based on the above rating scales.

**CHART 3.1C
MAINTENANCE BACKLOG BY PRIORITY
(\$million)**



3.1.12 The chart shows that 79 per cent of the backlog in maintenance is required to be undertaken within the next 2 years. Further, 52 per cent of schools require in excess of \$100 000 to fund their maintenance backlog needs.



3.1.13 In the 1997-98 financial year, the Department has currently allocated, through school global budgets, \$29 million to schools to address backlog maintenance priorities. This level of funding represents 10.2 per cent of the total backlog of \$275.4 million and only 55 per cent of the identified maintenance which is rated as urgent and required to be undertaken in the current financial year. However, additional funding provided for refurbishment and upgrades will further reduce the maintenance backlog.

3.1.14 It was further identified that \$37 million of the total assessed maintenance backlog is required to restore portable buildings. While these buildings were assessed during the departmental maintenance audits, schools were instructed by the Department not to spend funds over and above the allocations provided under the schools global budget, pending the results of a major departmental review of portable buildings which is to take place during 1998. Given the high level of maintenance that is required to restore the portable school buildings to an acceptable condition, the planned departmental review should be undertaken as a matter of urgency.

Maintenance funding provided under schools global budgets

3.1.15 The inclusion in school global budgets of maintenance and minor works funding was trialled in the 1991-92 financial year and fully implemented across the State in the 1993-94 financial year to give schools greater control over the application of funds for maintenance and minor works to ensure that local priorities are best addressed. Such funds are required to be used by schools to address:

- urgent works resulting from, inter alia, storm damage, vandalism and fire;
- maintenance of internal and external buildings materials;
- upgrading school facilities; and
- adapting facilities to meet current curriculum requirements.

3.1.16 The maintenance and minor works funding component of the school global budgets (which is an element of the works and services expenditure as highlighted in Chart 3.1B) is based on a formula developed in 1989 through a series of working parties and is based on the following 3 factors:

- 50 per cent of the allocation is based on the building area entitlement of the school given its current enrolment numbers as a proportion of the total entitlement for all schools in the State;
- 25 per cent of the allocation is based on building type to take account of the rate of deterioration of differing types of construction and building materials; and
- 25 per cent of the allocation is based on the time elapsed since the last major maintenance program was conducted at the school which recognises that a school will have higher maintenance and minor works needs where it has not been the subject of a major upgrade for some time.

3.1.17 The factors outlined above are then multiplied by a locality factor which seeks to compensate schools located in areas where there is a lack of trade services and competition which contribute to higher costs.

3.1.18 Although the formula takes account of the major factors which drive the level of maintenance requirements at schools, the following issues were identified by audit in relation to the funding formula:

- The locality factor built into the funding formula provides more remote country areas with funding supplementation of up to 22 per cent compared with metropolitan areas. The Department has advised that it has recently undertaken a review of the locality factors to ensure that they more accurately reflect the current demographic and population position. These revised locality factors are anticipated to be applied to the 1999 school global budgets; and
- Where a school holds buildings in excess of its assessed requirements based on enrolment levels, the funding formula in part only provides schools with funds based on its assessed requirements. While it could be argued that this funding process is in accordance with sound asset management principles, in practice it may result in anomalies where schools experience fluctuations in enrolments but hold and utilise pre-existing buildings such as libraries and gymnasiums which are larger than notional entitlement, but still require maintenance. In addition, classrooms and other areas in excess of entitlement must still be maintained to a minimum health and safety standard. Given that the Department currently has 352 campuses deemed to hold building areas in excess of entitlement by 30 per cent, the impact of this issue is significant.

3.1.19 Furthermore, an audit review of a random sample of schools in receipt of the school global budget funding indicated that:

- only 7 per cent of the schools considered that funding provided for maintenance was sufficient to maintain the school in an acceptable condition;
- 79 per cent of schools supplemented their funding with locally-raised funds or locally-provided labour to undertake urgent and on-going maintenance; and
- 36 per cent of schools indicated that urgent works accounted for the majority of maintenance money allocated, thereby not providing sufficient funding for preventative or minor maintenance.

3.1.20 **There is a need for the Department to continually reassess the formula utilised to determine funding allocations to schools for maintenance and minor works to ensure that there is an equitable distribution of funds and that minimum health and safety standards are maintained.**

Physical Resource Management System

3.1.21 At the date of preparation of this Report, the Department was in the final stages of implementing a new computer system designed to provide up-to-date information which would allow schools and the Department to monitor the level of outstanding maintenance on an ongoing basis.



3.1.22 The computer-based management information system known as Physical Resource Management System (PRMS) was designed by the Department to provide a comprehensive record of the current physical condition of each school in Victoria through the recording, rating and assessment of all school buildings, and to provide a means for schools to monitor works projects and undertake maintenance planning. The system is the primary record used by the Department to assess the current level of maintenance backlog and to plan future strategic directions for funding.

3.1.23 The design and implementation of the system was commenced in 1994 and external specialist participation was required to address the key tasks of developing the software, undertaking a room-by-room assessment of the physical condition of all school buildings and the training of staff at 1 660 schools throughout the State in the operation of the system. The Department called tenders in December 1994 to cover these 3 major areas, and a further tender was called for the engagement of a contractor to provide for project management services to oversee and co-ordinate all facets of the project. **However, contracts relating to the provision of these services were not formalised until October 1996, which delayed the development and implementation of the PRMS for almost 2 years.**

3.1.24 Furthermore, the training provided in relation to the PRMS was significantly effected by the delays in the software development and, as a consequence, **the contractor successfully recovered \$82 000 in damages from the Department which was not in turn recovered from the software developer.**

3.1.25 As only minimal PRMS training was initially provided, schools were not in a position to fully realise the benefits available from utilisation of the system. In particular, schools were unable to print reports or list information to determine priorities, and there was a lack of understanding of the types of reports available and their contents.

3.1.26 As part of the verification process for data maintained on the system, during 1997 individual schools were required to review the data and notify the Department of any concern. Where no response was received from schools and after each school was individually contacted by the Department, it was assumed that the assessed maintenance needs reported on the system were accepted by the school.

3.1.27 However, audit discussions with selected school principals determined that most were unaware of this requirement with only 14 per cent of schools requesting that their maintenance needs be reassessed.

3.1.28 Stage 2 of the PRMS encompassing the final portion of the software, the computer-based training package and reissued guidelines on the procedures for maintenance grants is anticipated to be delivered to schools in 1998. This will complete the implementation and training for the system and it is envisaged by the Department that additional training will be provided on a needs basis.

Accuracy of maintenance backlog estimates

3.1.29 During the examination of the PRMS records at schools, a number of inconsistencies were identified between the maintenance requirements recorded on the system and subsequent expenditure for maintenance purposes. This was illustrated at a school which was assessed as having total maintenance of \$76 000, however, subsequently the school expended \$195 000 refurbishing its main building, with both the toilet block and portables which required backlog maintenance excluded from the works.

3.1.30 In addition, audit identified certain instances where maintenance requirements may have been underestimated for older schools which had unique needs associated with old drainage and sewerage systems. Experience has shown that the ongoing cost of repairs to these systems has been high, with the costs associated with replacement so significant that they are prohibitive to most schools.

3.1.31 **Given the deficiencies identified, the current maintenance backlog estimate appears conservative indicating a need to critically reassess the maintenance requirements of schools and the associated funding implications.**

Williamstown North Primary School

3.1.32 A representative sample of schools were reviewed by my Office to ascertain their perspective on the level of maintenance required and the adequacy of the information systems used to record the maintenance requirements. Included in the sample was the Williamstown North Primary School, which was the subject of recent departmental action regarding its condition. Detailed below are some observations regarding the school.

3.1.33 The Williamstown North Primary School which was operating at capacity, with an enrolment of 530 students, utilised a building which was established in 1870 together with an additional building which was constructed in 1913. The last major upgrade at the school was performed in the 1983-84 financial year, under which the entire school was refurbished at a cost of \$1.2 million.

3.1.34 A maintenance review of the school was undertaken in March 1997, as part of the backlog maintenance assessments conducted by the Department. As a result of this process, the total maintenance needs of the school were assessed at \$512 000, of which \$239 000 was identified as urgent. The results of the maintenance review, in particular the total maintenance needs of \$512 000, were disputed by the school, however, no second review had been undertaken at the date of our audit.

3.1.35 Subsequent to our audit, the school buildings were closed in March 1998 as a result of a health and safety assessment and structural report commissioned by the school which detailed significant structural damage, making classrooms unsafe. The poor condition of the buildings had been recognised by the school since 1990 and communicated to the Department since that time.



3.1.36 This example illustrates the need for the Department to widen the scope of maintenance audits where it is indicated either by the school or the independent maintenance review that more significant problems exist. A comprehensive review in these instances should include a review of all factors which may provide a complete assessment of not only maintenance but all capital works requirements.



A classroom at Williamstown North Primary school.

3.1.37 The Department plans to adapt the PRMS to identify and manage a cyclical maintenance program for all schools, with independent audits of school condition to be ongoing within a 3 year cycle ensuring a maintenance backlog of significant proportions does not occur in the future. **The key to the successful future management of maintenance requirements hinges on the Departments ability to ensure the ongoing integrity and completeness of maintenance needs recorded on its information systems and the allocation of adequate funding to schools for this purpose.**

RESPONSE provided by Secretary, Department of Education

Maintenance backlog at schools

No mention is made in the Report of the Government's commitment to provide \$1 billion towards capital works in schools during the current term of office or the substantial increases in Works and Services funding, particularly in the 1995-96 and 1996-97 financial years, a substantial portion of which has been devoted to maintenance, in reducing the backlog by some \$345 million in the period 1993-97.

It should also be noted that while the number of school sites has reduced from 2 000 to 1 660 in the years 1993 to 1998, a large number of these were small country primary schools where the maintenance backlog was minimal in comparison with total maintenance requirements of all schools.

The Report also omits to mention that the capital outlays announced for education in 1998-99 represents a substantial increase to approximately \$248 million, a considerable proportion of which will be directed towards maintenance and upgrade works.

□ **RESPONSE** provided by Secretary, Department of Education - continued

Departmental review of maintenance requirements

The Report mentions without quantification that additional funding provided for refurbishment and upgrades will further reduce the maintenance backlog. Clearly, the fact that \$32 million for refurbishment work and \$86 million for construction/upgrade projects was provided in the 1997-98 financial year is very significant in comparison with the \$29 million provided annually to schools for maintenance and minor works. In many cases, the schools involved in these projects will require re-auditing thus reducing the extent of identified backlog.

Maintenance funding provided under school global budgets

This section purports to draw conclusions for all schools but draws on a very small sample survey of 17-20 schools (a one per cent sample). The statistics quoted when compared with the total number of schools (1 700) in the system are misleading and the questions/responses open to interpretation as follows:

- The annual allocation for Maintenance and Minor Works in the school global budget has never been intended to cover all maintenance works associated with the school. Major maintenance funds/refurbishment funds allocated on a priority basis have always supplemented the school global budget allocations; and
- While the Report states that 36 per cent of schools indicated that urgent works accounted for the majority of maintenance money allocated, there is no definition provided as to the nature of these works. The Department believes that on a Statewide basis, approximately 50 per cent of the maintenance funds in the school global budget are spent on urgent works. However, this figure will vary from year to year and from school to school.

The Department acknowledges that there is a need to continually reassess the formula utilised to determine funding allocations to schools for maintenance and minor works and will be utilising the audit data associated with PRMS for this purpose.

Physical Resource Management System

The summary result that only 14 per cent of schools requested that maintenance needs be reassessed is totally inaccurate. The actual total number of schools which queried the audit data represented approximately 30 per cent of 1 500 schools which had been provided with the data at the time. The response from the small sample of schools utilised for the survey is clearly not representative of the system-wide response from all schools.

Accuracy of maintenance backlog

The examples quoted in the Report tend to be misleading and require some clarification. The school cited as having total maintenance assessed at \$76 000 and subsequently expended \$195 000 refurbishing its main building was audited prior to the refurbishment works (which entail bringing some of the school facilities up to current standards not maintaining the total school facilities). The school is currently listed for a re-audit now that those works have been completed (December 1997). Additional maintenance funding will only be provided if the re-audit indicates a need for such funds.



□ **RESPONSE** provided by Secretary, Department of Education - continued

Accuracy of maintenance backlog - continued

With regard to the “maintenance requirements associated with older schools and the unique needs associated with old drainage and sewerage systems” this has been recognised with the specific introduction of a construction program to cater for works estimated to cost less than \$100 000. This program is intended to cover a number of unforeseen maintenance projects which without extensive investigation could not have been identified at the time of the PRMS audit (e.g. fire services, sewerage replacements, oil to gas heating conversions).

The Department does not agree that the current maintenance backlog estimate is conservative. The estimates have been prepared by independent building industry experts and represents the best available information at this time.

Williamstown North Primary School

This example represents a unique situation which the Department, following request for re-audit from the school, has extensively followed-up resulting in the closure of the main buildings at the school. It does not represent a typical situation which can be translated to all schools. It should also be noted that while the condition of the building has been recognised and addressed periodically since 1990, the major deterioration of the buildings has occurred in the last 6 months due mainly to the drought as identified in the structural engineer’s reports.

Overall comment

Overall, the Department has made significant achievements in reducing the maintenance backlog by adopting a strategic approach to the management of assets. The development of the Physical Resources Management System is a key feature of this strategic approach.

The System, together with other initiatives such as SAMS, puts the Victorian Department of Education at the leading edge of innovation and improvement in asset management practices. It provides a comprehensive overview of school maintenance requirement across the State and enables the Department to target expenditure to the highest priority areas.



CAPITAL EXPENDITURE AND ASSET MANAGEMENT AT SWINBURNE UNIVERSITY OF TECHNOLOGY

3.1.38 Swinburne University of Technology (Swinburne) is a multi-campus tertiary education institution which has a significant investment in property assets at its 4 campuses which are located at Hawthorn, Prahran, Lilydale and Mooroolbark. As at 31 December 1997 the value of properties held by Swinburne exceeded \$173 million.

3.1.39 In 1989, Swinburne acquired property for the establishment of a campus at Mooroolbark which the University subsequently decided will be discontinued and in 1996 constructed a car park and student residence complex at its Hawthorn campus. This Report outlines the results of an audit review of these asset acquisitions.

Car park and student residence complex

3.1.40 A business plan prepared in September 1992 for Swinburne provided for the conduct of an evaluation of a proposed development of a multi-deck car park at Swinburne's Hawthorn campus, including consideration of available financing options, construction methods and costs.

3.1.41 Subsequently, in early 1993, Swinburne received indicative figures from a number of construction groups with experience in the design and construction of multi-deck car parks within the Melbourne metropolitan region, which indicated that at other universities, user-pay arrangements provided sufficient revenue to initially fund the development of such car park facilities and to meet their ongoing maintenance costs.

3.1.42 However, in June 1993, Swinburne determined not to proceed with the development following a review of the costs associated with similar projects and parking policies at other universities around Australia, which concluded that the costs for the construction of multi-deck car parks were "... *significantly under-estimated and the consequential fee structure for users as a stand-alone, self-funding car park were prohibitive*".

3.1.43 During 1995, due to community and staff pressure, Swinburne reconsidered the need for the construction of a multi-deck car park and the University received proposals from developers for the design and construction of a car park and a student residence complex at its Hawthorn campus, which was to be located on council land.

3.1.44 In late 1995, following an evaluation of tenders, a developer was appointed to undertake the project at a cost of \$9.3 million. However, the local council did not endorse the project which included the use of council land for the development but accepted an alternative proposal from Swinburne for the complex to be constructed wholly on the University's land. **Consequently, the developer revised its earlier proposal, increasing the number of car park spaces and the number of apartments in the student residence, which increased the total development cost from \$9.3 million to \$13.3 million.**



3.1.45 Construction of the car park and student residence complex was subsequently completed in late 1996.



Car park and student residence complex, Hawthorn campus.

3.1.46 The developer’s proposal, which was supported by cash flow projections covering a period of 21 years, indicated that an accumulated positive cash flow of \$19.5 million in 1995 dollar terms would be generated from the operation of the car park and student residences, which represented a 6.95 per cent rate of return for Swinburne.

3.1.47 Given that the nature of this project differed from the traditional “core” activities for the University and introduced significant commercial aspects, it was important that all risks relating to this investment decision be identified and fully assessed by the University. In this regard, audit noted that the cash flow projections were subjected by Swinburne to various scenarios, including reduced income resulting from lower occupancy rates for the hostel and apartments, variations in car park rental, movements in interest rates and increases in the cost of construction.

3.1.48 During the construction period, Swinburne entered into a lease agreement under which the nominated car park operator, as lessee, agreed to bear the costs of all fit-out work required for the car park including the supply and installation of access doors, signage, card readers, space counters, boom gates, other car parking control equipment and an attendant’s office. The lease agreement also outlined the operator’s responsibilities for the daily running of the car park. The lease, which covers a 10 year period extending to the year 2007, provides that a minimum annual rental of \$700 000, subject to a CPI adjustment, payable monthly in advance. The minimum rental is also to be increased in the event that gross receipts exceed the level specified in the agreement. Under the agreement, the car park operator is liable for all outgoings, except for statutory charges relating to the car park and maintenance costs necessary to keep the car park in good condition.

3.1.49 A number of accountability measures have been built into the car park lease agreement, including the requirement for the car park operator to provide regular reports on the level of receipts, which are to be audited on an annual basis. In addition, a Guarantee Indemnity and Acknowledgment Agreement was entered into by the directors of the car park operator in May 1996, as an attachment to the car park lease agreement, which secures the University's position with respect to the receipt of the minimum annual rental payments.

3.1.50 Since the commencement of the car park lease agreement in March 1997, payments from the car park operator have not been made on the due date and the car park operator had sought and obtained approval from Swinburne to make the monthly payments required under the lease in the middle of the month rather than at the beginning of the month as required by the agreement.

3.1.51 Less than 6 months into the operation of the lease, continued delays in monthly payments became unacceptable to Swinburne and, accordingly, arrangements were made as from late August 1997 for Swinburne, rather than the car park operator, to bank moneys collected and to settle on a monthly basis the net amount owing under the lease agreement. Table 3.1D provides a summary of the collections made by Swinburne.

TABLE 3.1D
ANALYSIS OF CAR PARK COLLECTIONS BY SWINBURNE,
SEPTEMBER 1997 TO FEBRUARY 1998
(\$'000)

<i>Month</i>	<i>Lease rental</i>	<i>Receipts</i>
February 1998	58	27
January 1998	58	15
December 1997	58	11
November 1997	58	23
October 1997	58	35
September 1997	58	30
Total	348	141

3.1.52 As indicated in the table, the car park operator has been experiencing difficulties in generating sufficient revenue to meet the minimum rental payable under the car park lease agreement.

3.1.53 In October 1997, Swinburne arranged for the issue of letters of demand to the car park operator and the company's guarantor directors and, subsequently, the University found it necessary to have a creditor's statutory demand issued. This legal action was subsequently withdrawn and amounts outstanding in respect of August, September and October 1997 were received prior to the end of the 1997 calendar year. **However, at the date of preparation of this Report, an amount of \$157 000 was owing to the University in respect of the 4 months covering November 1997 to February 1998.**



3.1.54 While difficulties are being encountered in collecting the car park rental, Swinburne believes that liquidated damages that would arise from the failure of this contract would meet any shortfall in revenue under the car park lease agreement. Nevertheless, audit is of the view that Swinburne should take action to recover the outstanding amounts and to determine a future strategy to strengthen the financial viability of the car park.

3.1.55 With respect to the student residence complex, audit found that cash flow from the complex was less than that projected for the 1997 calendar year and Swinburne expects this position to continue in 1998. Furthermore, budget figures prepared by the University indicate that, over the decade to 2006, operating surpluses will be significantly lower than the amounts reflected in its cash flow projections.

3.1.56 Audit was advised by Swinburne that it intends in the near future to evaluate the performance of the car park and student residence complex following the first year of its operations. Such evaluation has become increasingly important, given the difficulties encountered by the car park operator in meeting its lease obligations and the extent of over-statement of the projected returns from the student residence complex.

Mooroolbark campus

3.1.57 In April 1989, a chartered accounting firm prepared a feasibility study for Swinburne in relation to the possible acquisition by the University of the MDA Grammar School situated at Edinburgh Road, Mooroolbark, which indicated that the acquisition of the property was an opportunity for Swinburne to establish an eastern region campus.

3.1.58 The school complex comprised primary and secondary school classrooms, technology and science buildings, administration offices, together with a swimming pool, tennis courts and a partly completed main oval, all situated on a site located 38 kilometres from Melbourne. Following its establishment in 1983, the school had experienced financial problems and was put into liquidation in late 1988, with its land, buildings and equipment offered for sale by tender.

3.1.59 The financial forecast included in the study for the first 3 years of operations of the Mooroolbark campus indicated that a profit would be generated in the third year, after allowing for depreciation and borrowing costs. The study also identified that capital expenditure would be required for the property if it was to be established as a campus, including the acquisition of surrounding land, construction of a car park and alterations to existing buildings.

3.1.60 A formal offer of \$3.5 million was made by Swinburne in June 1989 for the property freehold and the associated chattels, which was accepted by the liquidator of the school and a contract of sale was subsequently signed.

3.1.61 The purchase price of \$3.5 million for the Mooroolbark property was based on a valuation prepared on behalf of the Valuer-General and comprised the site value of \$710 000 and the value of improvements amounting to \$2.8 million. The purchase price also covered the acquisition of various chattels with a value of \$884 000 including leased items of \$209 000. Audit was advised that items of furnishings and equipment that could not be used in a tertiary facility were subsequently disposed of, generating in excess of \$100 000 in proceeds.

3.1.62 The then Minister responsible for Post-Secondary Education formally referred various issues regarding this property acquisition to the Chairman of the Victorian Post-Secondary Education Commission (VPSEC) for advice. The questions posed by the Minister centred on the overall cost of the development and its potential for the extension of higher education programs in the eastern region.

3.1.63 A VPSEC committee established by the Minister in September 1989 to examine certain issues pertaining to the purchase and proposed use of the Mooroolbark property, received submissions from Swinburne, Monash University, Victoria College, La Trobe University, the Outer-Eastern Municipalities Association and a number of individuals. In its report to the Minister in November 1989, the committee recommended that a review of higher education needs of the eastern region of Melbourne, including the outer-east and south-east, be undertaken with wide terms of reference and that independent assessments be made of the space needs of Swinburne's Hawthorn campus and its capacity to sustain the investment. The committee further recommended that up to \$300 000 should be spent to complete the proposed student and staff amenities building on the Mooroolbark property to support the provision of arts, humanities and business studies at the new campus. These recommendations were subsequently accepted by the Minister.

3.1.64 The process for reviewing the higher education requirements of the eastern region culminated in a November 1992 Report of a Joint-Ministerial Working Party, titled *Swinburne University of Technology Campus in the Outer-Eastern Region of Melbourne*. The crucial recommendation included in that report was that, in order to meet an identified need to provide higher education in the outer-eastern region, the most appropriate site for the development of Swinburne's eastern region campus was the David Mitchell Estate and adjacent properties in Lilydale, which are located near the Mooroolbark campus.

3.1.65 The Mooroolbark campus commenced operations in 1992 and continued until 1996 when the Lilydale campus was opened by Swinburne. The total development cost incurred on the Mooroolbark campus up to the time of its closure amounted to \$5.2 million, comprising the initial purchase price of \$3.5 million, site improvements of \$1.1 million covering the completion of the student and staff amenities building at a cost of \$300 000, and the construction in 1994 of 2 lecture theatres for \$616 000.



3.1.66 Table 3.1E outlines student numbers at the Mooroolbark and Lilydale campuses over the 6 year period to 31 December 1997.

**TABLE 3.1E
STUDENT NUMBERS AT MOOROOLBARK AND
LILYDALE CAMPUSES, 1992 TO 1997**

<i>Year</i>	<i>Mooroolbark</i>	<i>Lilydale</i>
1992	267	-
1993	450	-
1994	628	-
1995	722	-
1996	494	510
1997	-	1 060

3.1.67 The decision to locate Swinburne’s eastern region campus at Lilydale was based on the application of specific criteria established by the working party, including transport access, relationship with TAFE facilities, quality of site, consistency with general planning considerations, presence of infrastructure support and services, cost of the development and size of available land. The working party concluded that the Lilydale site would meet all the criteria and, in particular, it was considered to be adequate in size, accessible by road or rail transport and in close proximity to a range of public and commercial services. In comparison, the Mooroolbark campus was located at a distance from transport and other facilities.

3.1.68 The purchase of the Mooroolbark property by Swinburne for a cost of \$3.5 million was financed through a 10 year loan of \$4.6 million from the Victorian Development Fund (VDF) in September 1989, which provided additional funds of \$1.1 million above the purchase price to finance drainage and road works, establishment of a library, and the acquisition of furnishings and equipment.

3.1.69 The VDF loan had an initial 4 year interest only period which was followed by 6 years of repayments of principal in equal instalments. **The annual rate of interest was fixed at 15.25 per cent during the full term of the loan. The total interest liability under the loan arrangement amounted to \$5.1 million, of which \$2.8 million was borne in the first 4 years when no principal repayments were required.**

3.1.70 In deciding to redirect available resources to its Lilydale campus, Swinburne University has commenced action to facilitate the disposal of the Mooroolbark property. **The full financial impact of Swinburne’s decision to invest in the Mooroolbark campus at a cost of around \$5.2 million which was only utilised for 5 years, will not be determined until the property is sold.**

- **RESPONSE** provided by Deputy Vice-Chancellor, Swinburne University of Technology

Carpark and student residence complex

As at 28 April 1998, the outstanding amount owed by the car park operator to the University totalled \$35 851, which relates to part of the March lease rental. Arrangements are in hand for the operator to provide \$30 000 in instalments of \$15 000 by 8 May 1998 and the balance will be covered by the income in excess of the lease rental for April and, if necessary, offset against moneys owed by this University to the operator. This is a significant improvement in the status of the debt at the time of the audit. Occupancy performance has improved significantly over 1997 with March and April income levels in excess of the lease obligations and it is expected that this will continue for the balance of the academic year.

As we anticipated, the change from free parking to fee-paying has taken time to be accepted.

Mooroolbark campus

In 1988 the University recognised that it needed to seek additional accommodation to meet future demand and made a strategic decision to locate in an area which had both potential for growth and that had also been under-represented in higher education participation. The purchase of the Mooroolbark campus provided the opportunity and 2 561 students have been accommodated over the 5 year period of occupancy. After the Government decided that Swinburne should operate the new campus established within the eastern region at Lilydale, the University agreed to relocate and has considered a number of options for the Mooroolbark campus. We have now decided to dispose of the campus so that these resources might be better utilised at the Lilydale campus and for other University initiatives.

The University is satisfied that the decision to purchase the campus was correct, in that the needs of the region were fulfilled. Our decision has been endorsed by the Governments' subsequent decision to establish the Lilydale campus. Disposal of the Mooroolbark campus will provide for further needed development at the Lilydale campus and for other strategic initiatives.



DEVELOPMENT OF UNIVERSITY IT SYSTEMS - THE CASMAC PROJECT

3.1.71 The acquisition and implementation of computer systems to service an individual university’s administrative and management information needs has traditionally been a protracted and expensive process. To facilitate the efficient and timely development of common computing systems for application by universities across Australia, in 1991 a national initiative was established by the Australian Universities Vice-Chancellor’s Committee to prepare a Core Australian Specification for Management and Administrative Computing (CASMAC).

3.1.72 The CASMAC project was aimed at providing universities with efficiencies in software development through the sharing of knowledge and associated costs. The modules to be developed under CASMAC were:

- student records;
- finance;
- physical resources;
- research and consultancy; and
- human resources

3.1.73 The objective of CASMAC was to develop generic, adaptable and integrated core administrative computing applications that individual universities could tailor to meet local conditions and needs. In particular, it was anticipated that CASMAC-compliant software would meet around 80 per cent of the needs of any university.

3.1.74 During February 1993, a survey of universities was undertaken with the view of establishing the preferred development environment for the CASMAC software. The results of the survey indicated that there was not unanimous support for any one platform. As a consequence, 2 options were identified: one founded on the “Powerhouse” development environment, with CHA Computer Solutions Pty Ltd (CHA) as the supplier, and the other based on the “Oracle” development environment with the expectation of Oracle Systems Australia being the software supplier.

3.1.75 In July 1993, the Australian Vice-Chancellors’ Committee established a company known as UniPower Australia Pty Ltd, whose sole purpose was to deliver to a group of 19 universities the CASMAC-compliant software applications, under the “Powerhouse” development environment. **These 19 universities collectively agreed to meet the cost, estimated to be approximately \$11 million for software development and licence fees, and to provide resources in the form of staff time and expertise for systems specification, acceptance testing and implementation.** The Victorian universities involved were:

- Ballarat University;
- LaTrobe University;
- Monash University;
- RMIT University; and
- Victoria University of Technology.

.....

3.1.76 During July 1993, UniPower Australia Pty Ltd entered into a contract with CHA for the development of CASMAC-compliant software applications for utilisation by the member universities. The key phases of the project were to:

- further define functional specifications (CHA responsibility);
- develop detailed design specifications (CHA responsibility);
- develop the software (CHA responsibility);
- test the software (CHA responsibility);
- perform acceptance testing of the delivered software (UniPower responsibility); and
- implement within the member universities the software in accordance with their individual needs (individual university's responsibility).

3.1.77 With respect to the modules that were required to be developed, the following outcomes were achieved up to the end of 1996 by the project:

- the research and consultancy module was developed and accepted by UniPower Australia Pty Ltd in December 1995, subject to the resolution of a number of issues;
- the human resources module was accepted by UniPower Australia Pty Ltd in October 1996, based on a commitment by CHA to 3 additional deliverables to address a number of outstanding issues; and
- the physical resources module was accepted by UniPower Australia Pty Ltd in December 1996, subject to a subsequent resolution of certain outstanding issues.

3.1.78 In February 1997, UniPower Australia Pty Ltd advised CHA that the finance application software had repeatedly failed acceptance testing and that it was terminating its contract with CHA. As a consequence of this advice, both parties have commenced legal action against each other in the New South Wales Supreme Court. As at the date of the termination of the contract, the matters identified above remained unresolved.

Proposed audit review

3.1.79 During January 1998, I wrote to the RMIT, Monash and LaTrobe Universities and indicated my intention to undertake a review of their participation in the CASMAC project, with the audit focusing on whether:

- an adequate analysis of information requirements was conducted by the universities;
- key milestones were achieved by the universities within the established scheduled timeframe; and
- the universities' information requirements were met in the most economic, efficient and effective manner.



3.1.80 In response to this communication, the 3 universities advised that as the proposed review would examine issues in dispute between UniPower Australia Pty Ltd and CHA, based on legal advice it would be inappropriate for the review to proceed at this time when issues were subject to the Supreme Court's jurisdiction.

3.1.81 Given the above circumstances, I agreed to postpone the audit review until the litigation between UniPower Australia Pty Ltd and CHA is concluded. It is my intention to undertake the audit review following the finalisation of the legal action, with the results reported to Parliament at that time.

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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>
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MATTERS RESOLVED OR ACTION COMMENCED

DEPARTMENT OF EDUCATION

<i>Ministerial Portfolios, May 1996, p. 27.</i>	The Department 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.	The database has been interrogated and assets with excessive valuation were corrected following verification with schools.
<i>Ministerial Portfolios, May 1996, p. 27.</i>	The Department needs to reinforce to all schools that regular stocktakes need to be undertaken in order to identify missing or surplus assets.	The Department distributed advice to all schools which addressed the issue of stocktaking.
<i>Ministerial Portfolios, May 1997, pp. 26-7.</i>	There is a need for improved financial skills and accountability in schools. As schools become more independent consideration needs to be given to increasing their level of accountability to the Parliament. It is important that the Auditor-General, as Parliament's auditor, is involved in this accountability process.	Schools are encouraged to appoint the most suitability qualified people to School Councils and have the option of co-opting people with specific expertise. The annual financial audit program for 1998 now requires the auditor to comment if it is perceived there is a need for additional financial expertise and if School Councils are not regularly reviewing financial performance against budget projections.

UNIVERSITY OF MELBOURNE

<i>Ministerial Portfolios, May 1996, pp. 52-3.</i>	The University should implement an internal user-charging system to act as an incentive to ensure the economical use of existing properties and to assess requests for additional space.	The University has investigated methodologies used for space charging both in Australia and overseas. The University will consider if such a system is appropriate and if so when it will be implemented.
<i>Ministerial Portfolios, May 1996, pp. 47-8.</i>	The existing uneven pattern of use of the University's 66 lecture theatres, 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.	The University has implemented a computer-aided lecture theatre allocation process.



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>
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MATTERS RESOLVED OR ACTION COMMENCED - continued

UNIVERSITY OF MELBOURNE - continued

<p><i>Ministerial Portfolios, May 1996, pp 33-47.</i></p>	<p>Lengthy delays have occurred in the determination of an appropriate academic or research-related use for some property acquisitions. Audit identified substantial properties which had been under-utilised or inappropriately utilised for lengthy periods. The University should place greater emphasis on rationalising and consolidating its existing stock of property assets and reduce its focus on the expansion of its property portfolio.</p>	<p>The University has realised the strategic benefits of holding these properties. In particular:</p> <ul style="list-style-type: none"> • the fit-outs of properties situated at 234 Queensberry Street and 207-221 Bouverie Street, Carlton have now been completed and are fully occupied; and • the properties in the Leicester Street, Bouverie Street and Pelham Street, Carlton precinct have been made available to the Melbourne Business School to enable it to expand. <p>Further, the University has been successful in finding a buyer for the Russell Street, Theatre and that due to the relocation of certain University activities other properties in Kew and at Mt Derrimut are on the market for sale.</p>
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ROYAL MELBOURNE INSTITUTE OF TECHNOLOGY

<p><i>Ministerial Portfolios, May 1997, pp. 33-4.</i></p>	<p>A review conducted by independent consultants during 1995 identified that \$125 million of necessary expenditure on safety, regulatory and building condition works over a 10 year period was required to bring the University's building stock to an acceptable standard. However, the University's planned maintenance expenditure is substantially less than required.</p>	<p>The University is continuing to address the problems identified in the areas of safety, regulatory and building condition works given current government funding and fiscal constraints.</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>
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MATTERS RESOLVED OR ACTION COMMENCED - continued

ROYAL MELBOURNE INSTITUTE OF TECHNOLOGY - continued

<i>Ministerial Portfolios, May 1997, pp. 37-9.</i>	Internal reviews of utilisation levels have consistently established a compelling need for decisive action to redress the poor utilisation of teaching accommodation. The audit review found several parcels of accommodation which are within the University's area of strategic interest which currently do not contribute to its overall objectives as they are underutilised or inappropriately utilised. The University needs to place a greater emphasis on the rationalisation and maintenance of its existing property assets to ensure that the utilisation of properties held by the University is maximised.	A new room booking system has been introduced, and a space planning model is planned to be introduced, to maximise efficient and effective use of space. Further, a system for the internal charging for the use of all space within the University was introduced during January 1998 to provide a means to rationalise accommodation and further improve utilisation. The University's objective of long-term strategic planning is being implemented through, among other things, the commencement of a new long-term master planning project for the City and Bundoora Campuses and the revision and extension of the Capital Management Plan to provide a detailed 5 year outlook.
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ADULT, COMMUNITY AND FURTHER EDUCATION BOARD

<i>Ministerial Portfolios, May 1997, pp. 46-7.</i>	The Board needs to establish criteria to assess service providers' submissions and to document evaluations to ensure that funding allocations are soundly based and equitable.	The Board proposes to assess service providers' submissions using a best practice approach.
<i>Ministerial Portfolios, May 1997, p. 47.</i>	Due to deficiencies in accountability arrangements with service providers related to the follow-up, use and audit of service provider's financial statements by regional councils, assurance was generally not obtained that grants had been appropriately expended in accordance with performance agreements.	The receipt of service provider's financial statements is now monitored by a grants management system. In addition, the Board's best practice project aims to improve monitoring and performance.



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>
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MATTERS RESOLVED OR ACTION COMMENCED - continued

ADULT, COMMUNITY AND FURTHER EDUCATION BOARD - continued

<i>Ministerial Portfolios, May 1997, p. 48.</i>	To ensure probity over regional council operations, there is a need to reinforce members' responsibilities relating to issues of actual or potential conflicts of interest.	Regional council members have been reminded of their responsibility to declare pecuniary interests and a good governance guide has been issued.
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**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>
COMPLETED AUDITS				
Department of Education	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	28 Aug. 1997	29 Aug. 1997
EDUCATION				
Board of Studies	30 June 1997	" "	28 Aug. 1997	31 Aug. 1997
Telematics Course Development Fund Trust	31 Dec. 1996	30 April. <i>Financial Management Act 1994,</i> s.46.	7 April 1997	15 July 1997
TERTIARY EDUCATION AND TRAINING				
Adult, Community and Further Education Board	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	29 Aug. 1997	29 Aug. 1997
Council of Adult Education	31 Dec. 1997	30 April. <i>Financial Management Act 1994,</i> s.46.	24 Feb. 1998	27 Feb. 1998
International Training Australia Pty Ltd	31 Dec. 1997	30 April. <i>Financial Management Act 1994,</i> s.53A.	9 April 1998	9 April 1998
State Training Board	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	28 Aug. 1997	28 Aug. 1997
Victorian Tertiary Admission Centre	30 June 1997	No reporting requirements.	10 Oct. 1997	10 Oct. 1997
Australian Music Examination Board (Vic.) Ltd	31 Dec. 1997	30 April. <i>Financial Management Act 1994,</i> s.53A.	13 Feb. 1998	25 Mar. 1998
Australian National Academy of Music Ltd	31 Dec. 1997	" "	18 Mar. 1998	30 Mar. 1998
Centre for Innovative Enterprise Pty Ltd	31 Dec. 1997	" "	12 Mar. 1998	13 Mar. 1998
Centre for Innovative Enterprise Trust	31 Dec. 1997	" "	12 Mar. 1998	13 Mar. 1998
Citytech Pty Ltd	31 Dec. 1997	" "	1 April 1998	1 April 1998
Deakin University	31 Dec. 1997	30 April. <i>Financial Management Act 1994,</i> s.46.	16 Mar. 1998	16 Mar. 1998
Deakin Software Services Pty Ltd	31 Dec. 1997	30 April. <i>Financial Management Act 1994,</i> s.53A.	16 Mar. 1998	16 Mar. 1998
Dova Port Pty Ltd	31 Dec. 1997	" "	10 April 1998	28 April 1998

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>
COMPLETED AUDITS- continued				
Post-secondary education institutions				
<i>Universities and associated companies</i>				
Hawthorn Institute of Education Ltd	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.53A.</i>	21 Apr. 1998	22 Apr. 1998
Hawthorn International Education Ltd.	31 Dec. 1997	" "	30 April. 1998	30 April. 1998
Institute for Innovation and Enterprise Ltd	31 Dec. 1997	" "	5 Mar. 1998	13 Mar. 1998
La Trobe International Pty Ltd	31 Dec. 1997	" "	3 Mar. 1998	10 Mar. 1998
La Trobe Marketing Pty Ltd	31 Dec. 1997	" "	2 Mar. 1998	10 Mar. 1998
La Trobe University	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s. 46.</i>	8 April 1998	9 April 1998
La Trobe University Housing Ltd	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.53A.</i>	27 Feb. 1998	16 Mar. 1998
Melbourne Information Technologies Australia Pty Ltd	31 Dec. 1997	" "	20 Mar. 1998	25 Mar. 1998
Melbourne Research Enterprises Ltd (a)	31 Dec. 1997	" "	18 Mar. 1998	25 Mar. 1998
Meltech Services Pty Ltd	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.53A.</i>	23 Mar. 1998	25 Mar. 1998
Monash - Mt Eliza Graduate School of Business and Government Ltd	31 Dec. 1997	" "	17 Feb. 1998	10 Mar. 1998
Monash International Pty Ltd	31 Dec. 1997	" "	12 Feb. 1998	17 Feb. 1998
Monash IVF Pathology Services Pty Ltd	31 Dec. 1997	" "	17 Feb. 1998	5 Mar. 1998
Monash IVF Pathology Services Trust	31 Dec. 1997	" "	12 Feb. 1998	5 Mar. 1998
Monash IVF Pty Ltd	31 Dec. 1997	" "	17 Feb. 1998	5 Mar. 1998
Monash Language Centre Pty Ltd	31 Dec. 1997	" "	29 Jan. 1998	6 Feb. 1998
Monash Unicom Pty Ltd (b)	31 Dec. 1997	" "	11 Feb. 1998	12 Mar. 1998

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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>
COMPLETED AUDITS - continued				
Post-secondary education institutions - continued				
<i>Universities and associated companies - continued</i>				
Monash Merchandising Unit Trust	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.53A.</i>	9 Mar. 1998	13 Mar. 1998
Monash University	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.46.</i>	10 Mar. 1998	17 Mar. 1998
Monash Ultrasound Pty Ltd	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.53A.</i>	17 Feb. 1998	5 Mar. 1998
Monash Ultrasound Trust	31 Dec. 1997	" "	17 Feb. 1998	5 Mar. 1998
Monash University Foundation Pty Ltd	31 Dec. 1997	" "	9 Mar. 1998	10 Mar. 1998
Monash University Foundation Trust	31 Dec. 1997	" "	9 Mar. 1998	10 Mar. 1998
Montech Medical Development Pty Ltd	31 Dec. 1997	" "	26 Feb. 1998	5 Mar. 1998
Montech Pty Ltd	31 Dec. 1997	" "	6 Feb. 1998	5 Mar. 1998
Neurometric Systems Pty Ltd	31 Dec. 1997	" "	5 Mar. 1998	13 Mar. 1998
RMIT	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.46.</i>	9 Apr. 1998	15 April 1998
RMIT Foundation	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.53A.</i>	2 April 1998	2 April 1998
RMIT Innovation Ltd	31 Dec. 1997	" "	30 Mar. 1998	1 April 1998
RMIT International Pty Ltd	31 Dec. 1997	" "	24 Mar. 1998	1 April 1998
RMIT Malaysia	31 Dec. 1997	" "	30 Mar. 1998	9 April 1998
RMIT Resources Limited	31 Dec. 1997	" "	30 Mar. 1998	1 April 1998
RMIT Training Pty Ltd	31 Dec. 1997	" "	30 Mar. 1998	1 April 1998
RMIT Union	31 Dec. 1997	" "	24 Mar. 1998	25 Mar. 1998

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>
COMPLETED AUDITS - continued				
Post-secondary education institutions - continued				
<i>Universities and associated companies - continued</i>				
School of Forestry Creswick Ltd	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.53A.</i>	22 Jan. 1998	11 Feb. 1998
Sir John Monash Business Centre Pty Ltd	31 Dec. 1997	" "	27 Feb. 1998	10 Mar. 1998
Swinburne Ltd	31 Dec. 1997	" "	13 Mar. 1998	13 Mar. 1998
Swinburne University of Technology	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.46.</i>	13 Mar. 1998	13 Mar. 1998
Unilink Ltd	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.53A.</i>	7 April 1998	7 April 1998
University of Ballarat	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.46.</i>	27 Mar. 1998	27 Mar. 1998
University of Melbourne	31 Dec. 1997	" "	28 April 1998	30 April 1998
Victoria University Enterprises Proprietary Limited	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.53A.</i>	24 Mar. 1998	25 Mar. 1998
Victoria University of Technology	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.46.</i>	25 Mar. 1998	25 Mar. 1998
Victoria University of Technology Foundation Ltd	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.53A.</i>	25 Mar. 1998	25 Mar. 1998
Victorian College of Agriculture and Horticulture Ltd	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.46.</i>	23 Apr. 1998	29 Apr. 1998
Victorian College of Agriculture and Horticulture Services Ltd	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.53A.</i>	28 Feb. 1998	30 Apr. 1998
Victorian College of Agriculture and Horticulture Foundation Trust	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.53A.</i>	28 Feb. 1998	29 Apr. 1998
Victorian College of the Arts	31 Dec. 1997	30 April. <i>Financial Management Act 1994, s.46.</i>	20 Feb. 1998	16 Mar. 1998

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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>
COMPLETED AUDITS - continued				
<i>Institutes/Colleges of Technical and Further Education</i>				
Barton	31 Dec. 1997	30 April. <i>Financial Management Act 1994,</i> s.46.	25 Feb. 1998	27 Mar. 1998
Bendigo Regional	31 Dec. 1997	" "	12 Mar. 1998	12 Mar. 1998
Box Hill	31 Dec. 1997	" "	2 Mar. 1998	2 Mar. 1998
Box Hill Enterprises Ltd	31 Dec. 1997	30 April. <i>Financial Management Act 1994,</i> s.53A.	2 Mar. 1998	2 Mar. 1998
Casey	31 Dec. 1997	30 April. <i>Financial Management Act 1994,</i> s.46	6 Mar. 1998	11 Mar. 1998
Central Gippsland	31 Dec. 1997	" "	13 Mar. 1998	13 Mar. 1998
Driver Education Centre of Australia Ltd	31 Dec. 1997	30 April. <i>Financial Management Act 1994,</i> s.53A.	27 Mar. 1998	30 Mar. 1998
East Gippsland	31 Dec. 1997	30 April. <i>Financial Management Act 1994,</i> s.46.	26 Feb. 1998	12 Mar. 1998
Eastern (c)	31 Dec. 1997	" "	5 Mar. 1998	5 Mar. 1998
Gordon Institute	31 Dec. 1997	" "	26 Feb. 1998	27 Feb. 1998
Goulburn Ovens	31 Dec. 1997	" "	27 Mar. 1998	27 Mar. 1998
Holmesglen	31 Dec. 1997	" "	12 Mar. 1998	13 Mar. 1998
Kangan Batman (d)	31 Dec. 1997	" "	30 Mar. 1998	31 Mar. 1998
Melbourne Institute of Textiles	31 Dec. 1997	" "	24 Mar. 1998	25 Mar. 1998
Northern Melbourne	31 Dec. 1997	" "	23 Feb. 1998	26 Feb. 1998
Peninsula Institute	31 Dec. 1997	" "	10 Feb. 1998	10 Feb. 1998
School of Mines and Industries Ballarat Ltd	31 Dec. 1997	" "	18 Feb. 1998	18 Feb. 1998
South West	31 Dec. 1997	" "	26 Feb. 1998	16 Mar. 1998

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>
COMPLETED AUDITS - continued				
<i>Institutes/Colleges of Technical and Further Education - continued</i>				
Sunraysia	31 Dec. 1997	30 Apr. <i>Financial Management Act 1994,</i> s46.	26 Feb. 1998	17 Mar. 1998
Western Melbourne	31 Dec. 1997	" "	17 Mar. 1998	20 Mar. 1998
William Angliss	31 Dec. 1997	" "	31 Mar. 1998	31 Mar. 1998
Wimmera	31 Dec. 1997	" "	18 Feb. 1998	18 Mar. 1998
Wodonga	31 Dec. 1997	" "	2 Mar. 1998	5 Mar. 1998

INCOMPLETE AUDITS

EDUCATION

Telematics Course Development Fund Trust	31 Dec. 1997	30 April. <i>Financial Management Act 1994,</i> s.46.	Audit substantially completed.
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- (a) Melbourne Research Enterprises Ltd was previously known as UniMelb Ltd.
 (b) Monash Unicom Pty Ltd was previously known as Monash Merchandising Trust.
 (c) Eastern Institute of TAFE was previously Outer Eastern.
 (d) Kangan Batman results from the merge of Kangan and John Batman Institute of TAFEs.

Part 3.2

Human Services

KEY FINDINGS

Department of Human Services tendering procedures

- Departmental procedures do not require that a business case be developed when considering the outsourcing of functions or activities and therefore the Department is not in a position to determine whether the most cost-efficient and effective option has been selected for the provision of services.
Paras 3.2.14 to 3.2.15
- Audit examination identified instances where there was no documentary evidence to substantiate whether goods and services had been provided in accordance with the contract specifications nor was there any analysis of the quality of service provision by contractors.
Paras 3.2.18 to 3.2.22
- A number of procedural deficiencies were identified by audit which need to be addressed by the Department to ensure the ongoing integrity of its contracting arrangements.
Paras 3.2.16 to 3.2.17

Management of Residents' Amenities Funds

- Deficiencies were identified in the content, approval and monitoring of expenditure plans relating to Residents' Amenities Funds.
Paras 3.2.23 to 3.2.29
- Audit identified that Residents' Amenities Funds were not only used to acquire goods and services for the use of residents but were also used to fund the normal operating activities of institutions.
Para. 3.2.30 to 3.2.31
- The Department was not in a position to readily identify assets purchased from Residents' Amenities Funds and therefore ensure as required by the governing legislation that the proceeds on disposal of these assets are returned to eligible persons.
Paras 3.2.35 to 3.2.36

3.2.1 The Minister for Health and 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. In addition to the Department of Human Services, the entities listed below were subject to audit by the Auditor-General during the 1996-97 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>
Aboriginal Affairs	-
Aged Care	-
Youth and Community Services	-
Health	Advanced Dental Technicians Qualifications Board Ambulance Officers' Training Centre Alexandra and District Ambulance Service Ambulance Service Victoria - Metropolitan Region North Eastern Region North Western Region South Eastern Region South Western Region Western Region Anti-Cancer Council of Victoria Chiroprodists Registration Board of Victoria Chiropractors and Osteopaths Registration Board of Victoria Dental Board of Victoria Dental Technicians Licensing Committee Health Computing Service Victoria Ltd Infertility Treatment Authority Medical Practitioners Board of Victoria Mental Health Review Board Nurses Board of Victoria Optometrists Registration Board of Victoria Pharmacy Board of Victoria Physiotherapists Registration Board of Victoria Prince Henry's Institute of Medical Research Psychologists Registration Board of Victoria Psychosurgery Review Board Public cemeteries - Anderson's Creek Cemetery Trust Ballarat General Cemeteries Trust Bendigo Cemeteries Trust Cheltenham and Regional Cemeteries Trust Geelong Cemeteries Trust Keilor Cemetery Trust Mildura Cemetery Trust Preston Cemetery Trust Templestowe Cemetery Trust Trustees of the Fawkner Crematorium and Memorial Park

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

<i>Ministerial portfolio</i>	<i>Entities subject to audit</i>
Health	Trustees of the Lilydale Memorial Park and Cemetery Trustees of the Memorial Park Altona Trustees of the Necropolis Springvale Werribee Cemetery Trust Public hospitals (99) Victorian Health Promotion Foundation
Housing	-

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

DEPARTMENT OF HUMAN SERVICES TENDERING PROCEDURES

3.2.4 The Department of Human Services spends around \$5 billion per annum on providing a diverse range of health, housing and community services. In the 1996-97 financial year, services with a value of approximately \$3.9 billion were provided by agencies under funding and service agreements with the Department. These agreements are generally with government-related agencies such as hospitals, health care networks and public nursing homes, and a range of community and non-government organisations which mainly provide welfare services. The Department is progressively introducing contestability for these services which will result in a substantial increase in the number of services subject to tender arrangements in the future.

3.2.5 Through the Office of Housing, the Department administers over 69 300 direct tenure and community-managed public rental properties. For many years, the repair, maintenance and construction of these properties has been provided under contracts arranged by the Office. The Office's contracting procedures were recently reviewed by the Department's internal audit which found that, overall, the procedures were satisfactory although certain deficiencies in tender lodgement, registration and payment authorisation procedures were identified. These deficiencies are currently being addressed by the Department.

3.2.6 The Department also directly provides certain services, particularly in the areas of intellectual disability accommodation, child protection and mental health. In line with the Government's policy of reducing the State's role in the direct provision of services, the Department is increasingly engaging service providers to deliver these services, as well as outsourcing certain administrative and support functions. During the year ended 30 June 1997, the Department entered into more than 123 such contracts valued at over \$50 million.



3.2.7 In view of the Department's increasing reliance on outsourcing arrangements, it was considered timely for audit to review the Department's centralised tendering procedures. The review involved a detailed examination of a sample of contracts awarded during the 1996-97 financial year and was aimed at determining whether the Department's centralised tender and contract processes were consistent with the government's guidelines and represented best practice.

3.2.8 The audit review identified that the Department had established a comprehensive framework to enable the effective management of the tender process and that, overall, its contracting procedures were operating effectively and in line with government guidelines. However, **a number of deficiencies were identified relating to the evaluation of service delivery options, completeness of documentation and contract monitoring which require attention in order to strengthen the Department's contracting processes and service delivery outcomes.**

Contracting framework

3.2.9 The Victorian Government Purchasing Board (VGPB) was established in February 1995 with the aim of introducing more effective business practices, systems and skills into government purchasing arrangements. Under procedures implemented by the Board, each department is required to establish an Accredited Purchasing Unit (APU) to oversee tendering arrangements and to ensure that procedures for the purchase of goods and services are in accordance with guidelines established by the VGPB.

3.2.10 The APU established by the Department of Human Services meets weekly and is responsible for approving contracts with a value greater than \$100 000 based on recommendations submitted by responsible areas within the Department. The Department's APU has a delegation to approve individual contracts for the purchase of goods and services to a value of up to \$500 000, with contracts over this amount required to be endorsed by the APU prior to submission to the VGPB for approval.

3.2.11 To facilitate control over tender and contract processes, the Department has issued guidelines titled *A Guide to Purchasing, Tendering, Consultancies & Contracting* which are available for use by all departmental officers involved with any aspect of purchasing. Audit found that the guidelines were generally comprehensive and consistent with the requirements of the VGPB.

3.2.12 In addition, the Department has established within each of its divisions and regions a contracting and tendering co-ordinator who, as the first point of contact, provides advice and assistance in relation to engaging consultants or entering into contracts. The co-ordinator has the responsibility to ensure that the process of engaging consultants and contractors is effectively controlled. The role encompasses distributing information, consulting with all relevant parties, co-ordinating reporting requirements, and monitoring divisional and regional compliance with government and departmental guidelines.

3.2.13 Audit found that the role of contracting and tendering co-ordinators was well-defined and assisted in the provision of effective control and co-ordination over the contracting process.

Evaluation of service delivery options



3.2.14 As previously indicated, the Department's community service responsibilities and its administrative and support functions are performed utilising a mix of in-house resourcing and a range of service providers from the private sector, charitable institutions, and government and semi-government agencies. Given that the different modes of service delivery can result in substantial variations in cost and effectiveness, it is important that any outsourcing opportunities be fully evaluated to determine whether the respective functions or activities should be performed internally or outsourced. Such evaluations should include the development of a business case which compares internal operations with external options, from both a cost and service perspective, to ensure that any decision to outsource is soundly based.

3.2.15 **Audit found that the Department's procedures do not require that a business case be developed when considering the outsourcing of functions or activities. In the absence of such analysis, the Department is not in a position to determine whether the most cost-efficient and effective option has been selected for the provision of services.**

Procedural deficiencies

3.2.16 The audit review identified a number of procedural deficiencies which need to be addressed by the Department to ensure the ongoing integrity of its contracting arrangements. In particular:

- One contract had not been signed more than 18 months after the contract was awarded. Without a formal agreement in place which details the rights, obligations and liabilities of the respective parties, any disputes which may arise could be difficult to resolve and may result in either party suffering financial loss;
- As part of the Department's procedures supporting the selection of successful tenderers, reports are prepared which include documentation on the selection criteria, the rating of tenderers, and the rationale for selection of the successful tenderer. However, audit found that these reports were not always prepared. The absence of such documentation raises doubts over the transparency of the decision-making process; and
- The Department's guidelines state that tenders cannot be removed from the tender box until the close of the tender process and that no tenders will be accepted after the closing time. While audit found that the tender closing times were adhered to and tenders were not accepted after the advertised closing time, in cases where a large volume of tenders were received, the tender box was often emptied prior to the advertised tender closing times. Furthermore, no procedures or controls had been established to ensure that such occurrences were formally documented and authorised, with provision of adequate security over the tender documentation.

3.2.17 **There is a need for the Department to address these deficiencies to ensure that all parties have full confidence in the integrity of the processes.**



Contract monitoring

3.2.18 The Department's guidelines detail the monitoring and evaluation requirements in regard to consultancies. Under the guidelines, a formal assessment of the consultant's performance covering competency, fulfilment of contractual obligations and whether the consultant should be used for future work, must be undertaken prior to final payment being made under the contractual arrangements.

3.2.19 In regard to other service providers, the guidelines state that, "... it is expected that the officer responsible for the contract monitors it and ensures the goods and services are provided in accordance with the contract specifications". However, audit identified that specific monitoring requirements were not set out in the guidelines.

3.2.20 Notwithstanding the limited monitoring requirements in the guidelines, the Department has recently strengthened the monitoring of contract expenditure following the identification of a substantial cost over-run in a major contract. The contract, which related to communication consultancy services with a total contract sum of \$568 000 had contract over-runs totalling \$505 000. Under the revised arrangements, the Department has enhanced its Executive and Management Information System to assist in monitoring both actual expenditure compared with budget and time expended against the term of contracts.

3.2.21 Audit found that the revised arrangements for monitoring consultancy arrangements were satisfactory. However, in regard to the other contracts reviewed by audit, there was no documentary evidence to substantiate whether goods and services had been provided in accordance with the contract specifications, nor was there any analysis of qualitative issues, such as the level of service provided, the responsiveness of the contractor and quality of performance. In the absence of this information, audit was unable to determine whether the contractor had complied with the contractual obligations and provided a satisfactory level of service.

3.2.22 To ensure adequate accountability over contracts, the Department needs to establish formalised monitoring procedures covering both service delivery and qualitative issues. Such procedures should enable poor performance to be highlighted and appropriately addressed by management.

□ RESPONSE provided by Secretary, Department of Human Services

While the Report includes endorsement of departmental procedures and processes, the scale and complexity of the policy and service environment should also be acknowledged, to provide fuller context to the criticisms that are also contained. The Department has made large improvements in tendering service provision to the community, and has put in considerable effort in managing the transition from grants provision to the community, and has put in considerable effort in managing the transition from grants provision to contestability in service delivery. In these areas, the Department arguably leads agencies in any other jurisdiction across Australia.

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

Contracting framework

The audit finding is a welcome endorsement of internal procedures established by DHS.

Evaluation of service delivery options

The Department is committed to the principles of accountability and the selection of its service providers by the most contestable method appropriate. DHS has established a Contestability Steering Committee to develop policy in this regard. Business rules concerning contestable service provider selection have been drafted and will be promulgated across the Department, pending endorsement.

The Department's policy development has considered principles to ensure the most appropriate and cost-effective option for service delivery is assessed and selected for DHS services, and it is likely that all internal services will be assessed for market testing. Key stages and processes will include In-Principle Ministerial approval of the Business Case and, where appropriate, post-implementation review of the outsourced services, with assessment of the outcomes of revised contestable arrangements against the original business case.

Procedural deficiencies

The Department is committed to compliance with all internal and external procedures, but, in a complex and evolving environment, there may have been occasions when processes or outcomes have been less than ideal. However, it is apparent there is some mis-interpretation of data provided to the Auditor-General, and misunderstanding of the validity of DHS procedures.

Contract not signed more than 18 months after the contract was awarded

Departmental procedures are devised and structured to promote proper practice and minimise occurrences of this nature in the timely development and execution of contracts.

The Department is making strong efforts to enhance the capacity of DHS staff to manage contracting and service purchasing. Strategies include development of management tools; develop and define business rules and processes; and development of promotion of training and skills development.

Lack of supporting documentation in contractor selection

DHS does not accept there is a procedural deficiency in its requirements for supporting documentation in contractor selection. The Department has well documented requirements in relation to contractor selection, and stringent endorsement and approval procedures. A tender evaluation report is a core element in the documentation required.

For commercial contracts, only the Secretary to the Department, or the relevant Minister, may execute an agreement, and this only after endorsement by the Tendering and Contracting Co-ordinator, the program managers, the appropriate Director, the Director, Corporate Resources and, where the tender is for an amount greater than \$100 000, the DHS Accredited Purchasing Unit (APU). Without a tender evaluation report, a commercial contract with any contractor would not be approved nor executed.

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



Lack of supporting documentation in contractor selection - continued

In one instance referenced, documentation was prepared and sighted by the DHS APU, but may not have been filed at the time of the audit.

Tender box procedures

DHS has confirmed with the Victorian Government Purchasing Board (VGPB) that procedures for removal of tender documents from the tender box prior to the advertised closing time for tenders accord with procedures recommended by the VGPB.

The action is appropriate where tender box facilities are inadequate for large volumes of tender submissions, or large individual submissions, received prior to tender closing and where there is a risk of security breach if alternative measures are not instituted. VGPB Supply Policies and Guidelines provide for the Officer on Duty (who is an Authorised Tender Officer) to be responsible for this action.

In DHS, Authorised Tender Officers are the only personnel in possession of keys to the tender box, which is only opened in the presence of 2 authorised officers.

Where such action has been taken in relation to DHS tenders, the Authorised Tender Officer has approved the removal and secure storage of documentation, and has been present to ensure that the security and integrity of the tender process is not compromised. In view of the Department's established procedures and their concurrence with VGPB guidelines, process integrity is not at risk in relation to tender receipt.

Contract monitoring

The Department's tendering and contracting procedures promote accountability through performance assessment. A major component of the Department's contracting function, Service Agreements, are performed-based, incorporating annual assessment and review. Service Agreements account for some 80 per cent of the Department's budget.

For commercial contracts, payment to contractors is based upon delivery of defined products or achievement of stages in a project, with the contract manager responsible for assessment of whether these stages have been achieved and products delivered before payment is authorised. Where a contract is for an amount greater than \$25 000, the Department's standard agreement states: "The Secretary shall withhold 20 per cent of the amount to be ... until the Secretary is satisfied that the Project is satisfactorily completed".

Where a contract is classified as a consultancy, the Department follows the recommendations of the VGPB and requires 2 evaluation reports to be prepared, an Evaluation Report prepared prior to final payment to the consultant, and a Post-Implementation Report, prepared 3 to 6 months after completion of the project and implementation of recommendations. The extension of this requirement to all contracts, rather than just consultancies, is under consideration.



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

Contract monitoring - continued

The Department has established contract monitoring facilities through its Executive and Management Information System, the Service Agreement Management System and the Contracts/Consultants Database.

Additionally, DHS will be introducing new business rules to ensure evaluation of the effectiveness of outsourcing services. Programs will undertake a post-implementation review of outsourced services and assess the outcomes of revised contestable arrangements against the original business case.





MANAGEMENT OF RESIDENTS' AMENITIES FUNDS

3.2.23 The Department of Human Services, through its Disability Services Division, provides care and support for people with intellectual, physical, sensory and neurological disabilities. As well as providing institutional care, the Department also funds community-based residential care and home accommodation for people with such disabilities.

3.2.24 In recent years, there has been a downsizing of institutional care, with the majority of people with disabilities now living in community settings supported by various departmental programs. At 31 December 1997, there were 4 institutions operated by the Department which provided accommodation for approximately 850 clients.

3.2.25 Residents' Amenities Funds have been in place for many years at departmental-operated institutions as a means of enhancing the well-being and quality of life of residents. Up until 1992, residents were required to pay a levy into a Residents' Amenities Fund operated by each institution. However, since 1992, such levies were not required to be raised and amenities funds have only derived income from donations, proceeds from the sale of assets originally purchased with moneys from the Funds, interest and occasional grants from the Department. As at 31 December 1997, around \$1 million was held in Residents' Amenities Funds.

3.2.26 The management of the Residents' Amenities Funds is regulated by the *Intellectually Disabled Persons' Services Act 1986*. Under the Act, Residents' Amenities Funds may be operated at each institution and can only be applied "... for the purposes of providing goods or services or other amenities for the benefit or use of eligible persons generally at that institution". Furthermore, the Act requires that :

- an annual plan for expenditure from these Funds be prepared by the Secretary to the Department;
- when an institution is closed, the proceeds from the sale of assets originally purchased from these Funds are to be paid back into the Funds; and
- amounts remaining in these Funds following the closure of an institution are to be distributed to eligible persons.

3.2.27 The Department has also issued guidelines to institutions to assist in the management of Residents' Amenities Funds. As well as detailing the requirements of the Act, the guidelines list the types of expenditure which are considered to be appropriate in relation to these Funds.



Approval and monitoring of expenditure plans

3.2.28 As previously mentioned, legislative provisions require that annual plans for expenditure from each Residents’ Amenities Fund be prepared by the Secretary of the Department of Human Services. To ensure adherence to these plans, at the end of each financial year, the Department reviews the financial operation of these Funds to ensure that expenditure was within the overall budget. However, the audit review identified that:

- annual plans for the past 2 years were not approved until up to 7 months after the beginning of the financial year;
- details of the proposed expenditure funded from donations did not form part of the annual expenditure plans submitted to the Secretary for approval; and
- although annual expenditure from these Funds was within the overall approved budget, some items of expenditure exceeded the approved amount.

3.2.29 **There is a need for the Department to address these deficiencies in order to improve the management and control of the Residents’ Amenities Funds.**

Inappropriate expenditure

3.2.30 Residents’ Amenities Funds can only be used to acquire goods and services for the use of residents generally, and are not to be used for the normal operating activities and maintenance of institutions. However, audit found that these Funds had been expended on items that, based on the departmental guidelines, were considered inappropriate, which included:

- kitchenware for day-to-day use;
- hardware items such as stepladders used for maintenance purposes;
- gardening and landscaping supplies including top-soil, timber sleepers and computerised watering equipment;
- pool chemicals and maintenance costs for swimming pools;
- physiotherapy and speech therapy services; and
- outdoor furniture.

3.2.31 **Residents’ Amenities Funds should only be used for the purposes outlined in the governing legislation and the departmental guidelines, and not to supplement an institution’s operating budget.**

Viability of Funds

3.2.32 Leisure trips and outings which provide stimulation and variety are important activities for residents of institutions. Over many years, moneys from Residents’ Amenities Funds have been used to purchase suitable motor vehicles for these activities and to cover the operating expenses of the vehicles.



3.2.33 Vehicle operating expenses are now the major item of expenditure from the Funds and are rapidly consuming moneys remaining in the Funds. Indeed, at one institution, the Residents' Amenities Fund was recently depleted, due mainly to the costs of operating vehicles used for residents' activities. As a consequence, the institution will be required to fund the future costs of these vehicles from its own operating budget.

3.2.34 Given that vehicle costs are rapidly depleting amounts available in Residents' Amenities Funds, the Department needs to urgently review the ongoing viability of these Funds.

Inadequate control over assets

3.2.35 Over the years, many assets including vehicles, outdoor furniture, and electrical equipment have been purchased from moneys forming part of Residents' Amenities Funds. As previously mentioned, when institutions are closed, the Act requires that these assets be sold and proceeds from the sale returned to eligible persons. However, audit found that institutions did not have a systematic process to identify and record assets purchased with moneys from Residents' Amenities Funds.

3.2.36 Without adequate records, the Department was not able to assure the safeguarding of these assets. In addition, the Department was not in a position to readily identify assets purchased from these Funds and therefore ensure that proceeds on disposal of these assets are returned to eligible persons as required by the Act.

Distribution of Funds

3.2.37 On the closure of an institution, the Act requires that moneys standing to the credit of the respective Residents' Amenities Fund be distributed to residents who paid the residents' amenities levy within 2 years of the date the institution was officially closed, and to other persons who the Minister for Youth and Community Services determines should receive a share of the money "in the interests of fairness".

3.2.38 At the date of preparation of this Report, there were 2 institutions that were in the process of being closed, with all the residents relocated by September 1997. The amount held in these Residents' Amenities Funds totalled \$150 000. As there had been no contributions to these Funds by clients within the past 2 years, there is a need for the Department to formulate a method for the distribution of these funds in line with the requirements of the Act.



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

The context you provide at the beginning of the Report is somewhat narrow, as the Disability Program funds a range of other services in addition to residential care, including day programs, case management, and therapy services to name but a few.

I note the issues raised under the approval and monitoring section. The Department will ensure that future approvals are completed before the beginning of the financial year to which they relate, and that funds received through donations are included in expenditure plans. I think the implied criticism that some individual expenditure items exceeded the approved budget needs to be balanced by the fact that the approved budget is the best estimate available at the time expenditure plans are prepared. I would expect that local management should have sufficient flexibility to expend funds greater than the approved level, within the global budget, without immediate reference back to me. I am proposing that the program put in place a system that reconciles expenditure each year and ensures that items where the approved budget has been (or is likely to be) exceeded are highlighted in the following year's expenditure plans.

Issues surrounding inappropriate expenditure are particularly contentious. The Department will always provide a safe and secure environment for residents. However, local management and parents' associations often identify requirements above and beyond what the Department needs to provide and seeks funding for these initiatives through the Amenities Fund. The Guidelines issued by the Department state that the purchase of the following items is appropriate:

- *the purchase and maintenance of items of recreational and leisure equipment;*
- *the construction/improvement of leisure recreational facilities; and*
- *the provision of therapeutic services to groups of residents.*

As such, I would consider that purchases such as pool maintenance, gardening and landscaping, outdoor furniture and therapy services can be appropriate Amenities Fund purchases, particularly in the context of specific local circumstances. I would point out that many clients in receipt of care in these facilities have high dependency levels and complex needs. Therefore, for example, the ability to enjoy the sensory and visual stimulus provided by an appropriately landscaped area (as opposed to lawn or concrete paving) does add to quality of life enjoyed by clients. This is particularly the case when issues such as absconding behaviour (which means that some clients require more structured and supervised access to outdoor environments) are also considered.

I would also point out that the governing legislation does not provide detailed specification on appropriate purchases from the Amenities Fund. Nevertheless, I fully agree that the Amenities Fund should not be used to support a centre's operating budget, but should be used to purchase services over and above what is provided for day-to-day operational requirements.

Prior to your review, the Department recognised potential problems with the level of funding available in the Amenities Fund at a number of centres. To proactively address these matters, an internal divisional review group has been established to revisit policy and practice in this area, and develop options for the longer-term viability of these funds (or the identification of alternative funding sources.). It is anticipated that the outcome of this review will be available by the end of July 1998. Accordingly, the timeliness of your Report is welcomed, and the deficiencies that it has identified will be further addressed as part of this process.



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

The final issue I would like to raise is that the Report fails to mention that the audit did not find any evidence of fraud or misappropriation of moneys from the Fund. As such, I would consider it appropriate that the review report make mention of this point, particularly since it was this type of allegation, made to your Office, that provided the impetus for this review.



**SCHEDULE A
STATUS OF MATTERS RAISED IN PREVIOUS R EPORTS**

<i>Report</i>	<i>Subject</i>	<i>Status at date of preparation of this Report</i>
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MATTERS RESOLVED OR ACTION COMMENCED

DEPARTMENT OF HUMAN SERVICES

<i>Ministerial Portfolios, May 1997, p. 63.</i>	Hospitals need to develop strategies to deal with the decrease in revenue from private practice activities in order to avert adverse impacts on other hospital activities.	The decline in private practice fees generated from private patients has been largely offset by an increase in private practice income generated from the privatisation of hospital services such as radiology and pathology.
<i>Ministerial Portfolios, May 1997, p. 64.</i>	Significant improvements have been made in the accountability of private practice arrangements, however, problems persist in a number of long-standing arrangements.	Improved accountability procedures are incorporated into new arrangements when existing long-term arrangements expire.
<i>Ministerial Portfolios, May 1997, p. 65.</i>	Despite assurances provided by the Department of Human Services in 1991, neither the hospital industry nor the Department had evaluated the adequacy of the facility charges imposed on medical staff for use of hospital facilities for private practice purposes.	The facility charge is reviewed by individual hospitals when existing long-standing arrangements expire and new arrangements are negotiated.
<i>Ministerial Portfolios, May 1997, p. 65.</i>	Delays in achieving sign-off of health service agreements is of concern, particularly given that the issue was brought to the attention of Parliament in 1992.	The Department advises that as at 31 March 1998, 95 per cent of Hospitals had signed Health Services Agreements for 1997-98, which compares with 72 per cent at the same time in the previous year. The improvement is due to better business processes. The networking, for the first time, of the Department's Service Agreement Management System in 1998-99 will further improve efficiencies achieved in 1997-98.

**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>
COMPLETED AUDITS				
Department of Human Services	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	10 Sept. 1997	29 Sept. 1997
HEALTH				
Advanced Dental Technicians Qualifications Board	30 June 1997	" "	19 Sept. 1997	26 Sept. 1997
Ambulance Officers' Training Centre	30 June 1997	" "	8 Sept. 1997	30 Sept. 1997
Alexandra and District Ambulance Service	30 June 1997	" "	19 Aug. 1997	11 Sept. 1997
Ambulance Service Victoria -				
Metropolitan Region	30 June 1997	" "	21 Aug. 1997	4 Sept. 1997
North Eastern Region	30 June 1997	" "	4 Sept. 1997	19 Sept. 1997
North Western Region	30 June 1997	" "	25 Aug. 1997	19 Sept. 1997
South Eastern Region	30 June 1997	" "	8 Oct. 1997	23 Oct. 1997
South Western Region	30 June 1997	" "	20 Aug. 1997	26 Aug. 1997
Western Region	30 June 1997	" "	20 Aug. 1997	16 Sept. 1997
Anti-Cancer Council of Victoria	31 Dec. 1997	" "	24 Mar. 1998	30 Mar. 1998 (a)
Chiropodists Registration Board of Victoria	31 Dec. 1997	" "	17 Feb. 1998	27 Feb. 1998
Chiropractors and Osteopaths Registration Board of Victoria	30 June 1997	" "	21 Apr. 1998	28 Apr. 1998
Dental Board of Victoria	30 Sep. 1997	" "	20 Nov. 1997	1 Dec. 1997
Dental Technicians Licencing Committee	30 June. 1997	" "	19 Sep. 1997	26 Sep. 1997
Health Computing Service Victoria Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.53A.	28 July 1997	10 Oct. 1997
Infertility Treatment Authority	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	26 Sep. 1997	2 Oct. 1997
Medical Practitioners Board of Victoria	30 Sept. 1997	" "	10 Dec. 1997	12 Dec. 1997

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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>
COMPLETED AUDITS - continued				
HEALTH - continued				
Mental Health Review Board	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	19 Sept. 1997	26 Sept. 1997
Nurses Board of Victoria	30 June 1997	" "	20 Aug. 1997	2 Sept. 1997
Optometrists Registration Board of Victoria	30 June 1997	" "	11 Sept. 1997	19 Sept. 1997
Pharmacy Board of Victoria	30 June 1997	" "	26 Aug. 1997	4 Sept. 1997
Physiotherapists Registration Board of Victoria	30 June 1997	" "	5 Nov. 1997	6 Nov. 1997
Prince Henry's Institute of Medical Research	31 Dec. 1997	" "	24 Mar. 1998	26 Mar. 1998
Psychosurgery Review Board	30 June 1997	" "	17 Sept. 1997	26 Sept. 1997
Public Cemeteries -				
Anderson's Creek Cemetery Trust	31 Dec. 1997	" "	30 Mar. 1998	31 Mar. 1998
Ballaarat General Cemeteries Trust	31 Dec. 1997	" "	11 Mar. 1998	12 Mar. 1998
Bendigo Cemeteries Trust	31 Dec. 1997	" "	16 Mar. 1998	26 Mar. 1998
Cheltenham and Regional Cemeteries Trust	31 Dec. 1997	" "	27 Feb. 1998	17 Mar. 1998
Geelong Cemeteries Trust	31 Dec. 1997	" "	16 Mar. 1998	27 Mar. 1998
Keilor Cemetery Trust	31 Dec. 1996	" "	1 Aug. 1997	15 Aug. 1997
Keilor Cemetery Trust	31 Dec. 1997	" "	24 Mar. 1998	30 Mar. 1998
Mildura Cemetery Trust	31 Dec. 1996	" "	19 June 1997	1 July 1997
Templestowe Cemetery Trust	31 Dec. 1997	" "	26 Mar. 1998	31 Mar. 1998
Trustees of the Fawkner Crematorium and Memorial Park	31 Dec. 1996	" "	30 April 1997	9 May 1997
Trustees of the Fawkner Crematorium and Memorial Park	31 Dec. 1997	" "	23 Feb. 1998	26 Feb. 1998

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>
COMPLETED AUDITS - continued				
HEALTH - continued				
Trustees of the Lilydale Memorial Park and Cemetery	31 Dec. 1997	31. Oct. <i>Financial Management Act 1994</i> , s.46	26 Mar. 1998	31 Mar. 1998
Trustees of the Memorial Park Altona	31 Dec. 1996	" "	29 April 1997	28 May 1997 (a)
Trustees of the Memorial Park Altona	31 Dec. 1997	" "	19 Mar. 1998	30 Mar. 1998
Trustees of the Necropolis Springvale	31 Dec. 1997	" "	27 Mar. 1998	30 Mar. 1998
Trustees of the Preston Cemetery Trust	31 Dec. 1996	" "	1 Aug. 1997	4 Sept. 1997
Trustees of the Werribee Cemetery Trust	31 Dec. 1996	" "	6 Feb. 1998	6 April 1998
Victorian Health Promotion Foundation	30 June 1997	" "	15 Sept. 1997	17 Sept. 1997
PUBLIC HOSPITALS				
Alexandra District Hospital	30 June 1997	" "	19 Aug. 1997	8 Sept. 1997
Alpine Health	30 June 1997	" "	14 Jan. 1998	19 Mar. 1998 (a)
Bacchus Marsh and Melton Memorial Hospital	30 June 1997	" "	12 Aug. 1997	24 Sept. 1997
Bairnsdale Regional Health Service	30 June 1997	" "	27 Aug. 1997	28 Aug. 1997
Ballarat Health Services	30 June 1997	" "	21 Nov. 1997	2 Dec. 1997
Beaufort and Skipton Health Service	30 June 1997	" "	29 Aug. 1997	10 Sept. 1997
The Beechworth Hospital	30 June 1997	" "	25 Aug. 1997	11 Sept. 1997
Benalla and District Memorial Hospital	30 June 1997	" "	19 Aug. 1997	15 Sept. 1997 (a)
Bendigo Health Care Group	30 June 1997	" "	25 Aug. 1997	10 Sept. 1997 (a)
Bethlehem Hospital Incorporated	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.53A.	22 Aug. 1997	1 Sept. 1997
Birregurra and District Community Hospital (b)	31 Dec. 1996	31 Oct. <i>Financial Management Act 1994</i> , s.46.	16 Sept. 1997	1 Oct. 1997

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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>
COMPLETED AUDITS - continued				
<i>PUBLIC HOSPITALS - continued</i>				
Boort District Hospital	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	21 Aug. 1997	29 Aug. 1997
Bright District Hospital and Health Services (b)	31 Oct. 1996	" "	13 Nov. 1997	23 Dec. 1997
Caritas Christi Hospice Limited	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.53A.	25 Sept. 1997	28 Oct. 1997
Casterton Memorial Hospital	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	13 Aug. 1997	27 Aug. 1997
Central Wellington Health Service	30 June 1997	" "	15 Aug. 1997	25 Aug. 1997
Cobram District Hospital	30 June 1997	" "	16 July 1997	24 July 1997
Cohuna District Hospital	30 June 1997	" "	19 Aug. 1997	4 Sept. 1997 (a)
Colac Community Health Service (b)	31 Dec. 1996	" "	16 Sept. 1997	19 Sept. 1997
Colac Community Health Service	30 June 1997	" "	16 Sept. 1997	10 Oct. 1997
Coleraine and District Hospital	30 June 1997	" "	25 Aug. 1997	18 Sept. 1997
Corangamite Regional Hospital Services	30 June 1997	" "	6 Oct. 1997	20 Oct. 1997
Dental Health Services Victoria	30 June 1997	" "	26 Sept. 1997	1 Oct. 1997
Donald District Hospital	30 June 1997	" "	20 Aug. 1997	3 Sept. 1997
Dunmunkle Health Services	30 June 1997	" "	19 Aug. 1997	5 Sept. 1997
East Grampians Health Services	30 June 1997	" "	18 Aug. 1997	1 Sept. 1997
Echuca Regional Health	30 June 1997	" "	25 Aug. 1997	9 Sept. 1997
Edenhope and District Memorial Hospital	30 June 1997	" "	8 Aug. 1997	1 Sept. 1997
Far East Gippsland Health and Support Service	30 June 1997	" "	25 Aug. 1997	9 Sept. 1997

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>
COMPLETED AUDITS - continued				
PUBLIC HOSPITALS - continued				
Geelong Hospital	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	18 Aug. 1997	11 Sept. 1997
Gippsland Southern Health Service	30 June 1997	" "	20 Aug. 1997	9 Sept. 1997
Goulburn Valley Base Hospital	30 June 1997	" "	22 Aug. 1997	5 Sept. 1997
Grace McKellar Centre	30 June 1997	" "	25 Aug. 1997	2 Sept. 1997
Hamilton Base Hospital (b)	30 Nov. 1996	" "	30 June 1997	29 Aug. 1997
Hamilton Base Hospital	30 June 1997	" "	28 Aug. 1997	29 Aug. 1997
Hesse Rural Health Service	30 June 1997	" "	22 Sept. 1997	29 Sept. 1997
Heywood and District Memorial Hospital	30 June 1997	" "	28 Aug. 1997	29 Aug. 1997
Inglewood and Districts Health Service	30 June 1997	" "	25 Aug. 1997	8 Sept. 1997
Inner Healthcare Network	30 June 1997	" "	25 Aug. 1997	15 Sept. 1997
Kerang and District Hospital	30 June 1997	" "	25 Aug. 1997	2 Sept. 1997
Kilmore and District Hospital	30 June 1997	" "	12 Aug. 1997	25 Aug. 1997
Kooweerup Regional Health Service	30 June 1997	" "	29 Oct. 1997	5 Nov. 1997
Kyabram and District Memorial Community Hospital	30 June 1997	" "	11 Aug. 1997	18 Aug. 1997
Kyneton District Health Services	30 June 1997	" "	25 Aug. 1997	3 Sept. 1997
Latrobe Regional Hospital	30 June 1997	" "	21 Aug. 1997	29 Aug. 1997
Lorne Community Hospital	30 June 1997	" "	24 Sept. 1997	24 Sept. 1997
Maffra District Hospital	30 June 1997	" "	21 Aug. 1997	15 Sept. 1997
Maldon Hospital	30 June 1997	" "	25 Aug. 1997	5 Sept. 1997

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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>
COMPLETED AUDITS - continued				
PUBLIC HOSPITALS - continued				
Mallee Track Health and Community Service	30 June 1997	31 Oct. <i>Financial Management Act 1994, s.46.</i>	9 Sept. 1997	30 Sept. 1997
Manangatang and District Hospital	30 June 1997	" "	3 Sept. 1997	4 Sept. 1997
Mansfield District Hospital	30 June 1997	" "	21 Aug. 1997	5 Sept. 1997
Maryborough District Health Service	30 June 1997	" "	22 Aug. 1997	4 Sept. 1997
Mclvor Health and Community Services	30 June 1997	" "	22 Aug. 1997	29 Aug. 1997
Mercy Public Hospitals Inc.	30 June 1997	31 Oct. <i>Financial Management Act 1994, s.53A.</i>	20 Oct. 1997	24 Oct. 1997 (a)
Mildura Base Hospital	30 June 1997	31 Oct. <i>Financial Management Act 1994, s.46.</i>	22 Aug. 1997	29 Aug. 1997
Mt Alexander Hospital	30 June 1997	" "	21 Aug. 1997	15 Sept. 1997 (a)
Myrtleford District War Memorial Hospital (b)	31 Oct. 1996	" "	13 Nov. 1997	23 Dec. 1997
Nathalia District Hospital	30 June 1997	" "	26 Aug. 1997	4 Sept. 1997
North Eastern Healthcare Network	30 June 1997	" "	27 Aug. 1997	24 Sept. 1997
Numurkah and District War Memorial Hospital	30 June 1997	" "	5 Sept. 1997	9 Sept. 1997
O'Connell Family Centre (Grey Sisters) Inc.	30 June 1997	31 Oct. <i>Financial Management Act 1994, s.53A.</i>	2 Sept. 1997	29 Sept. 1997
Omeo District Hospital	30 June 1997	31 Oct. <i>Financial Management Act 1994, s.46.</i>	3 Sept. 1997	26 Sept. 1997
Otway Health and Community Services	30 June 1997	" "	19 Sept. 1997	24 Sept. 1997
Ouyen and District Hospital (b)	31 Dec. 1996	" "	9 Sept. 1997	30 Sept. 1997
Peninsular Healthcare Network	30 June 1997	" "	25 Aug. 1997	8 Sept. 1997

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>
COMPLETED AUDITS - continued				
PUBLIC HOSPITALS - continued				
Penshurst and District Memorial Hospital	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	23 Aug. 1997	27 Aug. 1997
Port Fairy Hospital	30 June 1997	" "	18 Aug. 1997	3 Sept. 1997
Portland and District Hospital	30 June 1997	" "	19 Aug. 1997	27 Aug. 1997
Queen Elizabeth Centre (Carlton)	30 June 1997	" "	13 Sept. 1997	20 Oct. 1997 (a)
Robinvale District Hospital and Health Services	30 June 1997	" "	27 Aug. 1997	18 Sept. 1997
Rochester and Elmore District Health Service	30 June 1997	" "	14 Aug. 1997	1 Sept. 1997
Seymour District Memorial Hospital	30 June 1997	" "	25 Aug. 1997	9 Sept. 1997
South Gippsland Hospital	30 June 1997	" "	17 Sept. 1997	3 Oct. 1997 (a)
Southern Healthcare Network	30 June 1997	" "	1 Sept. 1997	15 Sept. 1997
St Arnaud District Hospital	30 June 1997	" "	25 Aug. 1997	4 Sept. 1997
St Vincent's Hospital (Melbourne) Limited	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.53A.	24 Sept. 1997	13 Oct. 1997
Stawell District Hospital	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	14 Aug. 1997	3 Sept. 1997
Swan Hill District Hospital	30 June 1997	" "	27 Aug. 1997	11 Sept. 1997
Tallangatta Hospital	30 June 1997	" "	11 Aug. 1997	15 Aug. 1997
Tawonga District General Hospital (b)	31 Oct. 1996	" "	13 Nov. 1997	23 Dec. 1997
Terang and Mortlake Health Service	30 June 1997	" "	4 Aug. 1997	25 Aug. 1997
Timboon and District Hospital	30 June 1997	" "	1 Sept. 1997	2 Sept. 1997
Tweddle Child and Family Health Service	30 June 1997	" "	27 Aug. 1997	17 Sept. 1997

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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>
COMPLETED AUDITS - continued				
PUBLIC HOSPITALS - continued				
Upper Murray Health and Community Services	30 June 1997	31 Oct. <i>Financial Management Act 1994, s.46.</i>	3 Sept. 1997	25 Sept. 1997
Wangaratta District Base Hospital	30 June 1997	" "	21 Aug. 1997	5 Sept. 1997 (a)
Warracknabeal District Hospital	30 June 1997	" "	19 Aug. 1997	16 Sept. 1997 (a)
Warrnambool and District Base Hospital	30 June 1997	" "	18 Aug. 1997	27 Aug. 1997
Western Healthcare Network	30 June 1997	" "	13 Oct. 1997	13 Oct. 1997
West Gippsland Hospital	30 June 1997	" "	21 Aug. 1997	3 Sept. 1997
Western Highlands Health Service	30 June 1997	" "	2 Sept. 1997	15 Sept. 1997
Wimmera Health Care Group	30 June 1997	" "	19 Aug. 1997	29 Aug. 1997
Wodonga District Hospital	30 June 1997	" "	11 Aug. 1997	2 Sept. 1997
Women's and Children's Healthcare Network	30 June 1997	" "	25 Aug. 1997	17 Sept. 1997 (a)
Wonthaggi and District Hospital	30 June 1997	" "	15 Aug. 1997	27 Aug. 1997
Wycheproof and District Health Service	30 June 1997	" "	21 Aug. 1997	8 Sept. 1997
Yarram and District Health Service	30 June 1997	" "	14 Sept. 1997	1 Oct. 1997
Yarrawonga District Hospital	30 June 1997	" "	21 Aug. 1997	5 Sept. 1997
Yea and District Memorial Hospital	30 June 1997	" "	22 Aug. 1997	3 Sept. 1997



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>
INCOMPLETE AUDITS				
Psychologists Registration Board of Victoria	31 Dec. 1997	31 Oct. <i>Financial Management Act</i> 1994, s.46.		Audit substantially completed
Mildura Cemetery Trust	31 Dec. 1997	" "		Awaiting signed financial statements.
Preston Cemetery Trust	31 Dec. 1997	" "		" "
Werribee Cemetery Trust	31 Dec. 1997	" "		" "
West Wimmera Health Service	30 June 1997	" "		Audit substantially completed

(a) Qualified audit report issued.

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

Part 3.3

Infrastructure

KEY FINDINGS

Privatisation of bus services

- The Government’s Service Agreement with the National Bus Company was extended for more than 6 years without being subject to competitive tendering. *Paras 3.3.18 to 3.3.24*
- The revised payment structure incorporated in the new Service Agreement with the National Bus Company is likely to result in a decrease in future savings to be achieved by the arrangement. *Paras 3.3.25 to 3.3.27*
- The Department advised that it now considers the punctuality target level to be unreasonable and intends amending the private bus Service Agreement to lower the target levels. *Paras 3.3.28 to 3.3.30*

Public transport revenue and patronage levels

- An analysis of metropolitan rail patronage levels which assists in monitoring fare evasion was not possible due to the removal of passenger counters pending the installation and operation of the automated ticketing system. *Paras 3.3.35 to 3.3.40*

Docklands redevelopment arrangements

- During December 1997, the Mirvac Group was announced as the successful developer for the Yarra Water precinct of the Docklands redevelopment. *Paras 3.3.52 to 3.3.54*
- Under the arrangements, the Developer has the option of not proceeding with individual stages of the Development where there is insufficient market demand, or it is not viable to do so. Accordingly, the Development is dependent on market demand. *Paras 3.3.87 to 3.3.89*



KEY FINDINGS - continued

Docklands redevelopment arrangements - continued

- Where development stages relating to the Yarra Waters precinct proceed, the State has access to certain revenue sharing arrangements but does not have a right to share in any profits achieved by the Developer in excess of those anticipated.

Paras 3.3.84 to 3.3.85

- In determining the preferred developers, the Docklands Authority decided not to assign any weighting to its evaluation criteria to signify the relative importance of the various criteria which would have provided greater objectivity and transparency in the evaluation process.

Paras 3.3.70 to 3.3.73

Quality of external financial reporting in the local government sector

- A threefold improvement occurred in the timeliness of external financial reporting within the local government sector for the 1996-97 financial year.

Paras 3.3.90 to 3.3.94

- The quality of external financial reporting would be further enhanced through the development by the Office of Local Government of a best practice set of financial statements for use by all local government entities.

Paras 3.3.102 to 3.3.105

Operation of audit committees and internal audit within the local government sector

- The use of audit committees and internal audit has not been universally adopted across the local government sector and, as a consequence, corporate governance within the sector has been diminished compared with best practice.

Paras 3.3.110 to 3.3.123

Management of municipal business undertakings

- Of the \$1.4 billion of municipal services subjected to market testing, approximately one-third are provided by council in-house provider teams.

Paras 3.3.124 to 3.3.128

- In response to an audit survey, 12 councils with contract expenditure in excess of \$68 million were unable to identify the surpluses or losses generated during the 1996-97 financial year from their business unit operations. This management deficiency may expose ratepayer's funds to risk, particularly where such units provide services external to the council.

Paras 3.3.136 to 3.3.141

- Fifty per cent of councils who responded to an audit survey indicated that profits of council business units were shared with employees.

Paras 3.3.145 to 3.3.149





KEY FINDINGS - continued

Poor tender specifications

- The Macedon Ranges Shire Council awarded a contract relating to road maintenance services valued at \$5.2 million to a third party, commencing from January 1997.

Paras 3.3.152 to 3.3.167

- The terms and conditions of the contract have been subjected to differing interpretations by the contractor and the Council due to a lack of clarity of the contractual obligations of both parties, especially the expected type and standard of service to be provided.

Paras 3.3.155 to 3.3.173

- During February 1998, a Deed of Amendment was entered into by the parties clarifying various provisions of the initial contract and incorporating a variation to the contract totalling \$620 000 to enhance the level of service provided for unsealed roads.

Paras 3.3.155 to 3.3.176

Competitive tendering arrangements at the City of Greater Dandenong

- Notwithstanding the City of Greater Dandenong's tender evaluation panel's recommendation to award the contracts for horticultural, parks and sports services to an external provider, councillors formally resolved to award the contracts to the in-house provider.

Paras 3.3.177 to 3.3.189

- In December 1997, a writ was lodged in the Victorian Supreme Court on behalf of the external provider seeking damages against the Council in excess of \$1.5 million.

Paras 3.3.177 to 3.3.191



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 Department of Infrastructure, were subject to audit by the Auditor-General during the 1996-97 financial year.

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

<i>Ministerial portfolio</i>	<i>Entities subject to audit</i>
Planning and Local Government	Architects Registration Board of Victoria Building Control Commission CityWide Service Solutions Pty Ltd Docklands Authority Heritage Council Melbourne City Link Authority Municipal councils (78) Plumbing Industry Board Prahran Market Pty Ltd Regent Management Co. Regional Library Corporations (16) Urban Land Authority
Roads and Ports	Marine Board of Victoria Roads Corporation
Transport	Public Transport Corporation

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

PRIVATISATION OF BUS SERVICES

Contracting-out of bus services

3.3.4 The Auditor-General’s May 1994 *Report on Ministerial Portfolios* commented on the contracting-out of certain metropolitan bus services previously provided in-house by the Public Transport Corporation (PTC). In that Report, audit outlined the process followed for the selection in August 1993 of the service provider, National Bus Company, which was awarded 80 per cent of the bus services previously provided by the PTC, with the remaining 20 per cent retained in-house by the PTC. The contract awarded to the National Bus Company related to the provision of bus services along certain allocated routes for a period of 7 years, at an overall cost to the PTC estimated at the time to be \$168 million.



3.3.5 Prior to the commencement of the service, the Minister for Public Transport announced that this privatisation would achieve annual savings to the State of around \$10 million. Audit conducted a review of the management of the contract and the outcomes achieved from its implementation.

Contractual arrangements

3.3.6 The principal arrangements for the operation of the bus services were set out in a Service Agreement entered into in November 1993 between the operator and the PTC, with the operator commencing provision of the service in December 1993. The main features of the Service Agreement were as follows:

- the operator to provide bus services along certain allocated routes in accordance with stipulated standards;
- the operator to collect fares from the sale of both Met tickets and the operator’s bus tickets;
- the operator to honour valid time-based Met tickets presented by customers; and
- the PTC to reimburse the operator on a monthly basis for fares forgone as a result of selling concession tickets and accepting Met tickets, based on independent surveys and an independent analysis of passenger statistics.

3.3.7 In addition, the PTC and the operator entered into a separate agreement in December 1993, whereby the operator agreed to lease 232 buses from the PTC over a 2 to 5 year period, with an option to purchase the buses at the end of the lease term. The lease agreement terminated in December 1996 when the operator purchased the vehicles at a price of \$1.5 million, with the PTC incurring a loss on sale of \$217 000.

3.3.8 Fees payable by the PTC to the operator in respect of service provision were made in the past after taking account of fares retained and bus lease payments owed by the operator.

3.3.9 In April 1994, the former Department of Transport became responsible for administering the Service Agreement for the provision of bus services as a result of an amendment to the *Transport Act* 1983.

Payments to the operator

3.3.10 Under the original Agreement, the Department was required to reimburse the operator for sales of concession fares and the acceptance of Met tickets, based on the number of passengers carried and the distance travelled by passengers.

3.3.11 Each quarter, an independent firm conducted surveys of bus passengers to determine the class of passenger travelling (e.g. adult, concession or student) and the average distance travelled on each route serviced by the operator. The information was used to verify passenger information provided by the operator and to develop a template of notional sections travelled for each passenger type, which was then converted to an equivalent fare that would have been charged had the passenger purchased a bus-only ticket. The fare was then applied to passenger information provided by the operator to determine the amount of the reimbursement to the operator.



3.3.12 The cost of the independent surveys and their subsequent analysis for the period December 1993 to March 1998 was \$400 000, which has been shared equally by the operator and the Department.

3.3.13 Prior to the commencement of the Service Agreement, it was anticipated that this arrangement would generate no additional cost to the Government, other than reimbursements for concession fares, Met tickets and associated administration costs. The audit review indicated that a number of reimbursements for administration costs were made by the Department to the operator, as outlined below:

- As the operator is required to sell Met tickets, the Department reimburses the operator for half of the estimated costs incurred for staff to maintain and submit records relating to Met ticket sales. **For the period since the commencement of the Agreement to June 1997, the Department subsidised the operator \$467 000 in relation to these costs;**
- The Department reimbursed the operator for costs incurred in relation to the supply, installation and maintenance of ticketing machines used on buses until introduction of the automated ticketing system. **A total of \$509 000 has been paid to June 1997, with payments scheduled to cease upon the full implementation of the automated ticketing system;** and
- The cost of cash counting, collection and banking of Met tickets is reimbursed to the operator. **For the period since commencement of the Agreement to June 1997, the Department has subsidised the operator \$201 000 in regard to the costs associated with cash collection.**

Revision of bus contract

3.3.14 As previously indicated, the Service Agreement provided for fees to be paid to the operator based on the number of passengers carried and the distance travelled by passengers. This arrangement differed from those in place with other private bus operators which were based, in part, on payment of a rate per kilometre travelled and which had attracted criticism from the Industry Commission, the Victorian Commission of Audit and this Office in successive Auditor-General's Reports as lacking incentives for operators to minimise costs and improve services.

3.3.15 In October 1995, the *Public Transport Competition Act 1995* was proclaimed with the main purpose of improving the operation of road-based public transport through the accreditation of bus operators and the implementation of a system of service contracts for bus operators. Pursuant to the objectives of the Act, an inter-departmental Bus Contracts Committee was formed in late 1995 to review the contract model applying to other private bus operators. The Committee, comprising the Parliamentary Secretary for Transport, Roads and Ports and representatives from the Department of Treasury and Finance, the Department of Infrastructure, the Department of Premier and Cabinet and the Bus Proprietors' Association, appointed a consultant to develop a new incentive-based contract model.



3.3.16 The consultancy involved the development of benchmark models of bus operating costs and the identification of an appropriate rate of return. The contract model developed by the Committee was devised to provide an incentive to operators to increase patronage and featured a variable reimbursement to be paid on the basis of passenger boardings and passenger kilometres.

3.3.17 Negotiations surrounding the implementation of the revised contracts, which were for a period of 10 years, were finalised with the other private bus operators in late 1997.

Revised National Bus Company Service Agreement

3.3.18 As previously indicated, the Service Agreement between the Department and the National Bus Company had an expiry date of December 2000. However, during negotiation of the revised contracts with other private bus operators, the Company approached the Department expressing concern at the apparent inequity that would result should all operators other than National Bus Company be offered 10 year contracts. The Department subsequently offered the operator the opportunity to negotiate a new Service Agreement based on the revised contract model.

3.3.19 **The new Agreement with the National Bus Company, which commenced in March 1997, is to operate for a period of 10 years at an estimated overall cost to the Department of \$240 million. Hence, the arrangement between the operator and the Department, which commenced in November 1993 and was due to cease in December 2000, has been extended to March 2007.**

3.3.20 In accordance with the model developed by the Bus Contracts Committee, the new Agreement incorporates a revised payment structure whereby the Department must make the following payments to the operator:

- a fixed payment, initially established at \$3.3 million; and
- variable payments whereby the operator is reimbursed on a monthly basis for fares foregone as a result of selling concession tickets and accepting Met tickets, with these payments continuing to be calculated with reference to independent survey results.

3.3.21 **Specifically, the rates at which the operator is to be reimbursed include:**

- a profit margin calculated at 6.5 per cent of agreed operating costs; and
- a return on capital calculated at 26.8 per cent of an agreed fleet capital value.

3.3.22 **Annual payments are capped at \$28 million, with this amount indexed every 6 months.**

3.3.23 Audit was advised that the Department did not approach the Victorian Government Purchasing Board to obtain approval for the revisions to the Service Agreement. As the original Service Agreement had been negotiated by the PTC, which was not required to obtain Board approval, the Department considered it unnecessary to approach the Board over the changes to the arrangement.



3.3.24 In audit opinion, in the light of the changes to the Service Agreement, a significant variation to the original Agreement has occurred. Accordingly, it would have been a preferable course of action for the Department to seek the approval of the Victorian Government Purchasing Board for the new arrangements prior to executing the new Service Agreement.

Payments to operator for providing the service

3.3.25 Since 1 July 1994 the operator has received the fees outlined in Table 3.3B under the Service Agreement.

TABLE 3.3B
PAYMENTS TO OPERATOR, JULY 1994 TO MARCH 1998 (a)
 (\$million)

<i>Financial year</i>	<i>Gross claims made by operator</i>	<i>Amounts retained by operator</i>	<i>Net payment to operator</i>
1994-95	21.6	5.8	15.8
1995-96	23.9	7.2	16.7
1996-97	23.8	8.0	15.8
1997-98 (to March 1998)	19.4	4.2	15.2
Total	88.7	25.2	63.5

(a) Payments made to the operator from the commencement of the Agreement in November 1993 to June 1994 were not available.

3.3.26 The Department has advised that for the financial year ended 30 June 1998 it is anticipated that the operator will be paid \$20.3 million under the arrangement, representing a 28 per cent increase since the 1994-95 financial year. This increase is due to the impact of the revised Service Agreement, CPI escalation factors allowed for in the original Agreement and the termination of the bus lease.

3.3.27 As indicated earlier in this Report, prior to the privatisation of the bus services, it was estimated that the arrangement would result in net savings to the State of \$10 million, based on projected annual payments of \$18 million to the operator. Actual net payments made by the Department to the operator for the financial years 1994-95 to 1996-97 have been below the initial estimate. **However, the revised payment structure incorporated in the new Service Agreement is likely to result in a decrease in the future savings to be achieved by the arrangement.**

Monitoring of service delivery

3.3.28 To encourage the provision of timely services, the Service Agreement stipulates that:

- scheduled journeys must not depart earlier than scheduled;
- a minimum 95 per cent of journeys must operate no more than 5 minutes late; and
- a minimum 99 per cent of scheduled services must operate.

3.3.29 Table 3.3C outlines service delivery and punctuality data relating to the operator as provided by the Department for the period July 1995 to December 1997.

TABLE 3.3C
SERVICE DELIVERY AND PUNCTUALITY
(per cent)

<i>Period</i>	<i>Service delivery</i>		<i>Punctuality</i>	
	<i>Target</i>	<i>Actual</i>	<i>Target</i>	<i>Actual</i>
1995-96	99	99.34	95	92.7
1996-97	99	99.81	95	91.7
1997-98 (to Dec. 1997)	99	99.83	95	91.2

3.3.30 The table indicates that reliability of service delivery has been excellent, however, punctuality remains below the established target levels since contracting-out of the service. Indeed, service punctuality has marginally deteriorated over the period of the arrangement. **Audit was advised by the Department that it now considers the punctuality target levels to be unreasonable and intends amending the Service Agreement to lower the target levels.**

Patronage levels

3.3.31 Audit conducted an analysis of patronage levels based on information supplied by the Department. Table 3.3D outlines the relevant details since the 1993-94 financial year.

TABLE 3.3D
PATRONAGE LEVELS
(million)

<i>Period</i>	<i>Patronage (boardings)</i>
1993-94 (a)	12.6
1994-95	14.5
1995-96	15.3
1996-97	14.6
1997-98 projected	13.9

(a) Includes 6 months of service operations by the PTC prior to contracting-out.

3.3.32 The analysis shows an overall 15 per cent improvement in patronage for the period 1993-94 to 1996-97. However, patronage levels have steadily declined since the 1995-96 financial year.

3.3.33 The Department's quarterly monitoring reports indicate that the operator has attempted to reverse this trend by revising timetables and route structures, operating newer vehicles with better carrying capacity and improved performance reliability, and introducing a promotional campaign. However, as indicated above, patronage levels continue to fall below expectations and, to date, the aforementioned strategies have had minimal effect.

Further contracting-out of services

3.3.34 In December 1997, the Minister for Transport announced that the remaining bus services provided by the PTC would be contracted-out to the consortium Melbourne Bus Link. It is anticipated by the Department that the 10 year contract will provide savings averaging at least \$2.5 million per annum over the period of the contract and will lead to improved service provision.

□ *RESPONSE provided by Chief Executive, Public Transport Corporation*

The Report indicates that a revised payment structure in the contract is likely to decrease future savings. As your Office is aware, this revision brings the National Bus Company (NBC) contract into line with recommendations arising from the Government Bus Contracts Committee review of bus industry benchmarks and which applied to all other private route bus contracts in metropolitan Melbourne. The revised contract with NBC will, as a minimum, continue to deliver in real terms the \$10m pa savings originally estimated and provided for in the PTC \$245m reform program.

The Report indicates that the Department considers that the contracted punctuality targets should be reduced. A high proportion of NBC services are to and from the City. On these routes, some services are experiencing road traffic congestion conditions which are impacting on punctuality. Originally, a single punctuality target was set for all routes. Consequently, the Department now considers that new targets should be set to properly allow for road condition differences between these routes and other routes that do not have similar operational conditions.

Your Office considers that it would have been preferable for the recent revisions to the NBC contract to have been put to the Victorian Government Purchasing Board (VGPB) prior to execution. As indicated to your Office, the original contract did not fall within VGPB jurisdiction and consequently it was considered inappropriate to refer the variations to the VGPB. Further, as the price variation was well within the original contingency allowance and the extension of the contract period by three years resulted from the recommendations of the Government Bus Contracts Committee, it is considered that both variations had satisfied appropriate approval processes.

Your Report indicates that notwithstanding NBC's high service standards, patronage levels have declined since 1995-96. Clearly, the exceptional patronage growth achieved by the Company up to 1995-96 (i.e. some 21 per cent increase after 2 years) could not be sustained. Annual patronage up to and including the current year (1997-98) has averaged more than 15 per cent above the level achieved by the PTC and has exceeded original expectations. The contract gives NBC every incentive to increase patronage and the Company is continually re-examining and restructuring its services to maximise patronage.



PUBLIC TRANSPORT REVENUE AND PATRONAGE LEVELS

3.3.35 The Auditor-General's previous *Reports on Ministerial Portfolios* have commented on patronage and revenue trends associated with Public Transport Corporation (PTC) operations. It was my intention to provide the Parliament with an update of the more recent patronage and revenue trends, covering the early phase of implementation of the new automated ticketing system. However, due to the incompleteness of information retained by the PTC regarding metropolitan rail patronage, in that information was only available for the period July to November 1997, I am unable to provide information on the patronage trends.

3.3.36 Table 3.3E illustrates the PTC's revenue levels for Met and V/Line services, for the period July 1994 to March 1998.

TABLE 3.3E
REVENUE LEVELS, JULY 1994 TO MARCH 1998 (a)
((\$million)

	1994-95	1995-96	1996-97	July 1996 to March 1997	July 1997 to March 1998
Revenue	228.5	238.9	249.8	186.1	191.8

(a) Relates to Met and V/Line services.

3.3.37 The audit analysis revealed that revenue levels have increased by approximately 4 per cent each year since the 1994-95 financial year. However, this trend has moderated over recent months, with revenue increasing by 3 per cent since July 1997. The PTC attributes the decline to the effect of increased industrial disputes within the PTC.

3.3.38 As mentioned above, audit was unable to conduct an analysis of patronage levels. Metropolitan rail patronage levels were previously compiled using automatic counters located in barriers at Central Business District railway stations. A statistical model was then applied to the data compiled by the counters in order to calculate metropolitan rail patronage.

3.3.39 In December 1997, the barriers in which the automatic counters were located were withdrawn in anticipation of the installation of automated ticketing system equipment. However, some of the new equipment, which will collect passenger data, was not fully operational from the date of its installation. Furthermore, audit was advised that the model to be applied in the calculation of patronage levels had not been finalised and as a result it was anticipated by the PTC that reliable patronage information will not be available until June 1998.

3.3.40 Given that metropolitan rail patronage in the past has constituted around half of the PTC's patronage, it is recommended that the PTC give priority to finalising its method of measuring rail patronage, as a means of monitoring fare evasion.

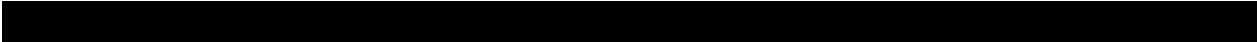


□ **RESPONSE** provided by Chief Executive, Public Transport Corporation

The Corporation regards the finalisation of a method for measuring rail patronage on the metropolitan rail system as a major priority.

As such, the implementation of the automated ticketing system has been planned to provide accurate statistical data on patronage.

Accurate patronage data will provide invaluable in the Corporation's efforts to minimise fare evasion. Continued growth in the Corporation's revenue is pleasing despite the significant effect of increased disputes during the past financial year.



THE DOCKLANDS REDEVELOPMENT

3.3.41 The Melbourne Docklands comprises an area covering some 220 hectares of land and water which is located beyond the Spencer Street railway station. Given its proximity to the Melbourne Central Business District and the Yarra River, the area has been identified as suitable for redevelopment by successive Victorian Governments.

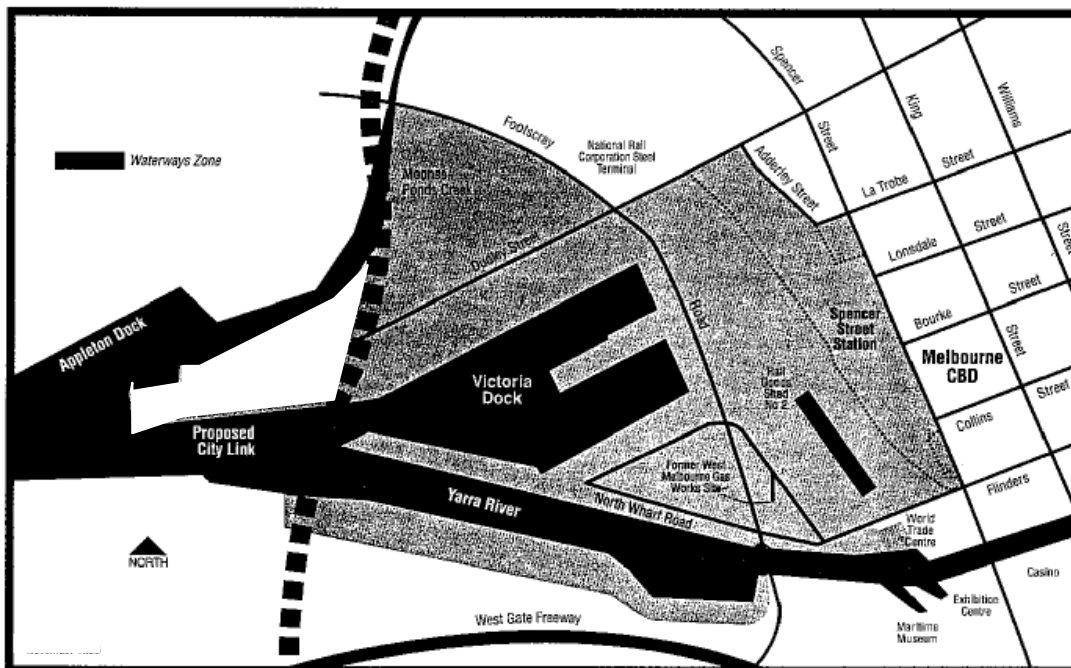
3.3.42 The Docklands Taskforce, comprising representatives of a number of public sector agencies and private sector consultants, was formed in early 1990 to explore alternatives for the use of the Docklands and formulate a long-term strategy for development. Three key reports titled *Melbourne Docklands strategic Options*, *Docklands Strategy* and the *Melbourne Docklands: Strategy for Redevelopment* were produced by the Taskforce between 1990 and 1992.

3.3.43 In 1991, the Docklands Authority was formed to:

- investigate development options for the Melbourne Docklands;
- prepare and implement development strategies; and
- promote and encourage the involvement of the private sector in the redevelopment of the area without long-term government funding and minimum practicable risk to the State.

3.3.44 The Authority undertook planning and research over a period of approximately 3 years, culminating in the State Government's acceptance of the Authority's strategy in August 1995, which identified 7 precincts within the Melbourne Docklands for redevelopment, currently known as Business Park, Victoria Harbour, Yarra Waters, Batman's Hill, Technology Park, Stadium and West End. The proposed redevelopment of the Docklands area is a massive project to be undertaken over many years, covering an area larger than the Central Business District itself. Chart 3.3G highlights the proposed redevelopment area at the Docklands, represented by the shaded area.

**CHART 3.3G
MELBOURNE DOCKLANDS REDEVELOPMENT AREA**



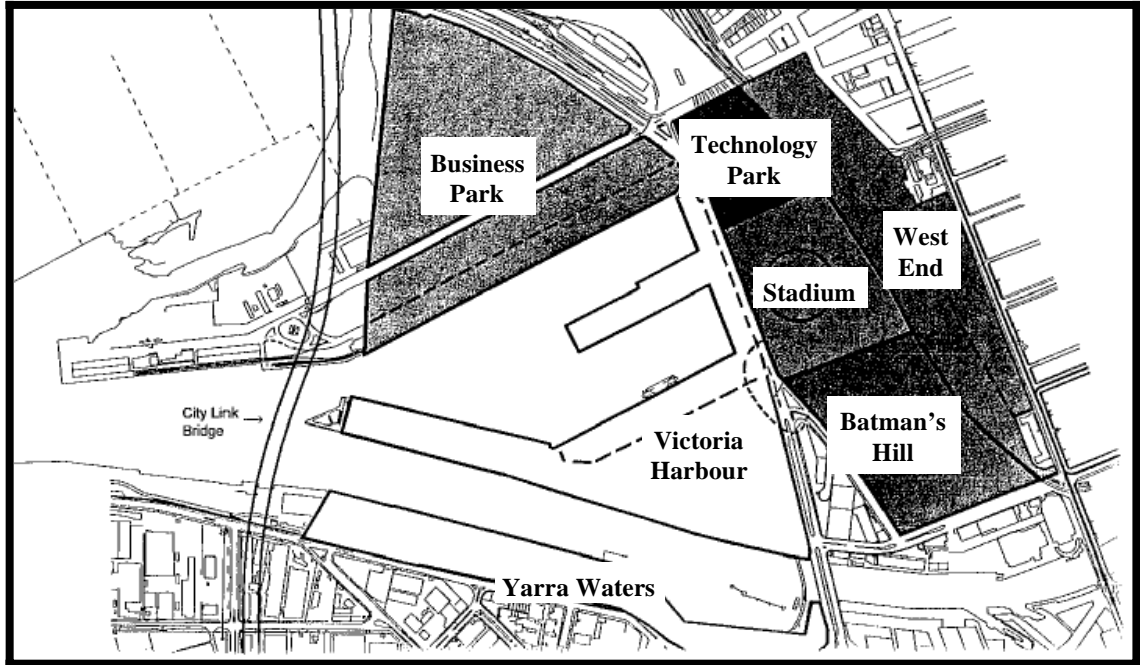
3.3.45 The Melbourne Docklands redevelopment was marketed by the Authority across Australia and overseas during 1996. Key features of the marketing strategy, which was designed to encourage developers to bid for the right to acquire and redevelop one or more of the precincts, included:

- a flexible design framework and planning scheme arrangement, which at a later stage included the Docklands Stadium as a major feature;
- the potential for developers to receive freehold title to the land on a staged basis;
- the opportunity for developers to defer the acquisition and development of land over lengthy periods, subject to market demand;
- the ability of developers to deal with a single co-ordinating public sector agency which is solely focused on the promotion of the redevelopment of the Docklands;
- provision of trunk infrastructure by the State, funded through the proceeds of certain land sales;
- packaging of land on a precinct basis which would provide developers with increased control of development within individual precincts, with less threat of competitive developments on adjacent land; and
- the State's acceptance of specified risks.



3.3.46 Chart 3.3H illustrates the locality and size of the 7 development precincts.

**CHART 3.3H
DOCKLANDS DEVELOPMENT PRECINCTS**



3.3.47 Table 3.3I outlines the current status of the agreed or proposed developments within each of the development precincts.



**TABLE 3.3I
THE DOCKLANDS DEVELOPMENT PRECINCTS**

<i>Precinct</i>	<i>Planned development</i>
Stadium	<ul style="list-style-type: none"> • Two year development of a multi-purpose sport and entertainment stadium incorporating a retractable roof.
Yarra Waters	<ul style="list-style-type: none"> • Twelve year development comprising some 1 900 medium to high-density apartments and townhouses, a marina and commercial and retail areas.
Business Park	<ul style="list-style-type: none"> • Two year development comprising a theme park, working film studio, cinema megaplex and retail outlets; and • Ten year development comprising 1 500 dwellings, commercial office space, retail space and a marina.
Victoria Harbour	<ul style="list-style-type: none"> • Eight year development comprising an export exhibition area, healthcare complex, marina, medium-low density residential development consisting of 1 340 units, hotels and entertainment facilities; or • Twelve year development comprising private and public universities, a telecommunications hub, a hotel, 1 500 residential apartments, office space, a marina, restaurants and a maritime museum.
Batman’s Hill	<ul style="list-style-type: none"> • Five year development comprising a 560 metre high rise tower (including 258 residential apartments, a 300 room hotel and 41 floors of commercial office space and retail activities), extension of Collins Street into the Docklands and precinct park; or • Six year development comprising commercial office space, a roller-dome stadium, apartments, entertainment area and a permanent technology exhibition.
Technology Park	<ul style="list-style-type: none"> • Ten year development comprising a “technology and knowledge” facility, apartments, retail and an exhibition and conference centre.
West End	<ul style="list-style-type: none"> • Development bids are yet to be called for this precinct.

3.3.48 The Authority and its expert advisers have identified several economic benefits for the State arising from the redevelopment of the Docklands, including:

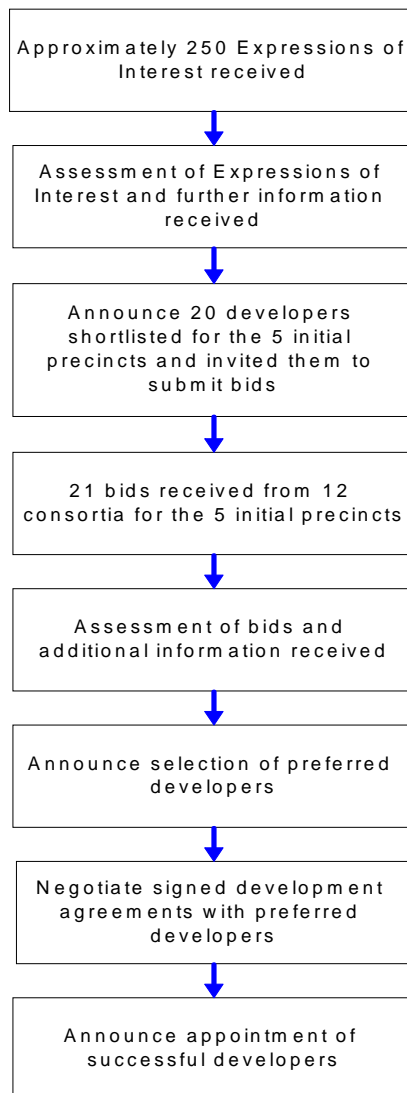
- substantial investment in public infrastructure;
- massive development financed by the private sector, predominantly residential, but also including retail, commercial, entertainment and improved public space and riverbank access;
- decontamination of the Dockland’s area;
- direct and indirect employment opportunities, both during construction and post-construction periods; and
- increases in tourism.

Determination of developers

3.3.49 The process adopted by the Authority for the selection of developers of individual precincts, as outlined in Chart 3.3J comprises:

- seeking expressions of interest;
- short-listing of entities which submitted expressions of interest and inviting the submission of bids from the short-listed developers;
- assessment of bids and the nomination of preferred developers; and
- further analysis and negotiation with the preferred developers leading to the announcement of the successful developers and the execution of the transaction documentation.

**CHART 3.3J
PROCESS FOR THE SELECTION OF DEVELOPERS**





3.3.50 Extensive documentation was developed by the Authority and made available to interested parties during 1996 and 1997 to assist in their understanding of the project and the formulation of their proposals. The documentation, which comprised several hundred individual reports and other documents, included:

- background information on the Docklands precincts;
- an Information Memorandum which acted as a guide to the information provided and the bidding and assessment processes;
- a Commercial Terms Summary which set out the main commercial terms which would be included in the development agreement, land sale agreement and ancillary agreements;
- a Form of the Bid Proposal document which described the bid format, documentation and analysis information required to be provided to the Authority to assist in assessing developers' bids;
- a Risk Allocation Table which set out details of the intended allocation of risks between the State and the developers;
- the proposed Development Agreement and Land Sale Contract;
- the conceptual planning and design framework; and
- planning scheme details.

3.3.51 While a limited number of documents were available for public inspection, potential developers had access to extensive documentation. Each developer was required to enter into a disclosure and confidentiality deed with the Authority prior to being provided with access to the detailed bid documentation and information.

The initial 5 precincts

3.3.52 An invitation for expressions of interest was extended by the Authority to potential developers, which resulted in approximately 250 submissions being received by the end of May 1996. Following a short-listing of the expressions of interest, in October 1996, 20 developers were invited to submit detailed bid proposals by April 1997 for one or more of the 5 initial precincts, being Business Park, Victoria Harbour, Yarra Waters, Batman's Hill and Technology Park. The Authority set a target date of October 1997 to announce all successful developers and to execute contractual documentation.

3.3.53 Following an assessment of the bids, the Authority in September 1997 announced the preferred developers for all precincts, with one preferred developer announced for the Technology Park precinct while 2 preferred developers were announced for each of the remaining 4 initial precincts.

3.3.54 During December 1997, the Mirvac Group was announced as the successful developer for the Yarra Waters Precinct and in March 1998 the Entertainment City Consortium and Yarra Nova Consortium were awarded the development of adjacent parcels of land within the Business Park Precinct subject to certain conditions. At the date of preparation of this Report, the successful developers for the other precincts had not been determined.

.....

The Stadium

3.3.55 During October 1996, expressions of interest were invited for the development of a multi-purpose sport and entertainment stadium in the Stadium precinct. In December 1996, following an evaluation of these expressions of interest, 10 consortia were short-listed and invited to submit proposals for the financing, development, construction, lease and transfer of the stadium.

3.3.56 In March 1997, following the assessment of bids received, 4 developers were invited to prepare detailed proposals for the Stadium precinct, comprising the stadium itself and the remainder of the precinct. The short-listed developers for the Technology Park and Batman’s Hill precincts were also advised that they could bid for the remainder of the Stadium precinct or the northern or southern section, respectively.

3.3.57 It was announced in September 1997 that Docklands Stadium Consortium led by Baulderstone Hornibrook, KPMG, Merrill Lynch, Westpac, the Seven Network and News Ltd was the successful bidder for the Stadium. Construction of the facility commenced later that month.

Trunk infrastructure

3.3.58 In November 1996, the Authority called for expressions of interest for the provision of trunk infrastructure for the whole of the Docklands redevelopment area. Trunk infrastructure comprises major road and traffic works, major pedestrian and bicycle links, tram works, major utilities (electricity, gas, water, sewerage and telecommunications), major stormwater drainage, special and other works including relocation of the Public Transport Corporation businesses, public open space, waterfront precincts and human services (health, education and community facilities). On completion of the works, ownership of the trunk infrastructure will transfer to various government agencies such as VicRoads and the Melbourne Water Corporation, and certain private sector entities.

3.3.59 During March 1997, following the short-listing of expressions of interest received, 5 developers were requested to submit bids for the financing and building of the trunk infrastructure and, in March 1998, the Transfield Powercor Consortium was appointed as the successful bidder.

Yarra Waters precinct - Audit review

3.3.60 At the time of preparation of this Report, the Authority had established contractual arrangements for the redevelopment of the Yarra Waters and Business Park precincts, and for the construction and operation of the Stadium.



3.3.61 An audit review was conducted to provide the Parliament with information on the progress made to date on the redevelopment of the Docklands, including the process applied by the Authority for the selection of the developers of the Yarra Waters precinct. Matters considered during the audit review included:

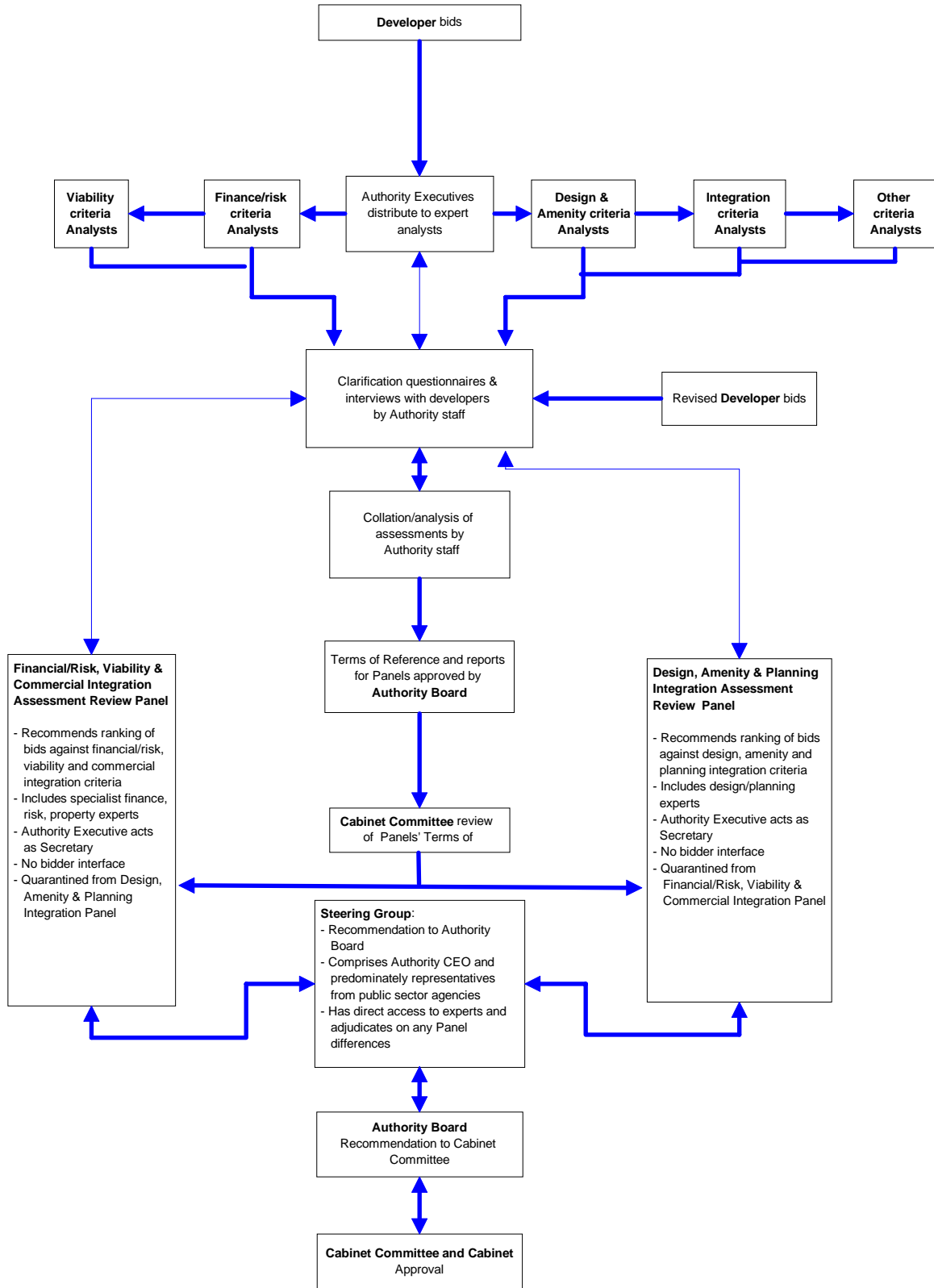
- developer evaluation, selection and other related processes;
- the risks and exposures to the State resulting from the development arrangements;
- benefits of the new arrangements for the State; and
- the identification of any indemnities, other undertakings or incentives provided to the developers or other parties which may have impacted on development arrangements, or may result in future financial exposures to the State.

3.3.62 It is my intention to provide further comment on the redevelopment arrangements for the Docklands, including the Stadium arrangements, in subsequent Reports to the Parliament.

Bid evaluation and negotiation process

3.3.63 Chart 3.3K outlines the bid evaluation process used by the Authority to identify preferred and successful developers.

**CHART 3.3K
BID EVALUATION AND NEGOTIATION PROCESS**





3.3.64 Chart 3.3K highlights the key participants in the bid evaluation and negotiation process and indicates their inter-relationships. It also highlights that the bid evaluation and negotiation process is mainly supported by analyses conducted by independent experts and that it is a dynamic process which responds to evolving bids by developers.

3.3.65 Once preferred developers have been identified, the process includes concurrent contractual documentation negotiation with each preferred developer.

Probity processes

3.3.66 The Authority placed significant importance on achieving best practice in its probity processes and, in conjunction with its main Probity Adviser and Probity Auditor, developed extensive probity processes in order to ensure:

- integrity in all evaluation and selection processes;
- all respondents were assessed objectively and consistently;
- all confidential information is protected;
- any potential perceived or actual conflicts of interest were addressed; and
- transparency of process.

3.3.67 The key elements of the Authority’s probity processes included:

- conduct of probity briefings for all those involved in the bid evaluation and decision-making processes;
- issue of codes of conduct for employees, expert analysts and members of the Authority in relation to actual or potential conflicts of interest, confidentiality, declaration of interests and other probity related matters;
- conduct of probity investigations of developers;
- issue of prescribed procedures for the handling of developer questions during the preparation of bids;
- maintenance of a register of interests containing relevant directorships, share holdings, and interests of Authority members; and
- conduct of probity audits of the various stages of the bid process.

3.3.68 The Authority’s probity process requires the Probity Auditor to undertake probity audits and issue a report at the end of each phase of the project. Probity audit reports sighted by audit found that no issues of probity remained outstanding, with the bidders evaluated and ranked fairly against the selection criteria and all bidders accorded fair and equitable treatment. However, audit was advised that it was decided not to prepare written probity audit reports for all phases of the bidding process, instead verbal reports were provided during each phase of the bidding process. In addition, audit was advised by the Authority that:

- the Probity Auditor attended all critical meetings of the assessment review panels, Steering Group and Board and that resolutions were documented at each phase of the process;



- throughout the bidding process, the Authority held intensive consultations with its Probity Auditor, Probity Adviser and outside legal advisers, all of which were documented through memoranda, letters or file notes; and
- a formal written probity audit report was prepared at the end of the expressions of interest phase and after the selection of the successful developer.

3.3.69 Audit is of the view that written probity audit reports, detailing work done, any exceptions noted and conclusions reached should have been prepared for all phases.

Evaluation criteria

3.3.70 The Authority established the following principal criteria to be used to evaluate development proposals for the 5 initial precincts:

- *Design and amenity* - concerned with the intent and quality of the design and amenity of the Docklands and Melbourne generally. Consideration is also given to the identity of design consultants, their demonstrated skills and examples of previously built projects;
- *Integration* - concerned with the integration of proposals within individual precincts, and the Docklands as a whole, and with Melbourne in general. Infrastructure and transport links, planning and design, and sequencing of the development are also considered;
- *Financial/Risk* - concerned with the price offered and the identification, management and allocation of project and financial risks, including methods for addressing these risks. It also focuses on the financial offer including the land price, trunk infrastructure requirements, land decontamination requirements, art in public spaces and other contributions;
- *Viability* - concerned with the market and financial viability of the proposal itself in the overall context of the Docklands and Melbourne’s economic potential; and
- *Other factors* - concerned with any other elements relevant to a developer’s proposal which have a bearing upon the proposed development, including any risks or benefits to the State or the Authority flowing from the development.

3.3.71 The Authority decided not to assign any weighting to its evaluation criteria to signify the relative importance of the various criteria. It is implicit in the approach taken by the Authority that all criteria, some of which are conflicting, were assigned equal weighting and that judgements over the comparative importance of the criteria and setting of “hurdle” ratings were made by members of the assessment review panels, the Steering Group and the Authority Board on a case-by-case basis. The assignment of weightings to evaluation criteria, which is the Victoria Government Purchasing Board’s preferred best practice for the analysis of bids, has the advantage of providing greater objectivity and transparency in the evaluation process as it:

- provides a more objective support or rationale for making decisions on bids;
- helps to focus attention on the most important aspects of the bid by both the Authority and bidders;
- lessens the judgement required to balance competing scores in different criteria;



- encourages a more consistent treatment of the relative importance of evaluation criteria; and
- enables a clearer linkage to the Authority’s objectives by placing emphasis on those criteria most closely linked to the Authority’s objectives for the redevelopment.

3.3.72 The use of weighted scores for each criteria does not remove the need for the exercise of judgement, but provides a sound basis upon which to make decisions using professional judgement.

3.3.73 However, it is the Authority’s view, based on independent advice from international experts, that a pre-determined weightings approach is no longer in common use nor is it considered the best practice in complex competitive design tenders comparable to the project. The Authority further indicated that the complex conceptual nature of the project, which relies heavily on visual and spatial integration of all the precincts, would be severely handicapped by a predetermined weightings approach since the project involves both quantitative and qualitative aspects.

Assessment of bids for initial 5 precincts against criteria

3.3.74 The assessment of bids against the Authority’s evaluation criteria was first undertaken by approximately 35 independent expert analysts during May and June 1997. The analysts were required to identify the strengths and weaknesses of each bid in relation to each of the key criteria and to assign a score for the related individual elements on a scale ranging from 0 to 10. The scoring provided by the expert analysts for each bid was collated by the Authority’s staff and presented to the relevant Assessment Review Panel for further consideration and the ranking of bids.

3.3.75 As detailed in the previous chart, 2 assessment review panels were established: one dealing with matters relating to finance, risk allocation, viability and commercial integration, and the other panel dealing with matters relating to design, amenity and planning integration. The assessment review panels recommended a ranking of the bids to the Steering Group which, in turn, made a recommendation to the Authority’s Board.

3.3.76 The Authority placed extensive requirements on the submission of bids by short-listed developers, including the requirement that bids must:

- be lodged by the specified date for the nominated precincts for which the developer had been short-listed;
- comply with the Authority’s requirements as set out in the bid documents;
- be unambiguous and enable a clear understanding of the basis of the bid;
- detail the price offered for the land and its composition;
- state clearly any additional financial benefits the bid offers to the Victorian economy and whether any such identified benefit would accrue only as a result of the specified proposal; and
- where a conforming bid is submitted, being a bid that meets all of the Authority’s requirements, a non-conforming bid would be considered if it met the objectives and evaluation criteria set out in the bid documents.



3.3.77 In respect of the Yarra Waters precinct, the Authority received bids that, to a varying extent, did not meet all the above requirements established by the Authority. In particular, specific areas where the bids did not meet the Authority's requirements ranged from design, public amenity, precinct specific proposals, financial offer, risk allocation, viability, integration, use, credentials and experience and benefits to Victoria. All bidders were subsequently given the same opportunity to improve their bids to resolve issues relating to their bid which were unacceptable or unsatisfactory to the Authority.

3.3.78 In relation to the successful bid, while initially like the other bids it was non-conforming, the Authority evaluated the bid despite its shortcomings which included concerns over the level of acceptance of certain risks by the developer. This bid achieved the highest interim ranking by the assessment review panels. Subsequently, the developer progressively provided further clarification of its bid. The developer submitted a firm financial offer and accepted certain key risks for the development prior to the preferred developers being decided by the Authority. The revisions to the developer's bid lowered its ranking by the individual assessment review panels but overall it had one of the highest rankings and accordingly the bid, together with one other, achieved preferred developer status in September 1997.

3.3.79 The 2 preferred bidders were then invited to negotiate outstanding conditions with the Authority in competition, leading to 2 executed development agreements (by the developers). The successful bidder was announced at the completion of this process after government approval in December 1997.

Assessment of developers' financial offers for the State's land

3.3.80 The developers' financial offers for the ultimate acquisition of the State's land were required by the Authority to not only include the estimated amounts to be paid to the Authority, including amounts arising from any revenue sharing arrangements, but also including certain costs estimated to be borne by the developer, such as environmental clean-up and land remediation, trunk infrastructure and the cost of services covering such things as emergency, health and community and education.

3.3.81 The Authority undertook the assessment of the developers' financial offers with significant input from expert accounting, property and valuation analysts, including the Office of the Valuer-General and the Department of Infrastructure.

3.3.82 The Authority's expert accounting advisers assessed the prospective developer's offers for the State's land and provided a comparative score for each bid.



3.3.83 In addition, the financial offers were assessed on the basis of whether or not they would result in a commercially viable development from the Developers' perspective in order to determine a fair commercial value of the land and because the risk of a developer failing is also a fundamental risk to the State. That is, an assessment of a developer's financial offer, which included consideration of estimates of development costs and revenues, which was aimed at ensuring that the financial offer to the State would lead to a reasonable commercial return or profit for the developer.

3.3.84 As noted below, the development arrangements for the Yarra Waters precinct provided that the developer may elect to not proceed with a stage or stages of the Development, without a penalty being imposed by the Authority, where there is insufficient market demand or it is not viable to do so, based on an independent assessment. Further, the Development Agreement makes provision for certain revenue sharing arrangements between the Authority and the developer under specified conditions. However, the Agreement makes no provision for the developer to compensate the Authority should it achieve a profit greater than anticipated.

3.3.85 Accordingly, under the arrangements, the developer has the option of not proceeding with individual stages of the development where there is insufficient market demand, or it is not viable to do so. However, where development stages proceed, the State has access to certain revenue sharing arrangements but does not have a right to share in any profits achieved by the developer in excess of those anticipated.

Risks borne by the State

3.3.86 The bid documents issued by the Authority for the initial 5 precincts set out the major risks associated with the Docklands redevelopment and detail how these various risks could be allocated between the developers and the State. Under the agreed risk arrangements arising from the Yarra Waters precinct, the first of the initial precincts where a successful developer has been announced by the Government, the following major categories of risk were allocated between the State and the developer:

- Legislative;
- Existing occupiers/tenants;
- Industrial action;
- Trunk infrastructure costs;
- Remediation costs;
- Contingent or variable purchase price for the land;
- Market demand;
- *Force majeure* events; and
- Project specific, including construction and financing.



3.3.87 Further, the development arrangements require that the developer commence and complete the necessary works in accordance with a schedule of milestones as set out in the agreement. Specific circumstances, which entitle the developer to an extension of time, are also set out in the agreement under which one or more of the planned stages of the development may not proceed as scheduled without a penalty being imposed on the developer.

3.3.88 The development arrangements do not limit the maximum period or number of any such extensions of time. However, the Authority may terminate the agreement and re-acquire any undeveloped land under certain circumstances.

3.3.89 While the development arrangements assign many risks to the developer, including construction cost overruns, the practical operation of the arrangement means that the developer can avoid proceeding with a stage or stages where there is insufficient market demand or where it is not viable to do so, based on an independent assessment. Accordingly, the development of this Docklands precinct will be dependent on market demand.

□ *RESPONSE provided by Chairperson, Docklands Authority*

Determination of developers - Public information

Extensive documentation was made available to the bidders and the public. Comprehensive information was also available to the public and all documents (other than a small number of commercial-in-confidence documents) were available for public inspection. Descriptive information regarding each bid proposal has been inserted in daily newspapers. Information included comprehensive bid documents, information memoranda, design guidelines and environmental management plans. The Docklands Authority set a new standard in competitive tendering by making some 40 000 pages of information available to bidders on CD-Rom in lieu of a traditional data room.

An extensive public consultation process was instigated by the Docklands Taskforce and has been maintained by the Docklands Authority. A number of general public seminars have been held to encourage the participation of the community and over 50 separate presentations on Melbourne Docklands have been given to a variety of organisations by Docklands Authority personnel.

Probity processes

The Melbourne Docklands development and private investment bid process is on a scale unmatched for property development in this country and comparable to a small number of global projects. From the outset, the Docklands Authority identified the essential requirement for, and has been committed to, developing rigorous and independent probity processes to achieve world's best practice.

The probity process was designed to achieve no less than this objective and the Authority undertook the following important steps, to ensure a result of the utmost procedural integrity.

- *sought independent advice on best practice probity processes by appointing a nationally recognised probity expert Ms Elizabeth Johnstone, Lawyer, National Director - Consulting, Blake Dawson Waldron, to design a process. Ms Johnstone also provided ongoing advice on specific probity issues;*



□ **RESPONSE** provided by Chairperson, Docklands Authority - continued

Probity processes - continued

- *segregated the Probity Auditor function from the Probity Design function by appointing the independent national expert, Mr Stephen Marks, Chartered Accountant, Principal of Stephen G Marks & Co Pty Ltd who reviewed and reported, as Probity Auditor, on all phases of the project;*
- *a probity process document was finalised as a detailed plan, which has been used subsequently on other major tendering projects;*
- *actively sought advice from Ms Johnstone and Mr Marks;*
- *appointed a sub-committee of the Board to monitor probity processes on a regular basis;*
- *conducted extensive probity briefings (to over 500 people);*
- *highlighted the public importance of probity in all relevant bid documents;*
- *consistently communicated with bidders in a thorough and timely manner; and*
- *segregated the independent assessment review panels and reinforced the importance of probity, process, commercial-in-confidence and conflict of interest issues to all those involved.*

Ms Johnstone and Mr Marks, and other independent national and international advisers from a number of disciplines (architecture, planning, accounting, law and finance) believe that there is clear evidence that the probity processes applied by the Docklands Authority are at the forefront of world wide probity best practice.

Written probity audit reports

The Authority, the Probity Adviser and Probity Auditor disagree with the Auditor-General's view that written probity audit reports should have been prepared for all phases. This is not part of the Docklands Authority probity process (where the Panel, Committee, or Board resolutions provide the written documentation at each phase), nor is it part of the Victorian Government's Purchasing Board's Guidelines.

In all phases of the bid process, the Probity Auditor was present and gave reports and advice prior to the preparation of written recommendations and resolutions by a Panel, Committee or Board from the meetings of Assessment Review Panels, Steering Group and the Board of the Docklands Authority. An unqualified written probity audit report was prepared at the conclusion of the process to complete appropriate probity documentation.

Evaluation criteria - Scoring and ranking

The approach used by the Authority of scoring and ranking competing submissions against a predetermined set of criteria and hurdles is the best process for these types of projects based on the independent advice from Australian and international experts. Any assessment of the bids which contain very diverse conceptual, land use and development proposals, would be severely limited by a predetermined weightings approach, in its capacity to consider all facets of each submission.



□ **RESPONSE** provided by Chairperson, Docklands Authority - continued

Evaluation criteria - Scoring and ranking - continued

The scoring hurdles and ranking approach use for this type of project:

- provides a transparent view of all scores and does not allow predetermined weightings to mask elements of proposals;
- prevents over-emphasis on weighted criteria to the exclusion of nonetheless important criteria;
- ensures that judgement is exercised, by the appropriate experts in full consideration of the bids rather than based on pre-bid pre-determined weightings;
- ensures the clearest linkage to the Authority's objectives which are encapsulated in the evaluation criteria.

The description of the evaluation criteria in the audit report as "conflicting" is misleading. Each of the evaluation criteria are distinct by their nature and although they may trade-off against each other such as design vs risk and finance, there is no conflict between the criteria.

Assessment of Yarra Waters precinct

In respect of the Yarra Waters precinct, the Docklands Authority received only non-conforming bids.

We note that the disclosure of the interim rankings could be totally misleading in any judgement of the final assessment. In a dynamic process, where information is progressively received as a result of clarification or negotiation, interim rankings are based on interim information and analyses, and are not conclusive.

Assessment of developers' financial offers - Yarra Waters

The development agreement with the appointed developer makes provision for the developer to pay an increased land purchase price to the Docklands Authority via a revenue share. Should the developer achieve a profit greater than anticipated due to circumstances including increased revenues, the Docklands Authority effectively participates in a share of this profit because of the revenue share.

The Docklands Authority deliberately chose a revenue share instead of a profit share because of its transparency and because this method diminishes the possibility of measurement disputes.

Risks borne by the State

Under the development agreement arrangements, the developer can apply for an extension of time, and receive such an extension if there is insufficient market demand, at that time, as determined by an independent assessor.

As Melbourne Docklands developments are to be demand driven, the developments are not to be a cost to government and they should only move forward if the market provides the appropriate conditions.





QUALITY OF EXTERNAL FINANCIAL REPORTING IN THE LOCAL GOVERNMENT SECTOR

Timeliness of year-end reporting

3.3.90 In my May 1997 *Report on Ministerial Portfolios*, I provided the Parliament with an assessment of the timeliness of external financial reporting in the local government sector for the 1995-96 financial year. In particular, it was concluded that, while a substantial improvement was achieved in the timeliness of financial reporting when compared with the previous year, scope remained for further improvement. In this Report, I have outlined the results of the 1996-97 external financial reporting cycle.

3.3.91 The *Local Government Act* 1989 prescribes that council annual reports, including the audited compulsory competitive tendering (CCT) and financial statements, must be forwarded to the Minister for Planning and Local Government within 3 months of the end of the financial year. To enable councils to satisfy this legislative reporting requirement, a deadline of 2 September 1997 was established by my Office for local government entities to submit their completed statements and the report of the contractors engaged to assist me on the audits, for review by my Office and the issue of my audit opinions.

3.3.92 In respect of the 1996-97 reporting cycle, it was found that by 9 September 1997, of the total of 97 local government entities, 23 of these entities had not complied with the above reporting deadline established by my Office. This result compared favourably with 63 non-compliant entities in the previous reporting cycle. Furthermore, by 30 September 1997, 7 entities still had not provided the requisite information to my Office, compared with 25 entities outstanding at the same time for the previous reporting cycle. **The threefold improvement in the timeliness of external reporting for the 1996-97 financial year occurred despite the need for certain entities to address significant issues associated with asset recognition and valuation, as required by Australian Accounting Standards, and for all entities to recognise and value their unfunded superannuation liabilities.**

3.3.93 The *Local Government Act* 1989 provides that the time frame for annual reports to be forwarded to the responsible Minister may be varied only at the Minister's discretion. In respect of the annual reports relating to the financial year ended 30 June 1997, the Minister granted 46 extensions to the prescribed reporting period, compared with 63 extensions granted for the previous financial year. However, 4 entities exceeded the Minister's approved extended time frame compared with 7 entities in the previous financial year.

3.3.94 As illustrated above, **there has been substantial improvement in the timeliness of financial reporting by local government entities which demonstrates that timely reporting can be achieved, given adequate resourcing, appropriate planning and management commitment. Nevertheless, the challenge remains for all entities to provide timely information to ratepayers by meeting the established reporting time frame.**

Compliance with Australian Accounting Standards

3.3.95 Local government entities are currently required by legislation to prepare their external financial statements in accordance with Australian Accounting Standards, particularly Australian Accounting Standard AAS 27 *Financial Reporting by Local Governments*, and additional reporting requirements prescribed in the *Local Government Act 1989* and the *Local Government Regulations 1990*.

3.3.96 During the 1996-97 financial year, the vast majority of councils and related entities complied with the Australian Accounting Standards and legislative disclosure requirements. Specifically, 89 local government entities received confirming audit opinions on their financial statements for the year ended 30 June 1997 (83 entities, for the year ended 30 June 1996) while 8 entities received non-confirming audit opinions on their financial statements (7 entities, for the year ended 30 June 1996). In relation to the Auditor-General's opinion on council CCT statements, only one council received a non-confirming audit report (30 June 1996, 1).

3.3.97 Table 3.3L outlines the key reasons for the issue of the non-confirming Auditor-General opinions on the financial statements of local government entities.

**TABLE 3.3L
BASIS OF NON-CONFIRMING AUDITOR-GENERAL OPINIONS**

<i>Issue</i>	<i>Financial year</i>	
	<i>1996-97</i>	<i>1995-96</i>
Inadequate or unreliable fixed asset records	4	4
Inappropriate recognition or disclosure of unfunded superannuation liabilities	2	-
Doubt over the value of debtors	1	1
Uncertainty regarding the future viability of the entity (a)	1	-
Grants received in advance not recognised as income	-	2

(a) Uncertainty relating to the future viability of a regional library corporation, as one member was considering withdrawing from the entity.

3.3.98 It is important that management takes appropriate remedial action during the current financial year to resolve the above non-confirming opinions, particularly those relating to fixed assets and superannuation.

Other emerging issues

Asset valuations and determination of useful lives

3.3.99 With the introduction of Australian Accounting Standard AAS 27 *Financial Reporting by Local Governments* in 1992, councils were required to identify, value, record and report within their annual financial statements all assets within a 5 year period expiring on 30 June 1997.



3.3.100 The audit review of the 1996-97 annual financial statements of entities within the local government sector revealed that the majority of councils had brought to account all their fixed assets. However, there was significant variance in the useful lives assigned to similar classes of assets by these entities. For example, one council assigned a life of 75 years for roads whereas a neighbouring council had assigned a life of 150 years for this asset class. In addition, some entities used the suggested useful lives for classes of assets contained in the *Asset Accounting Manual* issued by the Institute of Municipal Management, which has not been updated for many years.

3.3.101 While it is recognised that uniform depreciation rates and asset useful lives may not be appropriate for similar types of assets in the local government sector, given the divergence of conditions, including geographic and usage, it would nevertheless appear reasonable to expect some correlation in such rates between neighbouring councils. Accordingly, it is recommended that this area be reviewed to improve the quality of external reporting in the sector.

Possible disclosure enhancements

3.3.102 During the 1996-97 financial year, the Office of Local Government (OLG) within the Department of Infrastructure released Accounting Guideline No. 5 *Related Party Disclosure* as a guide to best practice for the disclosure of the remuneration of councillors and senior council staff and any transactions they, or their related parties, had with the council during the financial year. However, it was found that 10 councils (8 per cent) did not include related party disclosures within their 1996-97 annual financial statements.

3.3.103 **If the above guidelines provide the minimum standard of expected disclosure as determined by the OLG and such disclosures are not being adopted voluntarily by local government entities, then the Government may need to consider whether such disclosures should be mandated in legislation.**

3.3.104 **Furthermore, certain elements of the current local government financial reporting framework are considered to require review in order to enhance the achievement of quality financial reporting.** In particular:

- Councils are required to disclose within their financial statements certain forward financial commitments to external parties, including capital and operating commitments. Under the compulsory competitive tendering (CCT) environment, councils now have significant contracts with external parties for the provision of council services, such as garbage collection and road maintenance. However, these substantial obligations are not disclosed in aggregate form as part of the forward financial commitments of councils, together with the expected timing for meeting these obligations;
- The current legislation requires councils to provide the Minister for Planning and Local Government with explanations for the non-achievement of the CCT target. However, these explanations are not required to be incorporated in the published CCT statements. Consequently, ratepayers are not informed of the reasons for council's lack of success in this area of government policy;



- A valuable feature of the current reporting framework is the comparison of the actual accrual-based operating result with the result prepared on the basis of the rates determination statement. However, in a large number of instances, too much focus is given to the result achieved on the basis of the rates determination when the council's financial standing should be analysed based on its financial performance and financial position portrayed within the accrual-based statements;
- Provision exists for quarterly statements to be presented to council which reflect actual results against the rates determination budget, however, there is no requirement for accrual-based statements to be presented on a similar basis;
- Given the adoption of commercial practices by councils in financial and cash management, the need to continue with the longstanding legislative requirement of maintaining separate cash investments to meet long service leave obligations needs to be reviewed;
- Persons designated as principal accounting officers are not obliged to hold an accounting qualification or to be members of a recognised Australian professional accounting body, or to state their professional credentials in the statutory management report accompanying the financial statements, however, they are required to state that the statements comply with Australian Accounting Standards. As the governing legislation requires that the financial statements comply with Australian Accounting Standards, it is considered appropriate that the person who is responsible for the preparation of the financial statements is a member of a recognised Australian professional accounting body; and
- The current legislation requires the publication of specified annual financial ratios and the revaluation of council assets at least at the time of a municipal valuation for rating purposes. Given the changes to the sector, such as the valuation of assets at current values and the imminent introduction of performance statements, the legislative requirements may no longer be relevant.

3.3.105 The performance of the local government sector would be further enhanced through the development by the OLG of a best practice set of financial statements for use by all local government entities.

Performance statement

3.3.106 As from the 1998-99 financial year, council annual reports will be required to include an audited performance statement which outlines:

- performance targets and their applicable measures as shown in the annual business plan or the strategic corporate plan for that year; and
- the extent to which those targets were achieved.

3.3.107 At the date of preparation of this Report, the OLG had conducted extensive consultations with the local government sector in order to determine the mandatory qualitative and quantitative measures to be included in the Statement.



3.3.108 Over the past 12 months, my Office has encouraged councils to consider the implications that performance reporting will have on their activities, especially the need to develop systems for the collection, retention and verification of data supporting mandatory and other measures intended for external publication. In addition, my Office has recommended that, prior to 30 June 1998, the proposed measures and the underlying data collection systems be subject to independent review, possibly by internal audit, consultants, or a third party such as my Office, to ensure that appropriate, reliable and robust data is collected and retained for performance reporting purposes. However, to date, I am only aware of 2 councils that have resolved to undertake an independent review of their proposed performance measurement system.

3.3.109 To enable the efficient and effective production by councils of performance statements, it would be advantageous if the OLG and councils participated in a program whereby councils' preparedness for performance reporting is independently reviewed. To assist in this program, the OLG needs to develop guidance on the mandatory requirements of the Performance Statement, including the associated attestation requirements.

□ *RESPONSE* provided by Deputy Secretary, Local Government, Planning and Market Information

Timeliness of year-end reporting

Seven local government support managers have been appointed to work from regional locations with municipalities. One of their key tasks for 1998-99 will be to work to improve the performance of those councils which have not completed their annual reports, including audited financial reports within the statutory time frame. There will be ongoing liaison with the Auditor-General's Office, to achieve improved performance through co-operation with councils.

Compliance with Australian Accounting Standards

All municipalities receiving audit qualifications will be contacted by the Office to reinforce the need for compliance with the Australian Accounting Standards relating to the recording of fixed assets and their superannuation liability.

Emerging issues

Disclosure enhancements

Local government support managers will be working with municipalities to improve compliance for the disclosure of allowances payable to councillors and remuneration payable to senior council staff. The Local Government (Disclosure of Information) Regulations 1998 were introduced on 24 March 1998. These Regulations require councils to publicly disclose specific information in relation to councillor and mayoral allowances and senior staff remuneration packages, by including details in the annual financial statements.

Other disclosure issues raised in this section of the Report will be taken up with the local government sector through the auspices of the Municipal Association of Victoria; the Auditor-General's Office will be invited to be party to these discussions. The focus will be on continual improvement in the quality of financial reporting by local government.



□ *RESPONSE provided by Deputy Secretary, Local Government, Planning and Market Information - continued*

Disclosure enhancements - continued

As a separate exercise, the Office is working with the Moira Shire Council to develop a set of model financial reports to meet the needs of rural shires.

Best practice set of financial statements

Development of standard key performance indicators with local government has resulted in the introduction of industry-wide standard indicators for the 1998-99 financial year. Ongoing training and documentation of requirements is being facilitated by the Office of Local Government.





**OPERATION OF AUDIT COMMITTEES AND INTERNAL AUDIT
WITHIN THE LOCAL GOVERNMENT SECTOR**

3.3.110 In 1993, the Government commenced the reform and restructuring the State’s local government sector. An essential element of the reform process was the creation of a smaller number of councils with responsibility for higher levels of community resources. In this environment, the establishment and effective operation of corporate governance processes are critical for councillors to discharge their responsibilities to the community. The operation of an effective audit committee that is supported by an internal audit function are key components of effective corporate governance arrangements.

3.3.111 The Australian Accounting Research Foundation, the Institute of Internal Auditors in Australia and the Australian Institute of Company Directors in a December 1997 joint publication, titled *The Best Practice Guide - Audit Committees*, indicated that an audit committee performs a key role in assisting the board of directors or their equivalent to fulfil its corporate governance obligations and to oversee responsibilities in relation to an entity’s financial reporting, internal control structure, risk management systems, and the internal and external audit functions. An effective audit committee strengthens an entity’s control environment and establishes an appropriate ethical attitude and culture throughout an organisation.

3.3.112 The Australian Auditing Standard issued by the joint Australian professional accounting bodies, relating to *Considering the work of Internal Audit*, defines “internal audit” as an appraisal activity established within an entity as a service to the entity and is a component of the internal control environment which provides valuable and useful information to senior management for planning and decision-making purposes. In providing this assurance, internal audit may be directed by management to:

- evaluate the adequacy of the internal control structure and monitor the operations of information systems, with recommendations for improvements;
- examine financial and operating information including the testing of transactions, balances and procedures;
- review the economy, efficiency and effectiveness of operations including the non-financial controls of an entity; and
- review compliance with laws, regulations and other external requirements, management policies and directives and other internal requirements.

3.3.113 In this context, audit conducted a review of corporate governance processes related to audit committees and internal audit within the local government sector.

Audit committees

3.3.114 The existence of an effective audit committee is fundamental in enabling a local government entity to fulfil its corporate governance obligations. For an audit committee to be effective:

- it should operate under a formal charter approved and minuted by the council or board; and
- the chairperson and the majority of members should be independent of executive management and the elected representatives.

3.3.115 An audit survey of 97 local government entities revealed that only 50 entities had established an audit committee. However, 19 per cent of survey respondents indicated that their audit committee was comprised of members who were either executive management, elected councillors or directors. In addition, only 17 per cent of audit committees operated under the auspices of an approved audit charter with a further 29 per cent of audit committees currently developing such a charter.

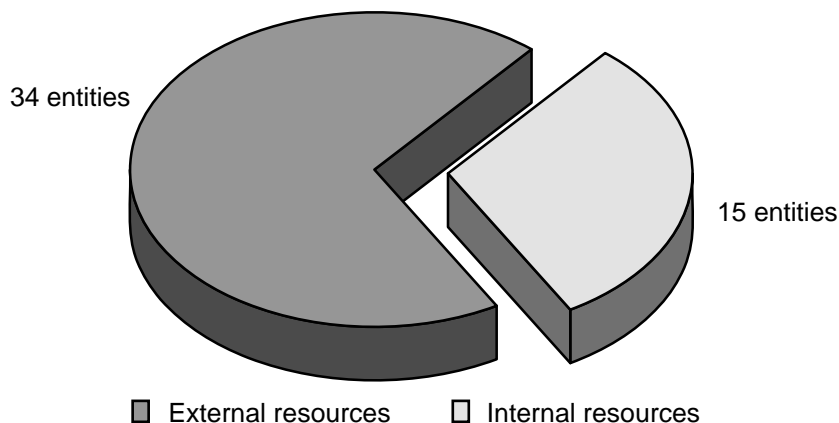
Internal audit

3.3.116 A strong internal control environment which incorporates an effective and efficient internal audit function is conducive to sound corporate management.

3.3.117 The audit review identified that 49 local government entities had established an internal audit function. Accordingly, it is disappointing that a **substantial proportion of local government entities responding to the survey had not established such a function, with the majority of these entities located in the State’s rural areas.** The key reasons provided by these rural councils for not establishing an internal audit function related to the size of the council and the lack of available funds.

3.3.118 Chart 3.3M outlines that of the 49 entities which had established an internal audit function, the majority of these entities utilised external resources to provide this function.

**CHART 3.3M
INTERNAL AUDIT RESOURCING ARRANGEMENTS**



3.3.119 Table 3.3N details the rationale provided by local government entities for either outsourcing this function or using in-house personnel.

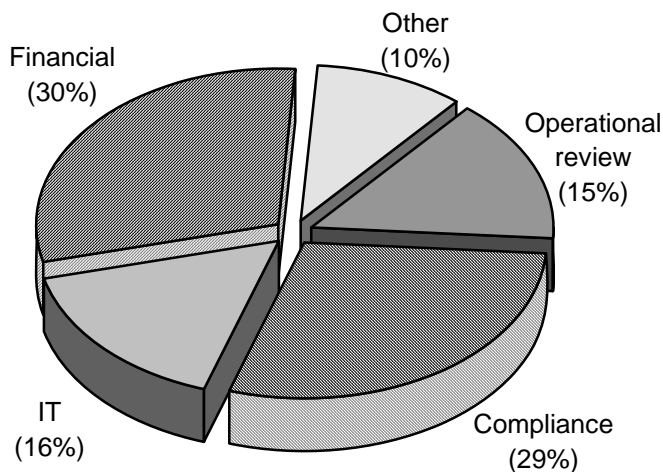
**TABLE 3.3N
RATIONALE FOR INTERNAL AUDIT RESOURCING**

<i>Reasons for outsourcing this function</i>	<i>Reasons for utilising in-house resources</i>
Acquisition of contemporary and specialist advice.	The cost of outsourcing could not be justified given the size of the organisation.
Higher degree of autonomy, coupled with independence and objectivity for proper governance.	Internal resources more familiar with the complexity of council operations.
Acquisition of varied skills and qualifications, and expertise in the local government area, with a higher degree of professionalism.	In-house resources more flexible and additional services are provided at no extra cost.
Obtain an external appraisal on the organisation risk profile by experienced personnel using current techniques and technology.	External skills required only on an ad-hoc basis to complement internal specialist skills.
More efficient and economical, as the size of the entity may not justify full-time resourcing.	In-house resources readily available to respond to management needs in a timely manner.

3.3.120 Services provided by internal audit vary widely depending on the requirements of management which can include the evaluation of the internal control structures, the assessment of operational efficiency and effectiveness, examination and testing of transactions, balances and procedures, and the review of compliance with regulations, management policies and other external and internal requirements.

3.3.121 Chart 3.3O illustrates the types of activities currently undertaken by internal audit within the local government sector.

**CHART 3.3O
SERVICES PROVIDED BY INTERNAL AUDIT
(per cent)**





3.3.122 Given the extent of work undertaken by internal audit, it was surprising that only 39 per cent of councils surveyed had developed an internal plan to enable management to prioritise the work to be undertaken by this function. It is recommended that audit committees develop such plans to enable adequate monitoring of the scope and effectiveness of the function.

3.3.123 **The use of audit committees and internal audit has not been universally adopted across the local government sector and, as a consequence, corporate governance within the sector has been diminished compared with best practice. Accordingly, it is recommended that the Office of Local Government develop and issue a *best practice* guide in respect of audit committees and internal audit to assist in the effective management of local government entities.**

RESPONSE *provided by Deputy Secretary, Local Government, Planning and Market Information*

Regional support managers will encourage those councils and regional library corporations which have not introduced an audit committee, to do so by 31 December 1998, utilising the Best Practice Guides developed by the Institute of Municipal Management and the Victorian Auditor-General's Office.

Consultations will take place with municipalities and regional library corporations to encourage the use of Best Practice Guides for audit committees and for internal audits, to assist in the effective management of municipalities and regional library corporations.



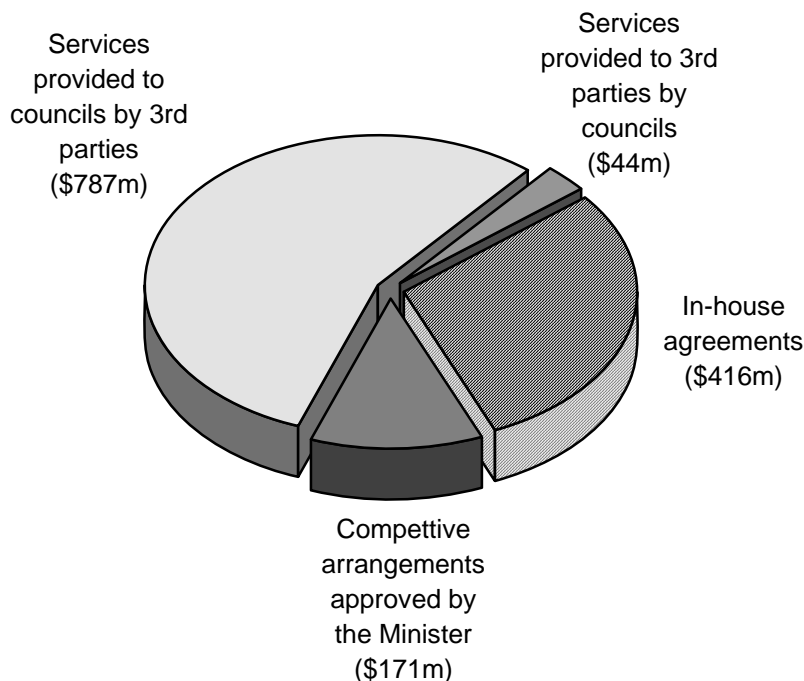
MANAGEMENT OF MUNICIPAL BUSINESS UNDERTAKINGS

3.3.124 An essential aspect of the Government’s local government reform program has been the introduction of a compulsory competitive tendering (CCT) regime whereby both direct and support services of councils are subject to market testing in order to ensure that ratepayers obtain cost-effective services. Under this regime, as long as the annual aggregate value of services that have been subjected to market testing is equal to, or exceeds, a legislated benchmark, which was equivalent to 50 per cent of normal operating expenditure for the year ended 30 June 1997, it is the prerogative of council to determine the specific services that are subjected to market testing.

3.3.125 An audit analysis of the audited CCT statements prepared by councils for the 1996-97 financial year established that **the value of services that had been subjected to market testing was \$1.4 billion.**

3.3.126 Chart 3.3P outlines the composition and value of market testing as reported by councils as at 30 June 1997. The chart also indicates that **approximately one-third of competitively tendered services are currently being provided by council in-house provider teams.**

CHART 3.3P
VALUE OF COMPULSORY COMPETITIVE
TENDERING ARRANGEMENTS AS AT 30 JUNE 1997
 (\$million)



3.3.127 Under current CCT arrangements, a council’s own workforce, otherwise known as in-house service providers or business units, compete with the private sector for contracts offered by their council and third parties, including public and private sector entities.



3.3.128 The provision of services to council and third parties by in-house service providers must be properly managed by councils in order to ensure that ratepayers receive an appropriate return from the funds invested on their behalf by council in the business unit, and that their financial exposure is minimised. Therefore, councils should ensure that adequate control mechanisms and accountability arrangements are in place to effectively oversight the operations of their business units.

3.3.129 **My audit of the Mildura Rural City Council for the year ended 30 June 1997 disclosed that the council was incurring losses on road maintenance contracts performed by an in-house service provider for external parties, such as VicRoads and neighbouring municipalities.** A report commissioned by the Minister for Planning and Local Government into the causes of these losses revealed that they totalled in excess of \$2 million, which was equivalent to almost 20 per cent of the council’s annual rate revenue. The report also found that the losses occurred as a consequence of council’s poor management and supervision of the contracts.

3.3.130 The findings arising from the Mildura investigation, together with the extent of council contracts awarded to in-house service providers, were the catalyst for an audit review into the management control practices implemented by councils to monitor the operations of in-house teams and to oversee the associated contracts.

Separation of the purchaser and provider roles

3.3.131 A clear separation of the purchaser and provider roles is fundamental to ensuring the integrity and transparency of CCT operations within councils. Several inquiries commissioned by the Minister for Planning and Local Government have reported this as being a critical factor in maintaining the probity and fairness of the tender process.

3.3.132 Councils were surveyed by audit to establish the arrangements that had been implemented for the separation of the purchaser and provider roles.

3.3.133 Table 3.3Q which is based on council responses, indicates that while most councils have implemented organisational arrangements for a functional separation of purchaser and provider activities, only 2 councils have adopted a complete separation of provider functions through external corporatisation, with the majority of councils retaining purchaser and provider groups as business units within their council. The table also highlights that:

- 28 councils have adopted *vertical* management arrangements under which the separated provider units are organised into either a single business unit or multiple business units directly responsible to the council’s chief executive officer;
- 33 councils have adopted *horizontal* management arrangements under which separated purchaser and provider units both exist within council operational groups, with both units subject to the overall direction of the senior executive responsible for the relevant group; and



- 5 councils have not adopted a formal purchaser/provider split as:
 - they maintained that the size of their council did not warrant such separation (4 councils), or
 - all services had been outsourced (one council).

**TABLE 3.3Q
COUNCIL PURCHASER/PROVIDER ARRANGEMENTS**

<i>Arrangement</i>	<i>Councils</i>	
	<i>(no.)</i>	<i>(%)</i>
Provider units externally corporatised	2	3
Purchaser and provider functions separated internally on a vertical basis	28	41
Purchaser and provider functions separated internally on a horizontal basis	33	49
No separation of purchaser and provider functions	5	7
Total	68	100

3.3.134 The preference of the majority of councils for either a horizontal management separation or no separation of the purchaser and provider roles is of concern as these forms of arrangement, compared with external corporatisation or vertical management arrangements, provide reduced transparency for the purchaser and provider functions in councils and can attract criticism relating to the probity of in-house tendering processes. This was recently highlighted in the Report by the Municipal Inspector appointed by the Minister for Planning and Local Government to review CCT matters at the Swan Hill Rural City Council which indicated that the organisational structure of that council which underpins the CCT process was inadequate. The structure did not provide a sufficiently clear separation between the purchaser and provider elements of council activity.

3.3.135 The diversity of council organisational arrangements for the separation of purchaser and provider roles arises from the absence of any central guidelines for the optimum organisation of purchaser and provider groups within councils. As the success of CCT depends, in part, on the continuing transparency of purchaser and provider functions, the Office of Local Government should develop *best practice* guidance for purchaser and provider arrangements within councils.

Business unit reporting

3.3.136 As was previously mentioned, the audit survey revealed that most respondent councils retained provider groups as part of their council entity in preference to the external corporatisation of these units. Under these arrangements, in-house service providers (business units) should operate under a regime which ensures that councillors receive timely and appropriate financial and performance reporting on their respective activities.

3.3.137 Table 3.3R illustrates the number of in-house business units currently operating within councils.

**TABLE 3.3R
IN-HOUSE BUSINESS UNITS (PROVIDERS)**

<i>No. of business units (a)</i>	<i>No. of councils</i>
1 to 5 units	20
6 to 10 units	20
11 to 20 units	12
Greater than 21 units	1
Separate trading entity	8
Total	61

(a) Excludes councils where no purchaser-provider separation exists.

3.3.138 An audit analysis of council responses regarding the financial and performance reporting practices adopted in relation to these business units revealed that:

- not all councils had developed adequate accounting systems for recording business unit transactions;
- accounting arrangements did not always provide for the recording of assets and liabilities associated with business units;
- costing policies did not always provide for a return on capital for council assets used by business units; and
- reporting by business units on contract performance did not always encompass performance and quality issues related to service delivery.

3.3.139 In particular, it was found that **12 respondents were unable to identify the surpluses or losses generated during the 1996-97 financial year from their business unit operations with contract expenditure in excess of \$68 million.**

3.3.140 The absence of best practice guidance for councils for the operation of business units has been a factor that has contributed to the incomplete accounting and reporting arrangements for these in-house units. In addition, the absence of adequate asset accounting, combined with the failure to include a return on capital vested with business units, could adversely impact on councils' implementation of competitive neutral pricing in the 1997-98 financial year, as required under National Competition Policy.

3.3.141 **There is a need for the Office of Local Government to develop best practice guidelines for financial and performance reporting by council business units and for councils to strengthen their internal processes for the monitoring of business unit operations, particularly where such units provide services external to the council and consequently expose ratepayers funds to risk.**

Performance of business units

Financial outcomes

3.3.142 Of the 78 Victorian councils, only 56 provided audit with details of surpluses or losses incurred in the 1996-97 financial year by in-house business units in relation to contract work performed under in-house agreements and work undertaken on behalf of external parties.

3.3.143 Table 3.3S summarises the details of surpluses or losses for these councils and indicates that in-house business units generally achieved financial surpluses on contract work in the 1996-97 financial year, with 10 councils reporting net surpluses in excess of \$500 000.

3.3.144 Although the survey indicated that 93 per cent of council business units had achieved surpluses in the 1996-97 financial year, the following factors should be recognised:

- the reported results have not been subject to a separate audit by my Office;
- deficiencies identified previously in this Report regarding accounting systems and practices used within business units may impact on the reliability of the reported surpluses and losses; and
- 12 councils were unable to complete this aspect of the survey.

TABLE 3.3S
SUMMARY OF FINANCIAL PERFORMANCE OF IN-HOUSE UNITS
(no. of councils)

Range	<i>In-house contracts</i>		<i>External contracts</i>	
	<i>Surpluses</i>	<i>Losses</i>	<i>Surpluses</i>	<i>Losses</i>
\$1 to \$50 000	14	3	12	-
\$50 000 to \$100 000	6	-	4	-
\$100 000 to \$250 000	17	1	4	-
\$250 000 to \$500 000	7	-	1	-
\$500 000 to \$1 million	6	-	2	-
More than \$1 million	2	-	-	-
Total	52	4	23	-

Distribution of business unit surpluses

3.3.145 The financial surpluses arising from in-house business unit operations are either shared between council and the respective business unit under “gain-sharing” arrangements, or are fully absorbed by the council. “Gain-sharing” arrangements have arisen from enterprise bargaining between councils and their employees and are usually formalised in workplace agreements. The advantages of “gain-share” arrangements are perceived as:

- rewarding business staff for good performance;
- encouraging efficiency and innovation within business units;



- providing additional funds for training and equipment needs; and
- ensuring better service provision to council.

3.3.146 Table 3.3T provides a summary of arrangements adopted by councils for the application of financial surpluses arising from in-house business units.

**TABLE 3.3T
APPLICATION OF BUSINESS UNITS SURPLUSES**

<i>Arrangement</i>	<i>No. of councils</i>
"Gain-share" distribution	34
Full absorption by council	33
Total	67

3.3.147 Audit identified that where "gain-share" arrangements were in existence, these arrangements generally provided for a 3-way split of business unit surpluses between council, the business unit and a contingency fund established to meet potential future losses by the business unit. The distribution to council was generally between 30 to 50 per cent of business unit results. The business unit generally re-distributes its share of the surpluses to its staff, however, in some cases moneys were identified to fund equipment and training needs.

3.3.148 Aggregate distributions to business units under 'gain-sharing' arrangements, notified by councils, for the 1996-97 financial year totalled \$2.5 million.

3.3.149 "Gain-share" arrangements represent a key element of current industrial practice and are seen as a means of ensuring a greater involvement and commitment of employees in the continued success of their employer. However, in audit opinion, **the operation of "gain-sharing" arrangements must ensure that the risks associated with them are equally shared. In particular, such arrangements should provide for the:**

- **distribution of gains to occur at the completion of a contract when the results are known rather than while the contract is in progress;**
- **results to be determined based on a full attribution of costs to the business unit, including an appropriate return on capital to the ratepayers; and**
- **operation of such arrangements and the business unit in general to be constantly monitored by councils to ensure that they continue to provide benefits to ratepayers.**



- **RESPONSE** provided by Deputy Secretary, Local Government, Planning and Market Information

Mildura Rural City Council

The findings and recommendations from the independent review of the operations of the road construction “in-house” business unit at Mildura Rural City Council have been circulated to all councils for their information, and to assist councils to better manage the finances of Business Units.

Organisational structures with purchaser provider split

Regional support managers will continue to encourage chief executive officers to adopt organisational structures which clearly demonstrate the purchaser provider split to improve transparency for council operators

Report of Swan Hill Rural City Council

All chief executive officers have been provided with a copy of the Independent Review of the Swan Hill Rural City Council in relation to the management of “in-house” business units. The letter covering the report reiterated the need for chief executive officers to implement staffing structures that adequately separate client/provider roles.

Business unit reporting

The Office of Local Government is developing, in consultation with councils and the Municipal Association of Victoria, Best Practice Guidelines for Financial and Performance Reporting by “in-house” business units to councils. This will include the monthly monitoring of business unit operations, especially where operations external to the council may expose ratepayers’ funds to greater risk. It is expected that councils will be required to publicly report the outcomes of all contracts against budgets in the financial statements, included in annual reports.

Performance of business units

The Office of Local Government will, in 1998-99 develop in consultation with councils and the Municipal Association of Victoria, Best Practice Operations Guidelines for “Gain Sharing” agreements to provide for the:

- distribution of gains to occur at the completion of a contract when the results are known rather than while the contract is in progress;
- results to be determined based on a full attribution of costs to the business unit, including an appropriate return on capital to the ratepayers; and
- operation of such arrangements and the business unit in general to be constantly monitored by councils to ensure that they continue to provide benefits to ratepayers.





IMPACT OF POOR TENDER SPECIFICATIONS

3.3.150 Following the introduction of compulsory competitive tendering (CCT) within the Victorian local government sector, councils have subjected a significant proportion of their operations and services to market testing. The efficiency and effectiveness with which such services are now expected to be provided by contracted service providers are specified within the tender specifications and executed contracts.

3.3.151 In this context, audit conducted a review of the processes adopted by the Macedon Ranges Shire Council to acquire maintenance services for its local road network, comprising 720 kilometres of sealed road and 840 kilometres of unsealed roads.

Development of tender specifications and the proposed contract

3.3.152 During the early part of 1996, a number of metropolitan and rural councils, with the assistance of a private consulting firm, collectively developed model specifications associated with the competitive tendering of road maintenance services.

3.3.153 In July 1996, the Macedon Ranges Shire Council, then under the control of government-appointed commissioners, adopted the model specifications for the purposes of tendering its road maintenance services. The tender specifications issued by the council to award a lump sum contract for the provision of road maintenance covered:

- the maintenance of the local road network, which is funded from council sources; and
- the routine maintenance of certain main roads to a quality standard specified by VicRoads, which is funded by the State.

3.3.154 Under the proposed contract component relating to the local road network, the appointed contractor would be required to provide all necessary labour, materials, plant and equipment to undertake:

- maintenance services, including:
 - all bridges and major culverts;
 - urban streets, including drainage, footpaths, bicycle paths and kerbs;
 - unsealed roads and shoulders, open drains, and culverts in rural and urban areas;
 - signs and roadside furniture;
 - sealed roads and car parks in rural and urban areas; and
 - line-marking;
- sweeping of kerbs, channels and streets; and
- minor capital works to the maximum value of \$50 000 per annum.

Tender evaluation and selection process

3.3.155 In August 1996, 5 submissions were received from prospective tenderers for both components of the contract as the council had reserved the right to make a separate appointment for each component.

3.3.156 In line with the council's competitive tendering policy, an evaluation panel was established to assess the tenders received and to recommend the most appropriate tender to the chief executive officer for consideration and presentation to the council for ratification. As one of the tenderers was the council's in-house work group, 2 independent persons with experience in the delivery of this type of service were appointed to the panel together with 3 council representatives.

3.3.157 In September 1996, the commissioners requested that legal advice be obtained to ensure the soundness and strength of the proposed contract, from the perspective of contract law, and to ensure delivery of the work envisaged without the successful tenderer resorting to demand for extras.

3.3.158 The legal adviser identified a number of minor weaknesses in the proposed contract, including the specifications, which had the potential to develop into contractual difficulties. These weaknesses related to the inconsistent use of the terminology, the lack of legal definitions and the failure to demonstrate the role and responsibility of the contract supervisor. The adviser also noted that the performance criteria within the local roads component of the contract did not clearly identify the penalties or deductions which would apply in the event of non-performance against the contract requirements and the schedules to the contract were unclear, with no references between the schedules and other sections of the contract, which meant that any ambiguity would be open to interpretation. The legal adviser recommended that after selecting the successful tenderer, but before the contract was awarded, the council should meet with the preferred tenderer with the aim of re-wording the specification and the contract to take into account the potential contractual weaknesses in order to eliminate the potential for mis-interpretations.

3.3.159 In addition, the chief executive officer engaged an independent road construction and maintenance contractor to identify any weaknesses in the proposed contract which could be pursued by the successful service provider in order to extract a financial advantage from the council which was not envisaged or intended, and to provide comment on the disparity in contract prices submitted by the prospective tenderers, especially with regard to the local roads component of the proposed contract. The contractor concluded that there were no substantial opportunities for the appointed contractor to successfully claim for contractual overruns or other associated costs. However, the contractor identified that the local roads component of the proposed contract:

- Was relatively new and untried;
- Could bring with it risks for both parties which may not be identified from a cursory glance;
- Incorporates specifications that leave the reader of the contract in no doubt that the council was looking for a high standard of maintenance provided at industry best practice however, the intent and the outcome could be divergent;



- Did not include penalty provisions or payment deductions which could result in a contractual dispute and, in addition, there was no correlation between actual performance of the contract and the right to payment; and
- Included an appendix which identified the council’s anticipated frequency of grading of unsealed roads. The contractor advised that the successful tenderer could determine when extra work was required, which would constitute a contract variation.

3.3.160 The tender evaluation panel received the advice of the legal adviser and the independent contractor prior to preparing its report to the council’s chief executive officer.

3.3.161 The report, which was submitted in October 1996, contained a recommendation which was not unanimous as one panel member, being a council representative, favoured the in-house bid as the lowest tenderers were unable to convince the member that their available resources would meet the level of works required to be delivered under the contract. The report also expressed a number concerns regarding the ability of the 2 lowest priced tenderers, including the recommended tenderer, to deliver the requirements of the contract. Furthermore, the report indicated that the tenderers which had submitted the lowest bids may not have appreciated the complexity and extent of the specifications as they related to the local geographical and climatic conditions of the Shire, which could result in variations to the contract. The panel was concerned that the selection of the lowest tenderers may lead to contract supervision problems, acknowledging that if specification problems arose, contract supervision would be critical. Finally, in the report the panel specifically drew the attention of the chief executive officer and the council to the concerns of the legal adviser and the independent consultant.

3.3.162 A review of the tender panel’s report revealed that it was the panel’s view that if the contract was not awarded to the lowest tenderers, the council would have difficulty in defending its decision on the basis of price. However, the panel recommended in its report to the chief executive officer that the council could benefit from a low contract price if it implemented the following 3 point plan:

- allocate time and resources to enable the council and the contractor to undertake a joint survey of road conditions to determine the works necessary to arrive at the required service levels;
- re-word the specification to overcome the weaknesses identified by the legal and technical advisers; and
- appoint a full-time contract supervisor with the exclusive role of supervising the road maintenance contract.

3.3.163 In addition, the panel report stated that if it was the council’s intention to maintain the existing road conditions and level of service, then the acceptance of one of the lower tenderers as the preferred tenderer could put the safety of road users at risk.

3.3.164 The chief executive officer advised the commissioners to adopt the recommendation of the tender evaluation panel to accept the lowest conforming bid and the preparation of a transitional plan.



3.3.165 The commissioners, in accepting the recommendation of the chief executive officer, directed that the proposals by both the evaluation panel and chief executive officer be implemented. Audit identified that:

- a full-time contract supervisor was appointed as from February 1997;
- a transitional work plan was developed applicable from December 1996;
- the joint road condition survey had not been undertaken; and
- a memorandum of understanding was completed on 16 October 1996 which identified that the contract specification had some shortcomings which would be overcome by the parties in order to ensure that the contract was successfully implemented.

3.3.166 In October 1996, a contract valued at \$5.2 million, relating to both components of road maintenance services, was awarded by the council to Bencon, a business unit of the City of Greater Bendigo which specialised in road construction and maintenance. The contract covered a period of 3 years, commencing from January 1997, with an option to extend the contract for a further 2 years at the council's discretion. Under the contract, services were required to be performed in accordance with industry best practice and delivered in accordance with the approved plan. In addition, the contractor's performance was to be measured against the performance criteria detailed within the specifications, with a performance assessment jointly undertaken between the council and the contractor every 3 months.

3.3.167 The council subsequently issued a formal press release announcing the successful tenderer, indicating that the council would save in excess of \$1 million per annum as a consequence of competitively tendering its road maintenance services. In addition, the commissioners indicated that as the in-house bid was unsuccessful, the council would retain up to 8 road workers to complete the existing construction commitments for a period of 6 months.

Contract management and dispute resolution

3.3.168 Since the commencement of the contract, both parties have identified problems with interpreting the contractor's obligations as defined in the specifications. In particular, over a 9 month period the council, based on its interpretation of the specifications, identified numerous instances of alleged non-compliance with the contract, including:

- the level of response and the quality of work undertaken did not accord with expected quality standards;
- the initial road inspection reports were not provided by the contractor within one month of the contract commencement, thereby delaying the approval of maintenance works for a substantial period;
- the contractor failed to undertake work on a pro-active basis as required under the contract;



- an unsatisfactory standard of grading of the unsealed road network; and
- the council’s inspection of work undertaken by the contractor indicated that works had not been undertaken or had not been completed in a satisfactory manner.

3.3.169 On numerous occasions, the contractor requested the council to provide greater detail of the location and nature of the alleged non-compliance to enable it to rectify or carry out such works. The contractor also advised the council that it had difficulty in assessing the road network due to the council’s failure to supply accurate locality plans identifying the road assets and, in June 1997, advised that several sealed roads in the municipality warranted rehabilitation works that were beyond routine patrol work. Given the excessive level of pot-holing identified by the contractor in the initial inspection reports and the level of subsequent patching performed by the contractor’s patrol crew, the contractor indicated that these roads had either major structural faults in the road pavement or the surface treatment had failed, both of which required work which was beyond the scope of the contract.

3.3.170 In July 1997, the council issued its first non-conformance warning to the contractor for continued failure to meet the required performance standard of work. In August 1997, the contractor responded by indicating that even though the majority of items inspected by the council were outside the requirements of the contract, the contractor had rectified those works at no additional cost. Also, the contractor indicated to the council that there was an urgent need to resolve the differences in interpretation of the specifications of the contract. The contractor and the council agreed that a formal dispute resolution process be utilised to provide certainty to both parties for the remainder of the contract.

3.3.171 In September 1997, the contractor issued a notice of dispute to the council, with the aim of appointing a third party to resolve a significant number of contractual disputes between the parties, mainly relating to key differences in interpretation pertaining to the specifications with respect to pot-hole patching, edge repairs, crack sealing, vegetation clearing, light and heavy grading, service levels and other matters.

3.3.172 A mediator was jointly appointed by the contractor and the council in late September 1997 to assist in the dispute resolution process and to address issues which could not be resolved between the parties. A significant number of contentious items were resolved during the mediation process, however, it was agreed that further work and re-wording of the contract was required.

3.3.173 During February 1998, a Deed of Amendment was entered into by the parties clarifying various provisions of the initial contract and incorporating a variation to the contract totalling \$620 000 to enhance the level of service provided for unsealed roads.



Overall conclusion

3.3.174 The terms and conditions of this contract have been subjected to differing interpretations by the contractor and the council due to a lack of clarity of the contractual obligations of both parties, especially the expected type and standard of service to be provided.

3.3.175 Some of the ambiguities in the contractual arrangements and their potential consequences were brought to the attention of council by the tender evaluation panel, its legal adviser, and the independent contractor, however, they were not effectively addressed.

3.3.176 To avoid a re-occurrence of the problems outlined above, councils when competitively tendering road maintenance services should ensure that:

- the state and condition of the road network at the time of tendering is clearly documented and accepted by both parties to enable a common understanding of the contract requirements;
- pre-tender meetings are held to enable a consistent understanding of the tender specifications, particularly in respect of the expected type and standard of service to be provided;
- the concerns of experts regarding the contractual arrangements are addressed in a timely manner, particularly where it is identified that the council may be exposed to claims if no remedial action is taken;
- the contractor is notified of any alleged sub-standard work in a manner that enables the contractor to readily identify the nature, extent and location of the alleged sub-standard work; and
- assessments of the contractor’s performance are based on periodic joint inspections.

RESPONSE provided by Chief Executive, Macedon Ranges Shire Council

In July 1996, Council adopted a road maintenance specification based upon a model specification developed collectively by a number of councils with the assistance of a private consulting firm. After the contract was advertised, a pre-tender meeting was held with interested organisation to provide an overview of the contract and clarify the requirements of the specification.

The pre-tender meeting was attended by 8 organisations and at the close tenders, 5 of them had submitted a conforming tender including a bid from Council’s own road maintenance team. This is a 3 year contract and tender prices ranged from \$5.18 million to \$10.2 million. The 3 lowest tenderers were external organisations (and the 2 lowest tenderers were not local). Council’s simple estimate of the contract value based upon the 1996-97 budget and 3 years was \$8.56 million.

Maintenance of the local road network and certain main roads was traditionally the responsibility of Council employees and this was the first time that this complex service had been documented in the form of a specification.

Because of concern about the adequacy of the specification to sustain a viable and effective 3 year contract, Council sought legal advice and also advice from an independent road contractor.



□ **RESPONSE** provided by Chief Executive, Macedon Ranges Shire Council
 - continued

Your Report accurately conveys that the Evaluation Panel (comprising 5 people) undertook a thorough evaluation of the tenders received. The Panel was concerned whether the 2 lowest tenderers would be able to deliver to the requirements of the specification and whether they had appreciated the complexity and magnitude of the specification in relation to the local geographical and climatic conditions of the Shire.

Nevertheless, the lowest priced tender was \$3.38 million less than the Council's estimate of the contract.

Because of this significant difference, the Panel was of the view that the Council would have difficulty defending a decision not to award the contract to the lowest tenderer on the basis of price.

Council's Competition Strategy requires the Panel to report to the Chief Executive Officer with a recommendation and, in turn, the Chief Executive Officer is required to submit a report and recommendation to Council. The Panel and Chief Executive Officer recommended that Council could benefit from a low contract price if it implemented the action plan clearly identified in your Report.

Although the Council did not accept my recommendation in its entirety, the Council nevertheless put in place an action plan which was intended to overcome the concerns identified by the Panel, Council's legal adviser and the independent road contractor.

The action plan directed by Council required that:

- *Council representatives meet with the lowest tenderer with a view to reaching an agreement on any outstanding matters and gaining assurance of their acceptance of the contract offered;*
- *Council and the contractor undertake a joint survey of road conditions to determine what works will be necessary to reach the required service levels;*
- *a Contract Supervisor be appointed to carry out appropriate supervision of the contract; and*
- *a transitional plan be prepared.*

Since the commencement of the contract, there have been problems interpreting and implementing the contractor's obligations as required by the specification. Nevertheless, there was, and still is, a genuine willingness by Council and the contractor to make the contract a success even though there have been differences in interpretation of the specification.

Council is confident that it has undertaken the steps identified in your conclusion but, having done so, it is clear that by taking these steps Council was not able to avoid the occurrence of the problems outlined in the Report. On the other hand, had Council and the Contractor not vigorously pursued a course of action to minimise the potential of problems worsening, this contract may, by now, have failed.

□ **RESPONSE** provided by Deputy Secretary, Local Government, Planning and Market Information

The Office of Local Government will, in 1998-99, co-operate with VicRoads and municipalities to develop Best Practice Guidelines for Road Maintenance Contract specifications.



COMPETITIVE TENDERING ARRANGEMENTS AT THE CITY OF GREATER DANDENONG

3.3.177 In August 1997, the Office of Local Government within the Department of Infrastructure requested that I review the processes that culminated in the City of Greater Dandenong awarding 3 contracts for horticultural, park and sports services to an internal service provider contrary to the recommendation made by council’s tender evaluation panel to award the contracts to the lowest priced tenderer, being an external party.

Notification and assessment of tenders

3.3.178 The responsibilities of the City of Greater Dandenong include the effective management of landscaped parks, bushland reserves, tree revegetation areas, annual and perennial flower beds, and sporting fields. The use and enjoyment of these environmental assets by the local community require regular servicing, maintenance, and enhancement.

3.3.179 In November 1996, as part of council’s planned program of market testing the provision of council services, press advertisements sought expressions of interest from interested parties to provide horticultural, park and sporting ground services.

3.3.180 Four submissions were subsequently received, comprising an in-house bid and bids from 3 external providers. In accordance with normal practice, the council established a tender evaluation panel which reviewed the submissions and recommended that the in-house business unit and 2 external service providers be invited to submit detailed tenders as they met the key selection criteria. The council formally approved the panel’s recommendation in February 1997.

3.3.181 The nominated service providers were invited to tender for either one or more of the 3 separate contracts covering horticultural, parks, and sports services. Documentation provided to all tenderers for each service covered:

- form of the agreement;
- format of the tender;
- general conditions of the contract;
- service specifications; and
- contract schedules.

3.3.182 The following selection criteria were established by the council, and advised to tenderers, as a basis for evaluating the tenders received:

- financial capability to perform;
- tendered price;
- demonstrated experience and ability to deliver the specified service;
- capability to develop and work to a program that provided services to a specified standard;



- management capability and qualifications;
- transition plan for both commencement and expiration of the contract; and
- relevance and quality of tendered references.

3.3.183 Tenders closed in March 1997, at which time only 2 tenders were received, comprising an in-house bid and an external bid for all 3 contracts.

3.3.184 The tenders were subsequently evaluated by a panel consisting of 7 members, including 2 members from the panel established to review the expression of interests. The panel convened on 7 occasions during April and May 1997 to examine and clarify various financial and operational aspects of both tenders. Neither tenderer was invited to re-price any part of their tender or advised of the prices tendered by their competitor.

3.3.185 Following the completion of the panel’s discussions with the 2 tenderers, an evaluation of the tenders against the selection criteria was undertaken which indicated that the bid tendered by the external service provider was superior to that submitted by the in-house team. **The prices tendered by the in-house unit and the external provider were \$8.99 million and \$7.23 million, respectively, a difference of \$1.76 million. This price variance reflected differences in the proposed level of resourcing offered by each tenderer to meet the required contract specification.**

3.3.186 Following reference checks, discussions and observation of work and resource utilisation practices, the panel concluded that the external provider could meet the contract specifications within the resource levels outlined in the tender.

3.3.187 Subsequently, in June 1997, the panel recommended to council that it accept the tender by the external provider for horticultural, parks and sports services for a price of \$7.23 million.

Awarding of the contracts

3.3.188 Notwithstanding the tender evaluation panel’s recommendation to award the contracts to the external provider, councillors formally resolved at a public meeting on 10 June 1997 to award the contracts to the in-house provider effective from 1 July 1997, having regard to the following issues:

- local employment opportunities offered by each tenderer;
- concern over the potential loss of organisational capacity in the parks area;
- concern over the impact on the skill base of council’s staff;
- the likely adverse financial impact of redundancy payments;
- the level of support expressed for the in-house provider by local sporting organisations; and
- the impact on the level of potential competition for future parks contracts.

3.3.189 Both tenderers were formally advised of the council’s decision to award the 3 contracts to the in-house team on 13 June 1997.



Litigation initiated by external service provider

3.3.190 In December 1997, a writ was lodged in the Victorian Supreme Court on behalf of the external provider seeking damages against the council in excess of \$1.5 million. The writ alleges loss of profit under the contract arising from council's failure to evaluate the contract in accordance with the tender evaluation criteria and to give the provider an opportunity to submit a tender conforming with revised criteria.

3.3.191 It is my intention to finalise the review of these contracting arrangements once the legal action, which remained pending as at the date of preparation of this Report, is concluded.

RESPONSE provided by Deputy Secretary, Local Government, Planning and Market Information

No comments are submitted pending the outcome of the Supreme Court proceedings commenced during December 1997, by the unsuccessful tenderer.



**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>
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MATTERS RESOLVED OR ACTION COMMENCED

LOCAL GOVERNMENT

<i>Ministerial Portfolios, May 1997, pp. 86-99.</i>	A significant number of councils failed to meet the legislated reporting deadline.	Significant improvement noted in current year - see Part 3.3 of this Report.
	Councils did not disclose related party transactions of councillors and key officers within their annual financial statements.	The Office of Local Government issued a <i>Best Practice Guide</i> for the 1996-97 financial year which recommends disclosure of related party transactions. Also see Part 3.3 of this Report.
	Councils had not undertaken reviews of contaminated land.	The Office of Local Government has monitored councils' action in reviewing contaminated land.

URBAN LAND CORPORATION (formerly Urban Land Authority)

<i>Ministerial Portfolios, May 1996, pp. 170-1.</i>	The lower than expected level of lot sales at the Lynbrook estate, situated at Lyndhurst, south-east of Melbourne, resulted in a deficit of \$284 000 being incurred on the project in the 1994-95 financial year.	The Urban Land Corporation (ULC) has continued to closely monitor the performance of the Lynbrook Estate. In accordance with financial reporting obligations, the Authority obtained an independent valuation of the estate which indicated that a higher return may be obtained from the sale of the estate. On this basis, the estate was offered for sale but no acceptable offer was received. A strategic decision to continue to develop the estate was therefore taken. The ULC believes that this action will provide a product more closely aligned to current market needs and will enable recovery of all costs associated with development of the estate.
<i>Ministerial Portfolios, May 1996, pp. 171-2.</i>	As the work undertaken by the Authority in certain areas is similar in nature to that performed by other government agencies, scope may exist for some rationalisation with potential for cost savings and more effective use of available expertise.	Following a government review of the role of the Urban Land Authority in 1996, the Victorian Government corporatised the Authority, with proclamation of the Urban Land Corporation Act on 3 February 1998. The new Corporation will continue the work of the former Authority in undertaking residential developments. It will also provide consultancy services in land development and project management. The Corporation will compete on equal terms with the rest of the market.



**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>
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NO ACTION TAKEN

PUBLIC TRANSPORT

<i>Ministerial Portfolios, May 1989, p. 236.</i>	The adequacy and quality of disclosure within the financial reports of the transport authorities is inadequate as financing costs related to centralised debt are not included.	Position unchanged. Finance costs are reported centrally by the Government.
<i>Ministerial Portfolios, May 1997, p. 121.</i>	The Department of Infrastructure has not performed a post-implementation review of the contracting-out of the Melbourne to Warrnambool and Melbourne to Cobram services and, accordingly, there is a possibility that the experiences gained from these arrangements may not be factored into future privatisation proposals.	Position unchanged.

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**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>
COMPLETED AUDITS				
Department of Infrastructure	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	29 Aug. 1997	29 Aug. 1997
PLANNING AND LOCAL GOVERNMENT				
Architects Registration Board of Victoria	30 June 1997	" "	18 Sept. 1997	24 Sept. 1997
Building Control Commission	30 June 1997	" "	19 Aug. 1997	2 Sept. 1997
Docklands Authority	30 June 1997	" "	29 Aug. 1997	29 Aug. 1997
Heritage Council	30 June 1996	" "	21 Aug. 1997	8 Sept. 1997
Melbourne City Link Authority	30 June 1997	" "	13 Oct. 1997	14 Oct. 1997
Plumbers, Gasfitters and Drainers Registration Board (b)	Period 1 July 1996 to 23 March 1997	" "	27 June 1997	7 July 1997
Urban Land Authority	30 June 1997	" "	27 Aug. 1997	29 Aug. 1997
ROADS AND PORTS				
Marine Board of Victoria	30 June 1997	" "	3 Sept. 1997	3 Sept. 1997
Roads Corporation	30 June 1997	" "	28 Aug. 1997	28 Aug. 1997
TRANSPORT				
Public Transport Corporation	30 June 1997	" "	28 Aug. 1997	28 Aug. 1997

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - continued

<i>Entity</i>	<i>Financial year ended</i>	<i>Reporting to Minister for Planning and Local Government</i>	<i>Financial statements signed by entity</i>	<i>Auditor-General's report signed</i>
COMPLETED AUDITS - continued				
LOCAL GOVERNMENT				
Alpine Shire Council	30 June 1997	30 Sept. <i>Local Government Act 1989, s.126.</i>	26 Aug. 1997	19 Sept. 1997 (b)
Ararat Rural City Council	30 June 1997	" "	19 Aug. 1997	19 Sept. 1997
Ballarat City Council	30 June 1997	" "	27 Aug. 1997	29 Sept. 1997
Banyule City Council	30 June 1997	" "	1 Sept. 1997	23 Sept. 1997
Bass Coast Shire Council	30 June 1997	" "	12 Nov. 1997	13 Nov. 1997
Baw Baw Shire Council	30 June 1997	" "	28 Aug. 1997	19 Sept. 1997
Bayside City Council	30 June 1997	" "	25 Aug. 1997	30 Sept. 1997
Boroondara City Council	30 June 1997	" "	8 Sept. 1997	10 Sept. 1997
Brimbank City Council	30 June 1997	" "	26 Aug. 1997	26 Sept. 1997
Buloke Shire Council	30 June 1997	" "	20 Nov. 1997	25 Nov. 1997
Campaspe Shire Council	30 June 1997	" "	11 Sept. 1997	29 Sept. 1997
Cardinia Shire Council	30 June 1997	" "	1 Sept. 1997	26 Sept. 1997
Casey City Council	30 June 1997	" "	22 Aug. 1997	25 Sept. 1997
Casey - Cardinia Regional Library Corporation	30 June 1997	" "	21 Aug. 1997	25 Sept. 1997
Central Highlands Regional Library Corporation	30 June 1997	" "	1 Sept. 1997	2 Oct. 1997
Central Goldfields Shire Council	30 June 1997	" "	25 Aug. 1997	10 Sept. 1997
CityWide Service Solutions Pty Ltd	30 June 1997	" "	17 Sept. 1997	23 Sept. 1997
Colac-Otway Shire Council	30 June 1997	" "	26 Aug. 1997	26 Sept. 1997

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - continued

<i>Entity</i>	<i>Financial year ended</i>	<i>Reporting to Minister for Planning and Local Government</i>	<i>Financial statements signed by entity</i>	<i>Auditor-General's report signed</i>
COMPLETED AUDITS - continued				
LOCAL GOVERNMENT - continued				
Corangamite Shire Council	30 June 1997	30 Sept. <i>Local Government Act 1989, s.126.</i>	26 Aug. 1997	26 Sept. 1997
Corangamite Regional Library Corporation	30 June 1997	" "	26 Aug. 1997	26 Sept. 1997
Darebin City Council	30 June 1997	" "	28 Aug. 1997	26 Sept. 1997
Delatite Shire Council	30 June 1997	" "	27 Aug. 1997	30 Sept. 1997 (b)
East Gippsland Shire Council	30 June 1997	" "	27 Aug. 1997	12 Sept. 1997
Eastern Regional Library Corporation	30 June 1997	" "	11 Nov. 1997	20 Nov. 1997
Frankston City Council	30 June 1997	" "	22 Sept. 1997	23 Sept. 1997
Gannawarra Shire Council	30 June 1997	" "	29 July 1997	25 Aug. 1997
Geelong Regional Library Corporation	30 June 1997	" "	21 Sept. 1997	9 Oct. 1997
Glen Eira City Council	30 June 1997	" "	1 Sept. 1997	30 Sept. 1997
Glenelg Shire Council	30 June 1997	" "	25 Aug. 1997	26 Sept. 1997
Glenelg Regional Library Corporation	30 June 1997	" "	3 Sept. 1997	30 Sept. 1997
Golden Plains Shire Council	30 June 1997	" "	16 Sept. 1997	29 Oct. 1997
Goulburn Valley Regional Library Corporation	30 June 1997	" "	28 Aug. 1997	30 Sept. 1997
Greater Bendigo City Council	30 June 1997	" "	29 Sept. 1997	30 Sept. 1997
Greater Dandenong City Council	30 June 1997	" "	13 Oct. 1997	17 Oct. 1997 (b)
Greater Geelong City Council	30 June 1997	" "	28 Aug. 1997	30 Sept. 1997
Greater Shepparton City Council	30 June 1997	" "	20 Aug. 1997	30 Sept. 1997

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - continued

<i>Entity</i>	<i>Financial year ended</i>	<i>Reporting to Minister for Planning and Local Government</i>	<i>Financial statements signed by entity</i>	<i>Auditor-General's report signed</i>
COMPLETED AUDITS - continued				
LOCAL GOVERNMENT - continued				
Hepburn Shire Council	30 June 1997	30 Sept. <i>Local Government Act 1989, s.126.</i>	27 Oct. 1997	24 Nov. 1997
High Country Regional Library Corporation	30 June 1997	" "	25 Nov. 1997	25 Nov. 1997
Hindmarsh Shire Council	30 June 1997	" "	1 Sept. 1997	29 Sept. 1997
Hobsons Bay City Council	30 June 1997	" "	26 Aug. 1997	10 Oct. 1997
Horsham Rural City Council	30 June 1997	" "	7 Oct. 1997	13 Oct. 1997
Hume City Council	30 June 1997	" "	23 Sept. 1997	23 Sept. 1997
Hume-Moonee Valley Regional Library Corporation	30 June 1997	" "	1 Oct. 1997	16 Oct. 1997
Indigo Shire Council	30 June 1997	" "	26 Aug. 1997	30 Sept. 1997
Kingston City Council	30 June 1997	" "	28 Aug. 1997	25 Sept. 1997
Knox City Council	30 June 1997	" "	2 Sept. 1997	26 Sept. 1997
La Trobe Shire Council	30 June 1997	" "	26 Sept. 1997	2 Oct. 1997
Loddon Shire Council	30 June 1997	" "	28 Aug. 1997	25 Sept. 1997
Macedon Ranges Shire Council	30 June 1997	" "	2 Sept. 1997	22 Oct. 1997 (b)
Manningham City Council	30 June 1997	" "	27 Oct. 1997	29 Oct. 1997
Maribyrnong City Council	30 June 1997	" "	28 Aug. 1997	30 Sept. 1997
Maroondah City Council	30 June 1997	" "	26 Aug. 1997	6 Oct. 1997
Melbourne City Council	30 June 1997	" "	17 Sept. 1997	23 Sept. 1997
Melton Shire Council	30 June 1997	" "	26 Aug. 1997	26 Sept. 1997
Mildura Rural City Council	30 June 1997	" "	1 Sept. 1997	6 Oct. 1997

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SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - continued

<i>Entity</i>	<i>Financial year ended</i>	<i>Reporting to Minister for Planning and Local Government</i>	<i>Financial statements signed by entity</i>	<i>Auditor-General's report signed</i>
COMPLETED AUDITS - continued				
LOCAL GOVERNMENT - continued				
Mitchell Shire Council	30 June 1997	30 Sept. <i>Local Government Act 1989, s.126.</i>	21 Aug. 1997	15 Sept. 1997
Moira Shire Council	30 June 1997	" "	28 Feb. 1998	30 March 1998 (b)
Monash City Council	30 June 1997	" "	24 Sept. 1997	24 Sept. 1997
Moonee Valley City Council	30 June 1997	" "	12 Sept. 1997	16 Sept. 1997
Moorabool Shire Council	30 June 1997	" "	27 Aug. 1997	26 Sept. 1997
Moreland City Council	30 June 1997	" "	1 Sept. 1997	25 Sept. 1997
Mornington Peninsula Shire Council	30 June 1997	" "	1 Sept. 1997	24 Sept. 1997
Mount Alexander Shire Council	30 June 1997	" "	10 Oct. 1997	21 Oct. 1997
Moyne Shire Council	30 June 1997	" "	2 Sept. 1997	8 Oct. 1997
Murrundindi Shire Council	30 June 1997	" "	26 Aug. 1997	23 Sept. 1997
Nillumbik Shire Council	30 June 1997	" "	26 Aug. 1997	29 Sept. 1997
North Central Goldfields Regional Library Corporation	30 June 1997	" "	28 Aug. 1997	12 Sept. 1997
Northern Grampians Shire Council	30 June 1997	" "	28 Aug. 1997	6 Oct. 1997 (b)
Port Phillip City Council	30 June 1997	" "	8 Sept. 1997	7 Oct. 1997
Prahran Market Pty Ltd	30 June 1997	" "	20 Aug. 1997	19 Sept. 1997
Pyrenees Shire Council	30 June 1997	" "	19 Aug. 1997	7 Oct. 1997
Queenscliffe Borough Council	30 June 1997	" "	30 Sept. 1997	9 Oct. 1997
Regent Management Co.	30 June 1997	" "	25 Sept. 1997	6 Oct. 1997
South Gippsland Shire Council	30 June 1997	" "	28 Aug. 1997	30 Sept. 1997

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - continued

<i>Entity</i>	<i>Financial year ended</i>	<i>Reporting to Minister for Planning and Local Government</i>	<i>Financial statements signed by entity</i>	<i>Auditor-General's report signed</i>
COMPLETED AUDITS - continued				
LOCAL GOVERNMENT - continued				
Southern Grampians Shire Council	30 June 1997	30 Sept. <i>Local Government Act 1989, s.126.</i>	1 Sept. 1997	7 Oct. 1997
Stonnington City Council	30 June 1997	" "	12 Sept. 1997	22 Oct. 1997
Strathbogie Shire Council	30 June 1997	" "	25 Aug. 1997	15 Sept. 1997
Surf Coast Shire Council	30 June 1997	" "	1 Sept. 1997	25 Sept. 1997
Swan Hill Rural City Council	30 June 1997	" "	25 Nov. 1997	26 Nov. 1997 (b)
Swan Hill Regional Library Corporation	30 June 1997	" "	15 Dec. 1997	18 Dec. 1997
Towong Shire Council	30 June 1997	" "	28 Aug. 1997	23 Sept. 1997
Wangaratta Rural City Council	30 June 1997	" "	21 Aug. 1997	12 Sept. 1997
Warrnambool City Council	30 June 1997	" "	2 Sept. 1997	26 Sept. 1997
Wellington Shire Council	30 June 1997	" "	4 Sept. 1997	9 Oct. 1997
West Wimmera Shire Council	30 June 1997	" "	26 Aug. 1997	8 Oct. 1997
West Gippsland Regional Library Corporation	30 June 1997	" "	2 Sept. 1997	2 Oct. 1997 (b)
Whitehorse City Council	30 June 1997	" "	1 Sept. 1997	29 Sept. 1997
Whitehorse Manningham Regional Library Corporation	30 June 1997	" "	1 Sept. 1997	9 Oct. 1997
Whittlesea City Council	30 June 1997	" "	29 Aug. 1997	13 Oct. 1997
Wimmera Regional Library Corporation	30 June 1997	" "	7 Oct. 1997	16 Oct. 1997
Wodonga Rural City Council	30 June 1997	" "	15 Sept. 1997	1 Oct. 1997
Wyndham City Council	30 June 1997	" "	22 Sept. 1997	13 Oct. 1997
Yarra City Council	30 June 1997	" "	29 Sept. 1997	30 Sept. 1997

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SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - continued

<i>Entity</i>	<i>Financial year ended</i>	<i>Reporting to Minister for Planning and Local Government</i>	<i>Financial statements signed by entity</i>	<i>Auditor-General's report signed</i>
COMPLETED AUDITS - continued				
LOCAL GOVERNMENT - continued				
Yarra Ranges Shire Council	30 June 1997	30 Sept. <i>Local Government Act 1989, s.126.</i>	10 Sept. 1997	14 Oct. 1997
Yarra Plenty Regional Library Corporation	30 June 1997	" "	3 Sept. 1997	29 Sept. 1997
Yarra-Melbourne Regional Library Corporation	30 June 1997	" "	16 Sept. 1997	16 Sept. 1997
Yarriambiack Shire Council	30 June 1997	" "	29 Aug. 1997	7 Oct. 1997

(a) Board abolished on 23 March 1997. New entity, Plumbing Industry Board, was established on 24 March 1997.

(b) Qualified audit report issued.

Part 3.4

Justice

KEY FINDINGS

Community-based orders by courts

- There was 6 000 community correction orders during 1996-97 representing a 3 per cent increase over the previous financial year. However, 27 per cent of these orders were revoked or breached.

Paras 3.4.11 to 3.4.12 and Paras 3.4.22 to 3.4.24

- The effectiveness of the administration of community correction orders could be improved by greater care being taken to ensure that assessments to support the allocation of offenders to appropriate projects are adequately documented and there is effective monitoring of offender's progress in meeting the requirements of the orders.

Paras 3.4.13 to 3.4.21

Management of infant investment trust accounts by courts

- An important element of the responsibilities of the respective judiciaries is the management of funds paid into the courts as a result of legal judgements and held in trust on behalf of persons under the age of 18 years or those who have a legal disability. At 30 June 1997, around \$318 million was held in trust funds by the State's major judicial institutions.

Paras 3.4.30 to 3.4.34

- Investment system enhancements should be implemented at the County Court and the Victims of Crime Assistance Tribunal to enable the regular production of transaction statements to trust fund beneficiaries.

Paras 3.4.35 to 3.4.39

Collection of fines and fees

- At 30 June 1997, \$324.5 million of fines, which were legally payable, were outstanding representing an increase of \$53.5 million (20 per cent) since the 1994-95 financial year.

Paras 3.4.40 to 3.4.47 and Paras 3.4.60 to 3.4.63

- Of the \$234.6 million payable to the State, 79 per cent of this amount has been outstanding for more than 12 months.

Paras 3.4.64 to 3.4.65



KEY FINDINGS - continued

Collection of fines and fees - continued

- The Department of Justice has over a number of years introduced various initiatives to improve its effectiveness in the enforcement and collection of fines and is considering a number of other initiatives including those raised by the Public Accounts and Estimates Committee in September 1997.

Paras 3.4.44 to 3.4.59

- The *Magistrates Court (Amendment) Act* 1996 was passed by the Parliament which resulted in debts of \$112 million no longer being legally collectable.

Paras 3.4.66 to 3.4.69

Charging for police services

- The Police (Charges) Regulations 1992 provide the legislative authority for Victoria Police to charge for services provided at sporting and other events, however the Regulations currently inhibit the recovery of the full cost of providing these services.

Paras 3.4.81 to 3.4.88

- Audit found significant delays in the raising of accounts for Police services at a substantial number of events and identified delays in the approval of applications for the waiving of Police charges for certain events.

Paras 3.4.89 to 3.4.90 and Paras 3.4.77 to 3.4.80



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 1996-97 financial year.

**TABLE 3.4A
MINISTERIAL RESPONSIBILITIES FOR PUBLIC BODIES WITHIN THE JUSTICE SECTOR**

<i>Ministerial portfolio</i>	<i>Entities subject to audit</i>
Attorney-General	Legal Practice Board Office of the Director of Public Prosecutions Office of the Legal Ombudsman Queen Victoria Women's Centre Trust Senior Master of the Supreme Court Solicitors' Guarantee Fund Victoria Legal Aid Victorian Electoral Commission Victorian Financial Institutions Commission Victorian Institute of Forensic Medicine
Police and Emergency Services	Country Fire Authority Metropolitan Fire Brigades Board National Institute for Forensic Science National Police Ethic Advisory Bureau Office of the Chief Commissioner of Police

3.4.3 Comment on matters of significance arising from the audit of entities within the Justice sector is provided below.

COMMUNITY-BASED ORDERS BY COURTS

Community correction orders

3.4.4 Under the *Sentencing Act* 1991, the Victorian judiciary has a range of custodial and non-custodial measures available to it when sentencing an offender. Non-custodial measures can take the form of community correction orders which require offenders to undertake unpaid community work, rehabilitation programs or both. The types of community correction orders available to the courts include:

- *Intensive correction* - Offenders are required to undertake 8 to 12 hours of unpaid community work on a weekly basis;
- *Community-based (community work as one of more conditions)*. In addition to other conditions, offenders are required to undertake 8 to 500 hours of unpaid community work;



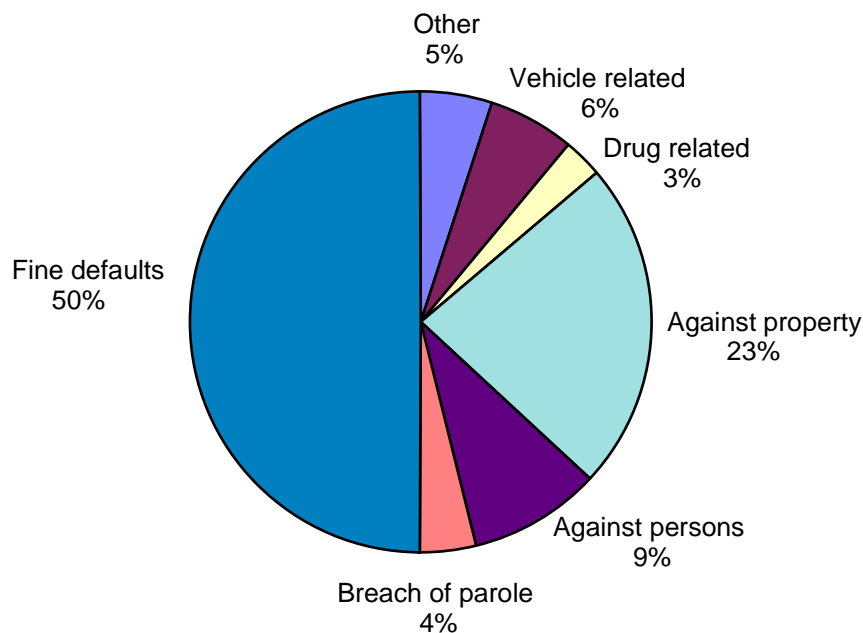
- *Community-based (community work as the only condition)*. Offenders are required to undertake 8 to 250 hours of unpaid community work;
- *Community-based (in default of a fine)*. In lieu of outstanding fines, offenders are required to undertake community work; and
- Other orders such as Adult Parole Board orders.

3.4.5 In the 1996-97 financial year, community correction orders resulted mainly from individuals:

- defaulting on the payment of fines (50 per cent);
- committing offences against property (23 per cent); and
- committing offences against other persons (9 per cent).

3.4.6 Chart 3.4B outlines the type of offences resulting in the issue of community correction orders.

CHART 3.4B
TYPES OF OFFENCES RESULTING IN THE ISSUE OF
COMMUNITY CORRECTION ORDERS
(per cent)



3.4.7 Community correction orders are administered by Community Correctional Services (CCS), a business unit within CORE - The Public Correctional Enterprise, which is a service agency providing prison and community-based correctional services within the Department of Justice.

3.4.8 The primary role of CCS, through its management of court orders and facilitation of appropriate rehabilitation programs and community work, is to ensure orders made by the courts are adhered to by offenders. CCS employs some 250 staff and manages around 7 500 offenders each year at a cost of approximately \$12 million.

3.4.9 In October 1997, CORE conducted an internal review of the Community Work Program managed by CCS, which resulted in a number of recommendations for improving its operation. The findings of the review are referred to throughout this Part of the Report.

Trends in community correction orders

3.4.10 A recent Council of Australian Governments report on government services stated that the average number of offenders on community correction orders per 100 000 of the general population in Victoria was 201, which was 196 lower than the national average of 397 offenders. In addition, the report indicated that the average number of prisoners per 100 000 population, 17 years of age and over, was 49 which was 71 lower than the national average of 120. These figures reflect Victoria's relatively lower level of offences compared with other States.

3.4.11 Of the 83 600 convictions recorded in the 1996-97 financial year, 36 300 (43.4 per cent) resulted in fines, 6 000 (7.2 per cent) resulted in community correction orders, 4 700 (5.6 per cent) resulted in custodial sentences and 36 600 (43.8 per cent) resulted in either suspended sentences, bonds or other sentences. **In addition, there was a 3 per cent increase in the number of community correction orders during the 1996-97 financial year.**

3.4.12 The major reason for the increased use of these orders during recent years is the benefits they provide which include:

- reduced cost to the public, as the average annual operating cost per offender under a community correction order is around \$2 200 compared with a prison sentence costing around \$53 000 per annum;
- direct benefit to the community where the order requires offenders to undertake community work;
- provide a better environment for rehabilitation by enabling offenders to remain in the community under supervision, rather than being placed in prisons where they may be subject to the influences of hardened criminals;
- more likely to modify behaviour and reduce the likelihood of re-offending by providing specific courses and rehabilitation programs; and
- provide offenders with valuable skills and work habits, which may assist them in finding paid employment.

Management of community correction orders

3.4.13 The procedure adopted by CCS for the management of offenders on community correction orders involve the following key functions:

- assignment of offenders to case managers;
- assessing the risks associated with offenders;
- treatment of offenders for substance abuse and psychological disorders where appropriate;



- assignment of offenders to specific community work; and
- ongoing supervision and case management.

3.4.14 In respect of community correction orders, CCS requires case managers to prepare individual management plans designed to address the needs of each high risk offender, within 3 weeks of the commencement of the court order. CCS staff have recently commenced monitoring the preparation and ongoing management of these plans.

3.4.15 **Audit review of these plans disclosed instances where plans were not prepared on a timely basis and in one instance where a plan was not prepared.**

3.4.16 Community work, undertaken by offenders, involves them providing services to non-profit or government agencies without monetary compensation and includes community projects such as maintenance of schools and parks, and involvement in activities such as *Clean Up Australia Day*.

3.4.17 In assigning offenders to community programs consideration is given to the:

- degree of supervision required of the offender;
- history of offending and risk of re-offending;
- rehabilitation of the offender;
- offender's physical and geographical constraints; and
- offender's skills, background and employment history.

3.4.18 The participation of offenders in community projects, often in close contact with vulnerable sections of the community, makes the placement of offenders to appropriate projects critical.

3.4.19 During a review of CCS case files, audit noted that the standard of assessments undertaken by case managers were of varying quality and the files often lacked sufficient detail regarding these assessments. An internal review completed by CCS in October 1997 found that:

- Around 86 per cent of offenders commenced community work within 2 weeks of receiving the order, comparing favourably with CCS's target of 85 per cent. The remainder were generally placed in a program within 4 weeks. However, in approximately half of the cases where offenders did not commence work within 2 weeks, reasons for the delays were not documented on the case files;
- Formal processes were not in place to determine an appropriate level of supervision relative to the assessed risk of each offender throughout the duration of the order; and
- There were no formal procedures for maintaining records of hours worked by offenders.

.....

3.4.20 As a result of the internal review, CCS has prepared a strategy for addressing the issues contained in the report. In addition, a consultant was engaged to undertake an organisational review of the operations of CCS in January 1998.

3.4.21 In order to improve the effectiveness of the administration of community correction orders, CCS should:

- **exercise greater care to ensure that assessments undertaken by case managers are adequately documented to support the allocation of offenders to appropriate programs and projects; and**
- **ensure that there is effective monitoring of offenders' progress in meeting the requirements of the orders.**

Breaches of orders

3.4.22 A breach of the conditions contained in community correction orders may result in a modification or revocation of the order. **For the 1996-97 financial year, 27 per cent of community correction orders were revoked or breached (1995-96 financial year, 24 per cent).**

3.4.23 Discussions with CCS staff indicated that breaches of orders by offenders occur due to a number of factors including absenteeism, non-compliance with directions, inappropriate behaviour or further re-offending.

3.4.24 The internal review conducted by CCS in October 1997 identified many instances where case files did not contain sufficient information to determine exactly when absences were notified and accordingly, it was not possible to determine whether these absences were investigated on a timely basis.

Information systems

3.4.25 Information relevant to the management of community correction orders is held in the following forms:

- *Manual case files on each offender* - Contain personal details regarding the offender, including their physical and geographic constraints, background and employment history, the degree of supervision required, documentation on their progress, prior offences and their individual management plan;
- *Offender Automated Search and Inquiry System (OASIS)* - Computerised system owned and maintained by the Office of the Correctional Services Commissioner, recording details of offenders under supervision by CCS;
- *Prisoner Information Management System (PIMS)* - Computerised system, owned and maintained by the Office of the Correctional Services Commissioner, recording information on offenders who have been jailed in Victoria; and
- *Law Enforcement Assistance Program (LEAP)* - Computerised system, maintained by the Office of the Chief Commissioner of Police, recording criminal case histories.



3.4.26 Important decisions regarding the management of community correction orders are required to be made by CCS. Where relevant information for decision-making is incomplete, inaccurate or difficult to access, it can have a significant impact on offenders and the community.

3.4.27 To enhance the management of community correction orders, consideration should be given to the computerisation of the current manual case files and the interface of the various information systems which hold relevant data on offenders.

Evaluation of projects and programs

3.4.28 The audit review identified that the following processes had been established by CCS to evaluate the effectiveness of community correction orders in providing benefits to both the community and offenders:

- questionnaires have been sent to community agencies and informal feedback obtained from these agencies and offenders, which are used to evaluate the relevant programs and projects;
- until recent times, the only performance information collected was the number of community corrections orders successfully completed and the cost to the Department of the placement of offenders on these orders; and
- a system of case reviews by senior officers.

3.4.29 In order to assist in assessing the effectiveness of community correction orders, consideration should be given to:

- **collecting and reporting further relevant performance information, such as the number of individuals placed on community orders who have re-offended and the costs incurred by service agencies in supplying treatment programs to offenders;** and
- developing more sophisticated evaluation techniques such as independent assessments of programs, assessment of offender behaviour prior to commencing and subsequent to the completion of the programs, and detailed post-order appraisals undertaken in conjunction with program providers and offenders.

□ *RESPONSE provided by Secretary, Department of Justice*

Management of community correction orders

Preparation and authorisation of Individual Management Plans (IMP) are one of a number of Service Delivery Outcomes (SDO) which CCS reports on a monthly basis to the Correctional Services Commissioner. In July 1997, the requirement for IMPs to be authorised within 3 weeks replaced a previous requirement for this to be done in 6 weeks. This SDO is currently being reviewed by CCS and the Office of the Correctional Services Commissioner. The Department is satisfied that CCS has put in place a number of strategies to address concerns in relation to the performance of this SDO and facilitate the movement from the 6 week to 3 week target.



□ **RESPONSE** provided by Secretary, Department of Justice - continued

Management of community correction orders - continued

CCS has recently undertaken a major organisational review, including a review of the effectiveness of administration of community correction orders. The Department is currently finalising proposed new structures and business practices which will address the issues identified above. A key outcome of the organisation review is a proposal to introduce a case management model utilising multi-disciplinary teams. This is consistent with best practice in the management of offenders.

Breeches of orders

In response to the outcomes of the internal review completed in October 1997, CCS has developed actions and an implementation strategy which will address this issue.

Information systems

The need to enhance the management of community correction orders by introducing computerised case files has been identified as a priority in a number of Department of Justice reviews: namely Project Pathfinder and the Office of the Correctional Services Commissioner's Sentence Management Unit review. The need for computerised files has also been identified as a priority in CORE's IT Strategy.

The Office of the Correctional Services Commissioner is currently carrying out a review of the existing IT platform for the corrections industry in Victoria and the Department is satisfied recommendations from these processes will lead to more efficient case management.

Evaluation of projects and programs

The CCS organisational review has identified both issues raised in this selection. It is anticipated that the proposed strategy to develop formal partnering relationships with service providers will involve the development of measures to evaluate performance and costing of programmes. In addition, CCS is moving towards introducing a more sophisticated offender risk assessment tool and evaluation techniques which will assist in assessing an offenders overall performance.





MANAGEMENT OF INFANT INVESTMENT TRUST ACCOUNTS BY COURTS

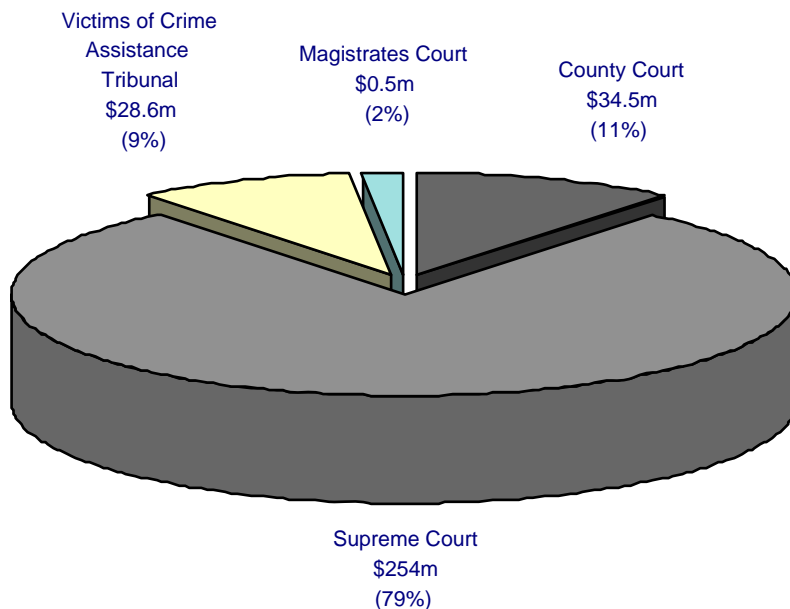
3.4.30 The Victorian judicial system consists of the Supreme Court (comprising the Court of Appeal and the Trial Division), County Court, Magistrates Court (including the Children’s Court and Coroner’s Court), Victims of Crime Assistance Tribunal and various boards and tribunals.

3.4.31 An important element of the responsibilities of the respective judiciaries is the management of funds paid into the courts as a result of legal judgements and held in trust on behalf of persons under the age of 18 years or those who have a legal disability.

3.4.32 At 30 June 1997, around \$318 million was held in trust funds by the State’s major judicial institutions, including \$254 million held by the Senior Master of the Supreme Court, \$28.6 million held by the Victims of Crime Assistance Tribunal, \$34 million held by the County Court and around \$500 000 held by the Magistrates Court. The trust funds managed by the Supreme Court were reported in its financial statements, while the remaining trust funds were reported in the financial statements of the Department of Justice.

3.4.33 Chart 3.4C illustrates the proportion of moneys held in trust by the key judicial institutions.

CHART 3.4C
TRUST FUNDS MANAGED BY COURTS, AT 30 JUNE 1997
 (\$million)





3.4.34 During the 1996-97 financial year, in their capacity as trustees, the County Court was responsible for 2 100 separate investment accounts, the Victims of Crime Assistance Tribunal was responsible for 3 400 separate investment accounts and the Magistrates Court was responsible for 180 separate investment accounts. In the case of the Supreme Court, all beneficiary trust accounts were pooled into a common fund.

Trust management deficiencies

3.4.35 A number of deficiencies were identified in the management by the courts of infant investment trust accounts.

3.4.36 While information systems operating at the County Court and the Victims of Crime Assistance Tribunal record details of amounts received to be managed on behalf of individual beneficiaries and any subsequent payments to beneficiaries, they do not record interest earned. As a result, it is not possible to reconcile the amounts held on behalf of all beneficiaries with the amounts recorded in the bank statement.

3.4.37 In addition, a number of compensation awards made by the Victims of Crime Assistance Tribunal and paid into trust accounts could not be traced to bank records. Following the acquisition of the State Bank of Victoria by the Commonwealth Bank, trust accounts held in the State Bank were electronically transferred to the Commonwealth Bank and allocated new account numbers. However, data transmission errors resulted in bank records not identifying all trust accounts held on behalf of the Victims of Crime Assistance Tribunal. Following an investigation by the Department, 214 previously unrecorded accounts, valued at \$1.2 million (including those referred to above), were identified.

3.4.38 Trustees of funds are generally required to periodically issue statements of accounts to their clients, detailing transactions during the relevant period. Audit found that the systems in operation at the County Court and the Victims of Crime Assistance Tribunal are not capable of producing periodic statements to beneficiaries.

3.4.39 **Investment system enhancements should be implemented at the County Court and the Victims of Crime Assistance Tribunal to enable interest revenue to be recorded against individual beneficiaries trust accounts and the regular production of transaction statements to trust fund beneficiaries. Furthermore, each trust account should be regularly reconciled to the bank records, with any discrepancies promptly investigated.**

RESPONSE provided by Secretary, Department of Justice

When reading the Report it is important to note that all interest earned on trust funds held on behalf of infants is paid on receipt to the relevant beneficiary account.

Terms of reference for a review of the constitutional, legislative and administrative framework, and the performance of the Courts in the management of funds for minors and persons with disabilities has recently been settled with the Supreme, County and Magistrates' Courts. The matters mentioned by the Auditor-General will be considered in the review.





COLLECTION OF FINES AND FEES

3.4.40 The Enforcement Management Unit (EMU) within the Department of Justice was formed in March 1994 through the amalgamation of the common operations of the Magistrates Court function known as the PERIN Court and the Sheriff’s Office of Victoria, to provide an integrated fines management system.

3.4.41 The PERIN Court is responsible for the enforcement of all government and non-government penalty infringement notices that are registered with the Court, while the Sheriff’s Office is responsible for the execution of civil and criminal court orders and warrants issued by courts in Victoria and the Federal Court.

- 3.4.42** The overall objectives of the EMU are to:
- implement policy and procedures for the efficient and cost-effective management of fine enforcement and to ensure the integrity of the judicial process;
 - improve revenue collection rates and reduce the level of outstanding court orders and warrants; and
 - ensure compliance with legislation and minimise the burden of work falling on the courts, while still protecting the individual’s rights at law.

3.4.43 Since the establishment of the PERIN Court in the 1986-87 financial year, audit has commented in several Reports to the Parliament on the high level of uncollected fines and costs. The main factors which have contributed to this unfavourable situation in the past have been inadequate and non-integrated computer systems and limitations in the powers of the Sheriff over the enforcement and collection of fines.

3.4.44 In particular, in my May 1996 *Report on Ministerial Portfolios*, it was reported that:

- despite productivity measures and amendments to legislation, the value of uncollected fines continued to rise;
- notwithstanding the substantial increase in uncollected fines and costs, the level of cash collections had decreased;
- a significant proportion of fines payable to the State had been outstanding for more than one year; and
- bad and doubtful debts in respect of amounts payable to the State continued to increase.

3.4.45 Following that Report, the Public Accounts and Estimates Committee of the Parliament conducted an inquiry into this issue and tabled its Report in September 1997. The Committee examined the fines collection system and made numerous recommendations to improve the effectiveness of the system.



3.4.46 The Committee’s recommendations included:

- creation of a new Act to govern the operation of the infringement notice system;
- development of guidelines to deal with offenders with medical, psychiatric or other special circumstances, which may justify waiving the infringement penalties;
- allowing fine payments to be made by direct debit against offender bank accounts or credit cards, or other means such as periodic payments; and
- amending legislation to give the Sheriff power to impose a charge on or execute against the defaulter’s real property, where the outstanding fines in total value exceed the dollar equivalent of 10 penalty units.

3.4.47 The Government’s response to the Committee’s recommendations was tabled in Parliament in April 1998. The Government has broadly accepted the Committee’s recommendations and is currently considering a number of initiatives.

Major departmental initiatives

3.4.48 The Department has over a number of years introduced various initiatives to improve its effectiveness in the enforcement and collection of fines. Audit undertook a review to assess the impact of these initiatives on the level of uncollected fines, doubtful debts and bad debts written-off. The results of this review are presented below.

Legislative amendments

3.4.49 Amendments to the *Magistrates Court (Amendment) Act* 1994, proclaimed in October 1994, provided the Sheriff with additional powers to facilitate the enforcement and collection of unpaid fines. These powers, which could be applied retrospectively, were as follows:

- the Sheriff may seize personal property or business assets of defaulters; and
- directors of body corporates may now be jointly and severally liable for the payment of fines imposed on body corporates.

3.4.50 Notwithstanding these amendments, the EMU has recognised the need for further legislative change to address certain inconsistencies in legislation relating to the PERIN and Open Courts, and inadequacies in the Sheriff’s enforcement powers.

3.4.51 Currently, the Department of Justice is conducting a review of all legislation relating to the enforcement of court orders and the management of fines with a view to developing an Infringement Notices Act. It is anticipated by the Department that the review will take 12 to 18 months to complete.

.....

Amalgamation of business units

3.4.52 There are 3 main business units which provide fine collection services within Government, namely, the Traffic Camera Office (TCO) and the Fixed Penalty Payments Office (FPPO) within Victoria Police, and the EMU business unit of the Department. Despite performing similar administrative functions, these business units operate independently of each other.

3.4.53 In 1995, the Department was allocated \$16.2 million in additional capital funding, of which \$7.2 million was provided to the EMU to enable the:

- amalgamation and re-engineering of the administrative processes of the EMU, TCO and FPPO;
- outsourcing of the amalgamated administrative processes; and
- development of an integrated computer system.

3.4.54 The balance of the funding was to be provided to Victoria Police for the purchase of new camera and image management technology. However, this decision has been revised to the extent that the entire ownership and operation of the traffic cameras will be transferred to a contractor who will provide Victoria Police with prosecutable images for enforcement.

3.4.55 The target date for finalising all contractual arrangements associated with the above tasks was 30 September 1996, with the anticipated project completion date set at the end of 1997. However, these anticipated completion dates have not been achieved. At the date of preparation of this Report, a preferred contractor had been recommended, with Ministerial approval of the appointment imminent. **Furthermore, the project is now expected to be completed in August 1999, some 2 years after the original planned completion date.**

3.4.56 The following factors contributed to the delays associated with the project:

- the complexity of the businesses and the issues involved;
- difficulties in developing an appropriate contractor payment formula and service measures, while maintaining the fundamental elements of the existing judicial system;
- difficulties in obtaining proposals from short-listed bidders that complied with tender requirements;
- uncertainty as to whether the project would be required to comply with Government Infrastructure Investment Guidelines; and
- difficulties associated with incorporating the commercialisation aspects of the project into the contract.

3.4.57 Of the \$16.2 million in additional capital funding received by the Department, \$4.5 million had been spent to date in the selection of the preferred contractor and additional initiatives to meet higher revenue targets. The Department is currently liaising with the Department of Treasury and Finance to resolve funding arrangements for future contractor payments and to determine whether the balance of the capital funding may be applied to meet such payments.

Productivity improvement initiatives

3.4.58 In addition to the abovementioned capital funding, the EMU was provided with the following supplementary recurrent funding:

- The retention of specified revenue, emanating from an agreement entered into with the Department of Treasury and Finance in July 1996 which allows the Department to retain filing fee revenue collected each year, over an agreed target base. Filing fees are charged to non-government agencies when they lodge an infringement notice at the PERIN Court. The amount of revenue retained in the 1996-97 financial year amounted to \$466 000; and
- An increase of \$1.6 million to the annual appropriation which commenced in the 1996-97 financial year.

3.4.59 The aim of the supplementary recurrent funding was to assist in the implementation of various productivity initiatives, including improved address validation and data matching processes, better targeting of debtors, and the introduction of flexible pay arrangements and a community education program.

Impact of initiatives on the collection of outstanding fines and costs

Level of uncollected fines

3.4.60 At 30 June 1997, \$324.5 million of fines were outstanding, representing an increase of \$53.5 million (20 per cent) since the 1994-95 financial year. Of this amount, \$234.6 million is payable to the State, of which \$75.5 million or 32 per cent is regarded as uncollectable and a further \$102.6 million or 43.7 per cent is regarded as doubtful. Accordingly, there has been a significant deterioration in the recoverability of total outstanding fines, with only \$76.1 million or 24 per cent (34 per cent, 30 June 1995) of such fines considered collectable. Table 3.4D details this position.

**TABLE 3.4D
UNCOLLECTED FINES AND COSTS
(\$million)**

Item	30 June 1997			30 June 1995
	Payable to the State	Payable to other bodies	Total	Total
Gross uncollected fines (a)(b)	234.6	89.9	324.5	271.0
Less:				
Cumulative provision for doubtful debts	(102.6)	(70.3)	(172.9)	(135.2)
Cumulative bad debt write-off (c)	(75.5)	-	(75.5)	(43.5)
Collectable debt	56.5	19.6	76.1	92.3

- (a) Does not include warrant execution costs which were deemed to be no longer legally collectable and were written-off as at 30 June 1997.
- (b) Gross uncollected fines represent the aggregate outstanding debt given that bad debts can only be written-off for accounting purposes but legally must remain on the Department's database as they are still legally collectable.
- (c) Bad debts were written-off for the first time in the 1994-95 financial year with the introduction of accrual accounting and have continued to be written-off annually, however, they remain legally payable.

3.4.61 The audit review further identified that in the 7 year period from the 1990-91 financial year to the 1996-97 financial year, the level of uncollected fines which remain legally payable to the State had increased from \$77.1 million to

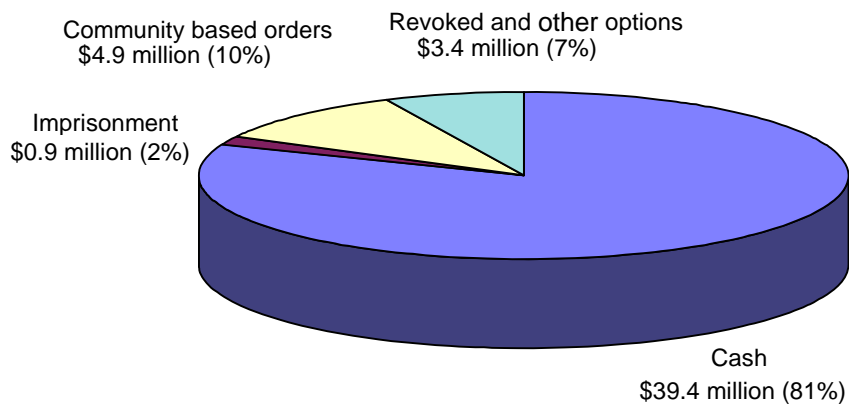


\$234.6 million, while fine clearances (which represent either cash collected, fines revoked or fines extinguished through the conversion to other penalties such as community based orders) have only increased from \$34.1 million to \$46.6 million.

3.4.62 The poor financial circumstances of many offenders and the inability of the Department to legally extinguish uncollected debts, has contributed to the increase in uncollected fines over time.

3.4.63 The settlement of uncollected fines and costs can be made in the form of cash payments or through a number of non-cash options, such as imprisonment and community-based orders. Chart 3.4E illustrates that, of the total fines settled during the 1996-97 financial year, 81 per cent (1994-95, 77 per cent) and 19 per cent (1994-95, 23 per cent) were settled through cash and non-cash options, respectively. Hence, there has been a slight increase in the level of cash settlements over the past 2 financial years.

**CHART 3.4E
PROPORTION OF FINES SETTLED THROUGH
CASH PAYMENTS AND NON-CASH OPTIONS,
1996-97 FINANCIAL YEAR**



Age analysis of uncollected fines

3.4.64 An analysis of uncollected fines payable to the State at 30 June 1997 disclosed that 79 per cent (30 June 1995, 75 per cent) had been outstanding for more than one year. Table 3.4F highlights that aged debts represent a significant portion of the uncollected fines and are gradually increasing.

**TABLE 3.4F
AGE ANALYSIS OF UNCOLLECTED FINES**

<i>Period outstanding</i>	<i>30 June 1997</i>		<i>30 June 1995</i>	
	<i>(\$m)</i>	<i>(%)</i>	<i>(\$m)</i>	<i>(%)</i>
Up to 1 year	46.5	20.7	47.4	24.5
1 to 2 years	35.2	15.7	35.4	18.3
2 to 3 years	31.6	14.1	30.9	16.0
more than 3 years	111.1	49.5	79.8	41.2
Total (a)	224.4	100.0	193.5	100.0

(a) The above analysis relates only to fines payable to the State. All police warrants were transferred from the Office of the Chief Commissioner of Police to the Department for collection in the 1991-92 financial year, however, the warrants are not able to be aged and accordingly have been excluded from the analysis.

3.4.65 The Department of Justice in its response to the Auditor-General's May 1996 *Report on Ministerial Portfolios*, stated that it would concentrate its efforts on recovering more recent fines and costs. During the current review, audit has been advised that a pilot project, focusing on more recent fines and costs commenced in February 1998 by the EMU. This project involves the PERIN Court Registrar performing address verification and follow-up activities in relation to Court Orders, prior to an electronic transfer of unactioned Court Orders to the Sheriff's database to enable follow-up by the EMU and, if necessary, the execution of a warrant. The feasibility of this initiative is to be assessed at the completion of the pilot program in June 1998.

Write-off of bad debts

3.4.66 The Department has developed criteria to enable a consistent approach to be applied to the write-off of bad debts for accounting purposes. It must be recognised that these debts legally remain payable. The criteria, which is applied to all uncollected fines owing to the State 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 has left an address and the Sheriff had been unable to identify his or her new address in the ensuing 12 months. The criteria does not apply to non-government fines, as these debtors are not controlled by the Department which acts as a collection agent on behalf of other organisations such as local councils.

3.4.67 In the 1996-97 financial year, the application of the above criteria to uncollected fines payable to the State have resulted in bad debt write-offs of \$26.6 million, bringing the aggregate value of bad debt write-offs for accounting purposes since the 1994-95 financial year to \$75.5 million.



3.4.68 During 1996, the procedures applied for the imposition and collection of fines and associated costs were subjected to an extensive legislative compliance audit by the Department. The departmental audit revealed a number of irregularities relating to the imposition of Sheriff fees and the re-issuing of expired warrants. As a result, the *Magistrates Court (Amendment) Act 1996* was passed by the Parliament which clarified that the EMU is not empowered to:

- impose and collect warrant execution costs at the point when warrants are issued; and
- automatically re-issue expired warrants (over 5 years old) without the leave of the Court.

3.4.69 The impact of the legislative amendments has resulted in debts of \$112 million no longer being legally collectable.

□ *RESPONSE provided by Secretary, Department of Justice*

Major departmental initiatives

While it is acknowledged that the project has taken longer to deliver than the early project estimates, this has been due largely to the need to carefully measure and analyse each of the 58 steps and permutations in the fines management process starting with the original detection of an offence and issue of an infringement notice by the Victoria Police or other agency through the registration of the notice by the PERIN Court and ultimately to the enforcement by the Sheriff of an unpaid fine. Each of these steps was measured, analysed and detailed in preparation for the tendering process, together with the many interface requirement between the contractor's and the government's responsibilities within the overall management process. The preparation of tenders by the bidders and their evaluation by the project team have been similarly complex, detailed and time-consuming.

Impact initiatives on the collection of outstanding fines and costs

Victoria's performance on fines collections is better than other jurisdictions in Australia for which data is available, with 92 per cent of all fines ultimately being cleared. Over \$200 million is generated for State and local government each year through this system. By contrast, cities such as London and Chicago only clear 65 per cent and 60 per cent of infringements. In Victoria, over 86 per cent of all fines are cleared within the first year, compared to a figure of 36 per cent in New Zealand.

It should be noted that the annual growth in the dept pool, comprised of uncollected fines plus attributed costs of collection, has declined from \$31.7 million to \$13.0 million over the period 1990-91 to 1996-97.

The Report recognises that part of the reason for the increased level of uncollected fines and costs is the poor financial circumstances of many offenders and the inability to legally extinguish uncollected debts. Further categories of defaulters are those who are difficult to locate because of their itinerant lifestyle and habitual offenders who deliberately evade their obligations; an analysis of defendants with multiple warrants indicated that 3 per cent of defendants were responsible for 25 per cent of fines in the uncollected fines pool. Improvements in the VicRoads address accuracy resulting from implementation of the Public Accounts and Estimates Committee Report and redevelopment of its database will greatly assist enforcement agencies' ability to locate these people.



□ **RESPONSE** provided by Secretary, Department of Justice - continued

Impact initiatives on the collection of outstanding fines and costs - continued

The use of 1990-91 year figures as the baseline for measuring growth in the debt pool should be treated with some caution. 1990-91 was the first full year after management of unpaid fines was consolidated in the Enforcement Management Unit following the transfer of functions from the Victoria Police.

Despite the difficulties and limitations of the present systems the Enforcement Management Unit has significantly improved its performance over the period from 1990-91 to 1996-97:

- *the annual amount of fines and costs recovered per staff member has increased by 30 per cent from \$136 000 to \$177 000; and*
- *total annual collections have increased by 36.6 per cent from \$34.1 million to \$46.6 million.*

Further substantial improvement is expected over the next 3 years through the re-engineering of the administrative and fines enforcement processes and the development and implementation of an integrated fines collection system as part of the implementation of the present TCO/EMU Outsourcing Project.





CHARGING FOR POLICE SERVICES

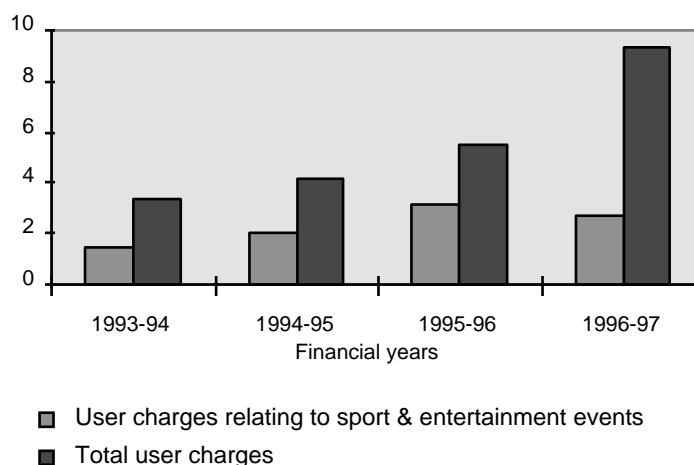
3.4.70 Under the current legislative and regulatory framework, which includes the *Police Regulation Act 1958* and the *Police (Charges) Regulations 1992*, the Chief Commissioner of Police may levy charges for police deployed at sporting and entertainment events where admission charges are made, and the events are commercial or entrepreneurially sponsored. Other police services for which costs may be recovered include searches relating to collisions and accidents, criminal history checks, search of police records and the provision of sworn affidavits.

3.4.71 The administrative arrangements for the charging of police services is set out in a policy endorsed by the Minister for Police and Emergency Services in December 1993. The aim of the policy is to improve the deployment of police resources through the efficient and effective use of police resources in the community.

3.4.72 Police charges for sporting and entertainment events may be waived, in full or part, by the Minister for Police and Emergency Services on the grounds that the event furthers the Government's strategies in areas such as health, sport, tourism, cultural or economic development, and where the viability of the event would be compromised by the payment of police charges.

3.4.73 Victoria Police allocates resources to more than 700 events annually for which user charges are raised. Since the 1993-94 financial year, a total of \$22.3 million has been levied in user charges of which \$9.1 million or 41 per cent relates to sporting and entertainment events. Chart 3.4G highlights the level of user charges levied by Victoria Police over the 4 year period ending 30 June 1997 and indicates the proportion attributable to sport and entertainment events.

CHART 3.4G
LEVEL OF POLICE USER CHARGES, 1993-94 TO 1996-97
((\$million))



.....

Need for improved management information systems

3.4.74 The majority of sporting and entertainment events within the State which require police presence are held within the metropolitan area, with responsibility for policing these events allocated to various sections of the police force.

3.4.75 An audit review of information systems used in managing this activity identified that:

- There was no central management information system to capture all relevant information pertaining to sporting and entertainment events. Accordingly, issues such as costs of provision of police services, level of cost recovery, consistency of application of the user-pays policy, and the extent of subsidisation resulting from the waiving of charges, were not effectively monitored; and
- In certain sections of the police force, the use of outdated and inadequate information systems resulted in inefficient administrative work practices, while in other sections more sophisticated event management systems were utilised facilitating appropriate data capture and the generation of management information such as deployment statistics.

3.4.76 Given, the increasing demands on limited police resources, there is a need for Victoria Police to implement a standard management information system to facilitate the efficient and effective management of user charges for sporting and entertainment events. The implementation of such a system should:

- provide Victoria Police with relevant information to facilitate appropriate monitoring of user charges, in particular the cost of deployment of police resources and the extent of cost recovery and any other issues relating to sporting and entertainment events at a Statewide level;
- enable Victoria Police to ensure that the user-pays policy is consistently applied on a Statewide basis; and
- provide timely response to information requests from relevant stakeholders, including Force Command and external third parties.

Waiving of user charges

3.4.77 In accordance with the police user-pays policy, event organisers must be advised by Victoria Police that “... *events which further the Government’s strategies in areas such as health, sport, tourism and cultural or economic development, and whose viability is threatened by payment of the charges*”, may be eligible for the waiver of user charges, or part thereof, by the Government under the policy.

3.4.78 Applications for the waiving of charges are independently assessed by the Department of Justice, which makes recommendations to the relevant Minister on these matters.

3.4.79 Since 1993, there have been in excess of 170 applications received by the Department seeking the waiving of user charges. However, an audit analysis of such applications disclosed significant delays in the decision-making process. According to Police records:

- 4 applications amounting to \$158 000, which were aged in excess of 90 days with some dating back to November 1993, were awaiting Ministerial determination; and



- 28 applications for the waiving of fees amounting to \$627 000 were approved by the Minister between 3 months and 2 years after the relevant events were held.

3.4.80 To improve the management of user charges, Victoria Police in conjunction with the Department of Justice should review current procedures to ensure that all applications for the waiving of fees are submitted and considered in a timely manner.

Adequacy of charge-out rates

3.4.81 The Police (Charges) Regulations 1992 provides the legislative authority for Victoria Police to raise fees for services provided and also specifies the recovery rates that can be applied.

3.4.82 A guide to assist agencies in the implementation of competition into the supply of goods and services, titled *Competitive Neutrality: A Statement of Victorian Government Policy*, was released by the Department of Treasury and Finance in 1997. The underlying principle of this policy is to ensure that fees charged by government agencies are not artificially low due to implicit subsidies received from the government which may “crowd out” private sector competition. The recovery rates for police services detailed in the Regulations cover only 3 broad bands of personnel and a limited number of other resources. In addition, the scope of charges excludes any consequential policing requirements such as traffic control in areas peripheral to the event.

3.4.83 A review of the charge-out rates revealed that all the rates have remained unchanged since 1992, notwithstanding submissions made by Victoria Police since 1993 to the Department of Justice recommending significant increases in the rates. Accordingly, the rates do not reflect the full cost of resources devoted to the policing of the relevant events which may provide Victoria Police with an unfair advantage over other organisations which compete for such services.

3.4.84 In a 1995-96 submission to the Department of Justice, Victoria Police estimated that increases of up to 32 per cent in hourly rates were required to enable full-cost recovery.

3.4.85 The Department in October 1997, advised Victoria Police that the delay in increasing fees had been to allow acceptance of police user charges by promoters. In March 1998, Victoria Police was further advised by the Department that the adjustment of the police user charges had been postponed pending the outcome of the national competition policy review of the *Police Regulation Act 1958* which is expected by the Department to be completed by June 1998.

3.4.86 In view of the fact that salary costs of sworn members have increased by 14 per cent since 1992, there is a need for action to be taken to update charge-out rates to enable **Victoria Police to substantially recover all costs associated with police attendance at major sporting and entertainment events.**



Police assisting visitors attending the Melbourne Grand Prix. (Photo: Courtesy of "Police Life".)

3.4.87 The limitation on the scope of police costs that may be recovered does not enable charge-out rates to reflect the full resources utilised by a modern, technologically advanced police force, in that costs critical to modern policing such as video cameras and night vision filters, cannot be recovered. Furthermore, the Regulations do not allow the recovery of any penalty rates paid to members attending such events which generally occur on weekends and in the evenings.

3.4.88 The ability of Victoria Police to effectively manage resources and apply full cost recovery principles is significantly inhibited by the limitation of the scope of costs permitted to be recovered.

Recovery of user charges

3.4.89 An analysis of the timeliness of billing for services provided by Victoria Police indicated that there was a significant delay in the raising of accounts for a substantial number of events. Table 3.4H below discloses the time delay between the holding of the events and the raising of accounts for the past 3 financial years.

**TABLE 3.4H
DELAYS BETWEEN HOLDING OF EVENTS AND
THE RAISING OF ACCOUNTS**

<i>Period between events and raising of accounts</i>	<i>Value of accounts raised</i>		
	<i>1994-95</i>	<i>1995-96</i>	<i>1996-97</i>
<i>(days)</i>	<i>(\$'000)</i>	<i>(\$'000)</i>	<i>(\$'000)</i>
0 to 30	1 162	681	969
31 to 60	364	773	383
Greater than 60	205	345	584
Total	1 731	1 799	1 936



3.4.90 As highlighted in the above table, there is a need for Victoria Police to examine current procedures to ensure the timely raising and collection of user charges.

□ *RESPONSE* provided by Deputy Commissioner, Victoria Police

Need for improved management information systems

The comments in relation to there being “no central management information system to capture all information pertaining to sporting and entertainment events” is noted. Progress in relation to this area has been made over the past few years, however, it is recognised that further development is required. Victoria Police, as part of the implementation of a Statewide computer network system, is working towards the standardisation of information technology which would allow for an integrated and linked management information system.

Waiving of user charges

Although Victoria Police generally concurs with this finding, the Force is working with the Department of Justice to ensure that applications of waivers are processed in a timely manner.

Adequacy of charge-out rates

Victoria Police acknowledges that the Regulations need to be amended to enable charge-out rates to reflect current salary and transport costs. The Regulations should also include charge out rates for a broader range of resources utilised by Victoria Police in service delivery for events that are commercially and entrepreneurially sponsored.

Recovery of user charges

The Victoria Police “user-pays” policy was recently reviewed and the guidelines are being tightened to ensure timely raising and collection of user charges. The revised policy is currently being finalised and will be promulgated in the near future.

The table referring to delays between holding of events and the raising of accounts includes delays due to invoices put on hold awaiting the Minister’s waiver determinations. In these circumstances, an invoice cannot be raised until Victoria Police are advised of the Minister’s determination of a waiver application.

□ *RESPONSE* provided by Secretary, Department of Justice

General comments

The user-pays policy is an important resource management tool. Its overarching and primary objective (and by far the most important in terms of costs avoided by Victoria Police) is to assist in achieving efficient, effective and equitable uses of police resources. That objective is achieved by:

- *making explicit the cost of delivering certain police services, which may otherwise be perceived by the user as unlimited “free services”; and*
- *requiring the user to meet at least some of the service costs, and thereby ensuring that the level of usage of the service is related to the cost of providing it.*

□ **RESPONSE** provided by Secretary, Department of Justice - continued

Waiving of user charges

The waiver application process should be seen in the context of the resource management objective of the user pays policy.

When applications for waivers are received in the Department of Justice, there may be extensive negotiations, not just about whether the application of user charges would threaten the viability of the event, but also about whether, and if so, how, the event could be staged in a manner which would reduce the need for police services. (Important options for reducing police services may include, for example, limiting the availability of alcohol at venues, routing race marathons through parklands rather than streets wherever possible, or trading-off the need for police services with resources from the private sector security industry). Although the negotiations can sometimes be lengthy, it has proven very successful across a wide range of sporting and entertainment events, including agricultural shows, foot and cycle marathon events, and at large tennis, football and cricket venues.

Nevertheless, it is agreed that Victoria Police and the Department will review procedures to ensure that applications for waivers are submitted and considered as expeditiously as possible.

Adequacy of charge-out rates

If the user-pays policy is to be successful, it must be generally accepted by the community. It is now becoming well accepted. Important reasons are that the user fees were not set at full cost recovery level in 1992, and that the fees have been stable since that time. This policy position is not inconsistent with guidelines issued by the Department of Treasury and Finance, which provide that charges may be set at levels lower than full cost recovery where there are good policy reasons for doing so. Because there are clearly broader community benefits flowing from the staging of sporting and entertainment events, there are sound public policy reasons for not necessarily seeking full cost recovery of police services allocated to such events.

Audit's comments about ensuring that the fees for police services are not artificially low and so "crowd out" the private security industry is noted. The intention of the user-pays policy is in fact the reverse; that is, it aims to attach a price to police services and so "crowd out" the inappropriate demand for their use. In this way, police services are often replaced with security services from the private sector.

The Police Regulation Act and the Police (Charges) Regulations made under that Act are scheduled to be reviewed under the Government's National Competition Policy commitments. That review will include a comprehensive assessment of the Regulations in terms of their scope, objectives and competitive contestability. The Department is also considering whether and if so, by how much, the prescribed fees should be increased prior to the completion of the competition review.



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

Report	Subject	Status at date of preparation of this Report
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MATTERS RESOLVED OR ACTION COMMENCED

DEPARTMENT OF JUSTICE

State Government Corporate Card

Ministerial Portfolios, May 1997, pp. 294-5.

There is a need for the Department to strengthen its authorisation and verification procedures to ensure the probity and accountability of all Corporate Card payments. Audit identified several instances where Corporate Card transactions had not been independently approved, cardholders had not confirmed the receipt of related goods and services and transactions were not supported by adequate supporting documentation. Consequently, it was difficult to determine whether such expenditure was incurred for official purposes.

The Department has:

- reviewed relevant policies and procedures;
- informed management of their obligation in relation to transaction authorisation and the need to leave a satisfactory audit trail;
- conducted an internal audit of Corporate Card management; and
- requested Business Units to review their cardholdings to ensure that cards are held by appropriate staff and that credit limits are also appropriate.

Refer to further comments included in this Report under the Department of Treasury and Finance.

Crimes Compensation Tribunal

Ministerial Portfolios, May 1995, pp. 157-8.

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.

Under section 16 of the *Victims of Crime Assistance Act* 1996, in determining whether or not to make an award or the amount of any award, the Tribunal may take into account any compensation, assistance or payments of any kind made under any scheme including those managed by the Transport Accident Commission and the Victorian WorkCover Authority and compensation paid in accordance with the Police Assistance Compensation Act 1968.

Ministerial Portfolios, May 1995, p. 159.

The Tribunal and the Director of Public Prosecutions (DPP) have not developed procedures to recover moneys from convicted offenders.

As a result of the *Sentencing Act* 1991, victims are now able to seek compensation for pain and suffering from convicted offenders. The Office of Asset Confiscation within the Department was established in 1998 to assist in the recovery process and a working party has been established to develop administrative arrangements for facilitating the recovery of compensation awarded by the courts.

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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>
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MATTERS RESOLVED OR ACTION COMMENCED

SHERIFF'S OFFICE

<i>Ministerial Portfolios, May 1996, pp. 187-8.</i>	Over the period 1986-87 to 1994-95 total outstanding fines and costs had grown 9 times.	Refer to comments under this Part of the Report.
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SCHEDULE B
COMPLETED/INCOMPLETE AUDITS

Entity	Financial year/period ended	Reporting to Parliament	Financial statements signed by entity	Auditor- General's report signed
COMPLETED AUDITS				
Department of Justice	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	29 Aug. 1997	29 Aug. 1997
ATTORNEY-GENERAL				
Legal Practice Board (a)	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	28 Aug. 1997	29 Aug. 1997
Office of the Director of Public Prosecutions	30 June 1997	" "	15 Sept. 1997	18 Sept. 1997
Office of the Legal Ombudsman	30 June 1997	" "	2 Oct. 1997	2 Oct. 1997
Queen Victoria Women's Centre Trust	30 June 1997	" "	25 Sept. 1997	29 Sept. 1997
Senior Master of the Supreme Court (b)	30 June 1996	<i>Supreme Court Act 1986.</i>	22 Apr. 1997	23 Apr. 1997
Senior Master of the Supreme Court (b)	30 June 1997	" "	13 May 1998	23 May 1998
Solicitors' Guarantee Fund (a)	31 Dec. 1996	31 Oct. <i>Financial Management Act 1994,</i> s.46.	9 Oct. 1997	16 Oct. 1997
Victoria Legal Aid	30 June 1997	" "	29 Aug. 1997	29 Aug. 1997
Victorian Electoral Commission	30 June 1997	" "	9 Sept. 1997	9 Sept. 1997
Victorian Financial Institutions Commission	30 June 1997	" "	13 Aug. 1997	13 Aug. 1997
Victorian Institute of Forensic Medicine	30 June 1997	" "	22 Aug. 1997	3 Nov. 1997
POLICE AND EMERGENCY SERVICES				
Country Fire Authority	30 June 1997	" "	18 Aug. 1997	18 Aug. 1997
Metropolitan Fire Brigades Board	30 June 1997	" "	27 Aug. 1997	27 Aug. 1997
National Institute of Forensic Service	30 June 1997	No reporting requirements.	26 Nov. 1997	30 Sept. 1997
National Police Ethnic Advisory Bureau	30 June 1997	" "	26 June 1997	30 Sept. 1997
Office of the Chief Commissioner of Police	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	29 Aug. 1997	29 Aug. 1997

(a) Following the assent of the *Legal Practice Act 1996*, the Solicitors' Guarantee Fund became part of the Legal Practice Board as at 1 January 1997.

(b) Senior Master of the Supreme Court produces financial statements which are not a statutory requirement and these statements are audited by arrangement.

Part 3.5

Natural Resources and Environment

KEY FINDINGS

Restructuring of water authorities

- There has been considerable progress in the achievement of key government reform strategies for the non-metropolitan water authorities.
Paras 3.5.4 to 3.5.7
- One of the objectives of the industry reform is to achieve efficiencies from authority amalgamations. However, the audit review found that operating costs in nominal terms over the first 3 years of the reform program increased by 12 per cent. It should be recognised that during the period costs were incurred with the aim of improving services to water customers.
Paras 3.5.16 to 3.5.18
- While the reform process envisaged the issue of licence agreements between the government and individual non-metropolitan water authorities by July 1995 and the establishment of an independent regulator, with the aim of improving the level of accountability and customer service, and to establish performance standards for the industry, these aspects of the reform process have not been implemented.
Paras 3.5.19 to 3.5.20 and Paras 3.5.48 to 3.5.50
- Only 57 per cent of the population supplied by non-metropolitan water authorities received water that met the guidelines for microbiological quality. Of particular concern was that one-third of water that was treated did not meet the guidelines.
Paras 3.5.32 to 3.5.37
- The estimated cost associated with raising the quality of water to a standard consistent with the guidelines was in the order of \$288 million.
Paras 3.5.32 to 3.5.37



KEY FINDINGS - continued

Restructuring of water authorities - continued

- Only 13 per cent of wastewater treatment plants operated by non-metropolitan water authorities fully met the Environment Protection Authority (EPA) Standards outlined in their licence agreements for the discharge of treated wastewater into waterways.

Paras 3.5.41 to 3.5.47

- The cost of upgrading non-metropolitan water authorities wastewater treatment plants to comply with their licensing agreements with the EPA has been estimated to be in the order of \$167 million.

Paras 3.5.41 to 3.5.47

Victorian Dairy Industry Authority Chinese joint venture

- The Victorian Dairy Industry Authority's share of the estimated accumulated losses in a joint venture in China to 30 June 1998 is expected to be \$564 000. In addition, the Authority has written-off \$530 000 of its initial investment on the venture of \$730 000, expended a further \$125 000 on the venture and incurred unquantified costs associated with its management. Accordingly, the joint venture has cost the Authority in excess of \$1.2 million.

Paras 3.5.51 to 3.5.58

- Although the joint venture has not been a financial success to date, it has established a new market for "Big M" milk products and enhanced the brand name through its exposure within the Chinese market.

Paras 3.5.59 to 3.5.61

- The Authority did not incorporate a provision within the agreement to ensure that a pre-determined percentage of Victoria market milk and dairy products would be exported to China for utilisation by the joint venture. As a result, the Authority created the potential for its participation in the joint venture to be ultra vires to the *Dairy Industry Act 1992*.

Paras 3.5.62 to 3.5.67

Milk marketing

- The establishment of Australian Milk Marketing Pty Ltd (AMM) by the Victorian Dairy Industry Authority has created the situation where it has effectively relinquished control over its marketing function. Furthermore, the Authority's actions in separating the purchaser of marketing services (the Authority) from the provider (AMM) only served to transfer the marketing functions of the Authority from the public sector to the private sector with the Authority losing direct control over the milk marketing function.

Paras 3.5.68 to 3.5.78

- The Authority's actions in forgoing its interest in AMM for nil consideration has resulted in a loss to the Authority of at least \$285 000.

Para. 3.5.80

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 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 Department of Natural Resources and Environment, were subject to audit by the Auditor-General during the 1996-97 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>
Agriculture and Resources	Agriculture Victoria Services Pty Ltd (a) Australian Food Industries Science Centre City West Water Ltd Emu Industry Development Committee First Mildura Irrigation Trust Gippsland and Southern Rural Water Authority Goulburn Murray Rural Water Authority Melbourne Market Authority Melbourne Water Corporation Murray Valley Citrus Marketing Board Murray Valley Wine Grape Industry Development Committee Non-metropolitan water authorities (15) Northern Victorian Fresh Tomato Industry Development Committee Radius Computing Pty Ltd (b) Renewable Energy Authority of Victoria River Management Authorities (16) South East Water Ltd Sunraysia Rural Water Authority Veterinary Practitioners Registration Board of Victoria (c) Victorian Dairy Industry Authority Victorian Dried Fruits Board Victorian Meat Authority Victorian Plantations Corporation Victorian Strawberry Industry Development Committee Water Training Centre Wimmera Mallee Rural Water Authority Yarra Valley Water Ltd
Conservation and Land Management	Alpine Resorts Commission Bairnsdale Regional Waste Management Group Eastern Regional Waste Management Group Eco Recycle Victoria (d) Environment Protection Authority Northern Regional Waste Management Group (e) Parks Victoria (f)

TABLE 3.5A
MINISTERIAL RESPONSIBILITY FOR PUBLIC BODIES
WITHIN THE NATURAL RESOURCES AND ENVIRONMENT SECTOR - continued

<i>Ministerial portfolio</i>	<i>Entities subject to audit</i>
Conservation and Land Management - continued	Phillip Island Nature Park Board of Management (g) Port Bellarine Committee of Management Royal Botanic Gardens Board Shrine of Remembrance Trustees South Eastern Regional Waste Management Group State Swimming Centre Committee of Management Surveyors Board of Victoria Trust for Nature (Victoria) Western Regional Waste Management Group Yarra Bend Park Trust Zoological Parks and Gardens Board (h)

- (a) Formerly known as Daratech Pty Ltd.
- (b) Ceased operations on 31 January 1998.
- (c) Formerly known as the Veterinary Board of Victoria.
- (d) Formed on 17 December 1996 from the amalgamation of the Recycling and Resource Recovery Council and the Waste Management Council.
- (e) Formerly known as the Northern Regional Refuse Disposal Group.
- (f) Formerly known as Melbourne Parks and Waterways.
- (g) Formerly known as Phillip Island Penguin Reserve Committee of Management.
- (h) Formerly known as the Zoological Board of Victoria.

3.5.3 Comment on matters of significance arising from the audit of entities within the Natural Resources and Environment sector is provided below.

RESTRUCTURING OF WATER AUTHORITIES

Reform of non-metropolitan urban water authorities

3.5.4 Prior to 1993, domestic water, sewerage and waterway management services across country Victoria were provided by around 120 non-metropolitan water authorities, which serviced a customer base of 1.1 million people, and were collectively responsible for annual revenue of \$400 million. At that time, these authorities faced a number of significant difficulties, including:

- two-thirds of customers were supplied with drinking water which failed to meet accepted public health standards;
- two-thirds of sewerage treatment plants did not comply with their licence agreements;
- appropriate systems and procedures had not been established to accurately assess the condition of infrastructure assets and the authorities lacked an understanding of good asset management practices;
- the cost of service provision was, on average, 20 per cent higher than that incurred by Melbourne water authorities;



- cross-subsidisation of services occurred between authorities and local councils; and
- there was an inability to finance capital expenditure without government assistance.

3.5.5 In October 1993, the former Office of State-Owned Enterprises of the Department of Treasury and Finance released a State Government policy document outlining the proposed future direction of Victoria’s water industry, titled *Reforming Victoria’s Water Industry A Competitive Future*. The key objectives of the policy were to:

- achieve efficiencies from economies of scale generated from authority amalgamations;
- provide greater focus on the core business of commercial water and wastewater services;
- introduce greater commercially focused management practices;
- improve the quality of Victorian water; and
- reduce the effluent discharged into Victorian waterways.

3.5.6 This Report provides an outline of the reform process to date and identifies some of the major issues still facing the industry, including water quality and waste water treatment.

3.5.7 **The audit review disclosed that, while there has been considerable progress in the achievement of key government reform strategies for the non-metropolitan water authorities, there is a need for continuing action to meet the overall objectives of the reform program.**

Water authority amalgamations

3.5.8 Given the large number of the water authorities, many of which were relatively small in size, the Government considered that there was substantial scope for the industry to improve its productivity and generate efficiencies from amalgamations, including:

- an estimated \$10 million in annual savings from reduced administration costs and more co-ordinated management;
- an increased capacity of larger authorities to meet capital requirements internally; and
- increased expert technical and scientific capabilities.

3.5.9 In March 1994, the Government introduced a plan to rationalise the number of water authorities. Adoption of this plan during the 1994-95 financial year resulted in the amalgamation of the State’s then 83 water authorities into 18. Additional amalgamations introduced in 1997 reduced the number of authorities to 15.



3.5.10 An audit review of the annual revenue of the amalgamated water authorities disclosed that individual revenue levels ranged from \$4.3 million to \$75.4 million, with 2 of the authorities having revenue levels of less than \$10 million, which was one of the threshold indicators set in the reform process to determine commercial viability.

□ **RESPONSE** provided by Secretary, Department of Natural Resources and Environment

The reforms in 1997 were based on identification of further customer benefits which could be delivered through boundary adjustments and mergers.

Focus on core business

3.5.11 A key objective of the reform process involved the concentration of authority activities on the core business of providing commercial water and wastewater services, through the separation of the water authority operations from those of local government entities and the transfer to other entities of certain other functions such as waterway management.

3.5.12 This objective has now largely been achieved with the severing of the association between water authorities and local government entities, and the transfer of other functions, such as waterway management, to catchment management authorities.

Commercial management

3.5.13 The Government reform agenda also involved the assumption by authorities of a greater commercial focus, through the introduction of a number of strategies, which are outlined below.

Introduction of skill-based boards

3.5.14 Given that non-metropolitan water authority services were often traditionally provided in conjunction with local government, board members were often drawn from government appointees, local councillors and directly-elected members. The strong links with local government entities often resulted in water authority management and boards lacking commercial management expertise.

3.5.15 With the establishment of the 15 new water authorities, the links between these authorities and local government have now been severed. In particular, the *Water (Amendment) Act 1993* has brought the arrangements for the appointment of the boards of non-metropolitan water authorities into line with practices of metropolitan and rural water authorities, enabling them to access appropriate business skills and knowledge.

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Proposed reduction in operating costs

3.5.16 In assessing the performance of authorities in reducing their operating costs, the Department of Natural Resources and Environment:

- defined operating costs as those involving operations, maintenance, administration and finance expenses; and
- adjusted the total annual operating costs for each authority to eliminate one-off expenses related to restructuring such as redundancy costs, operations and maintenance expenses associated with major new capital works, and costs associated with non-core activities such as timber mills and waterway management.

3.5.17 Based on the adjusted costs, as outlined above, the Department determined that cost savings of around 17 per cent were achieved by the sector over the 3 year period as compared with the reform program's target reduction of 20 per cent.

3.5.18 However, the audit review found that the total operating costs incurred by the non-metropolitan water authorities, as disclosed in their annual reports, have increased from \$255 million in the 1993-94 financial year to \$286 million in the 1996-97 financial year, representing an nominal increase of 12 per cent. It should be recognised, however, that during that period costs were incurred with the aim of improving services to water customers.

□ *RESPONSE provided by Secretary, Department of Natural Resources and Environment*

During the period of structural reform, non-metropolitan urban water authorities have been investing heavily in improving drinking water quality, improving wastewater treatment and in extending their sewerage services to new areas. The service improvements and extensions involve higher operating costs for finance, energy, asset maintenance and administration.

The 17 per cent saving represents \$35 million per annum saving in operating costs. In addition, there have been many cases of improved maintenance practices and systems planning.

Introduction of operating licenses

3.5.19 As part of the reform process, licence agreements were to be established between the State Government and individual authorities to improve the level of accountability and customer service, and to establish performance standards for the industry.

3.5.20 Although the reform agenda envisaged the issue of licences to authorities by July 1995, at the date of preparation of this Report, licences had not been issued by the Government as the requisite legislative amendments had not been made to establish such arrangements.



□ **RESPONSE** provided by Secretary, Department of Natural Resources and Environment

The review of legislation required to facilitate operating licences will be considered as part of the further reform program.

Ensuring authorities pay commercial dividends

3.5.21 The payment of commercial dividends is a key element of the reforms to government business enterprises. These dividends are set around a benchmark figure representing 50 per cent of the net profit of each business subject to the tax equivalent regime and 65 per cent for all other entities.

3.5.22 Dividends were first introduced in the non-metropolitan water sector in the 1992-93 financial year. During the 1996-97 financial year, the Government collected \$20.3 million in dividend revenue from these authorities.

3.5.23 In February 1998, the Government decided that all non-metropolitan water authorities should move to a commercial dividend framework under which dividends will be determined as follows:

- for the 1997-98 financial year - lower of \$24 per assessment or 50 per cent of 1996-97 net profit;
- for the 1998-99 financial year - 30 to 50 per cent of net profit; and
- for the 1999-2000 financial year and beyond - 65 per cent of the previous financial year's net profit.

3.5.24 The Department of Treasury and Finance estimates that the total dividends to be paid by the sector for the 1997-98, 1998-99 and 1999-2000 financial years will be \$16.1 million, \$15.6 million and \$17.7 million, respectively.

Introduction of tax equivalents

3.5.25 In April 1995, the Council of Australian Governments, of which Victoria is a member, agreed to implement the Commonwealth Government's National Competition Policy. The State Government's adoption of the National Competition Policy principles was outlined in the June 1996 document titled *Competitive Neutrality A Statement of Victorian Government Policy*. In relation to non-metropolitan water authorities, this policy statement did not set a specific date for the introduction of a tax equivalent system as it had not been decided at that time whether the competition neutrality policy was to apply to these bodies. However, the policy stated that this matter was to be assessed as part of the water industry reform process.



3.5.26 Although the reform process is well advanced, the Government has still not decided whether a tax equivalent environment will apply to these authorities.

□ *RESPONSE* provided by Secretary, Department of Natural Resources and Environment

The commercial dividend policy that is to be fully implemented by 1999-2000 has a higher percentage benchmark dividend payment where authorities do not pay a taxation equivalent. Where taxation is paid, the target dividend is 50 per cent of reported profit, whereas where no taxation is paid the target dividend is 65 per cent.

Reduction of debt levels

3.5.27 Debt owed directly by all non-metropolitan water authorities, at the commencement of the reform process in the 1993-94 financial year, was in the order of \$585 million. This level of direct debt had been reduced to \$507 million by the 1996-97 financial year, representing a reduction of \$78 million (13 per cent) over this period.

3.5.28 Although the level of debt reduction is significant and consistent with the Government's objective of reducing the overall level of debt in the sector, the reform policy did not identify an appropriate level of debt for the sector.

□ *RESPONSE* provided by Secretary, Department of Natural Resources and Environment

The skill-based Boards are expected to individually evaluate the proposed level of debt for their authority in light of capital expenditure projections, the strength of the balance sheet and the expected operating cash flows.

Introduction of a user-pays system for pricing water services

3.5.29 In 1992, when the latest phase of non-metropolitan urban water re-organisations was announced, water and wastewater tariffs for approximately 50 per cent of water authorities were calculated by applying a rate to the value of the property serviced.

3.5.30 As part of the Council of Australian Governments' Strategic Water Reform Framework, water authorities were required to introduce 2-part tariffs, comprising a fixed access charge and a volumetric charge, by 1 January 1998.

3.5.31 In the 1993-94 financial year, water authorities commenced the introduction of a 2-tier water tariff, which incorporated a fixed and a variable component. **By 30 June 1997, all non-metropolitan urban water authorities had converted to the agreed 2-part tariff system.**

Water quality

3.5.32 In my May 1995 *Report on Ministerial Portfolios*, comment was provided on the quality of drinking water provided by metropolitan and non-metropolitan water bodies, with recommendations made to address the existing shortcomings.



3.5.33 For some years, governments within Victoria have been aware that a significant number of consumers residing in non-metropolitan areas were supplied with drinking water which failed to meet relevant national and international drinking water quality guidelines. In order to develop strategies to improve the quality of Victorian water, a working group, with representatives from the former Departments of Conservation and Natural Resources, and Health and Community Services, was established in early 1994.

3.5.34 In a report issued in July 1994, the working party recommended the adoption of the World Health Authority 1984 guidelines as the appropriate standard to be applied to measure water quality. These guidelines set appropriate standards for water quality in terms of microbiological content and in respect to physical, chemical and radiological characteristics. In 1994, the non-metropolitan water authorities were directed to upgrade the quality of water supplied to meet these guidelines by 1999.

3.5.35 Information provided by the Department of Natural Resources and Environment and the Department of Human Services, in relation to the extent of compliance by the non-metropolitan water authorities with the guidelines, indicated that:

- In the 1995-96 financial year, 62 per cent of the population supplied by non-metropolitan water authorities received water that met the guidelines for microbiological quality, which represented a significant improvement since the 1992-93 financial year in which only 27 per cent of the population were in receipt of water which met the guidelines.

However, by the 1996-97 financial year, the performance against the guidelines had declined to 57 per cent. Notwithstanding this adverse movement, the Department of Natural Resources and Environment remained confident that all rural drinking water will meet the standards set in the guidelines by the year 1999.

A significant proportion of the water that did not meet the guidelines for microbiological quality, was of a particularly poor quality. Of particular concern was that one-third of water that was treated, and therefore regarded as disinfected, did not meet the guidelines. This result suggests that water treatment plants managed by authorities are either not operating effectively or authorities are neglecting other areas where water can become contaminated, such as open storages and tanks;

- The estimated cost associated with raising the microbiological quality of water to a standard consistent with the guidelines was in the order of \$288 million;
- In the 1995-96 financial year, 133 towns (31 per cent) tested for physical, chemical and radiological characteristics failed one or more of the specific tests in the guidelines; and
- Authorities were responsible for the collection and dispatching of water samples to approved chemical laboratories for testing, however, there was no independent sampling or verification of the samples taken by each authority.



3.5.36 In October 1997, the Government announced a \$1.3 billion water reform package directed at restructuring debt, accelerating capital works in non-metropolitan regions and providing an average price reduction of 18 per cent. The package provided \$410 million for the non-metropolitan urban and rural water sectors, part of which was to be applied in the upgrading of drinking water quality.

3.5.37 By requiring non-metropolitan water authorities to comply with the standards by 1999, the Department of Natural Resources and Environment has established a minimum standard for water quality. However, there is a need for continued action by both the authorities and the 2 Departments to ensure these standards are achieved and maintained.

□ *RESPONSE provided by Secretary, Department of Natural Resources and Environment*

The 57 per cent compliance result in 1996-97 is explained by some large towns/zones just failing by a small margin to meet the 95 per cent criterion. The December 1999 target is now based on works identified in a Memorandum of Understanding recently signed by each authority Chairperson.

Effluent standards for waterways

3.5.38 Effective wastewater management is integral to the health of Victoria’s rivers and streams. The Government’s policy and standards regarding wastewater treatment are outlined in the policy paper issued by the Environment Protection Authority, titled *State Environment Protection Policy Waters of Victoria*. The policy is designed to facilitate economic wastewater management through a number of mechanisms including:

- establishment of wastewater development plans;
- effective sewage treatment to minimise the impact of discharges into waterways, land or sea;
- provision of effective sewerage and reticulation systems; and
- establishment of appropriate controls over industrial discharges into sewerage systems.

3.5.39 As with water quality, the reform process involved the creation of a working group, with representatives from the former Department of Conservation and Natural Resources and the Environment Protection Authority (EPA) to develop strategies to reduce the effluent discharged into Victorian waterways. The working group presented its report titled *Working Group Report on Effluent Standards and Compliance for Waterways* in 1994, which required all authorities to submit wastewater management plans to the EPA by December 1995.



3.5.40 At the date of preparation of this Report, not all water authorities had submitted their plans to the EPA and many of the plans submitted lacked sufficient detail to enable them to be used as a basis to determine the appropriate future upgrade programs.

□ *RESPONSE provided by Chairman, Environment Protection Authority*

The EPA notes that while not all water authorities submitted plans to the EPA as set out in the Working Group Report on Effluent Standards and Compliance for Waterways (1994), all authorities worked closely with the EPA to develop acceptable treatment plant upgrade proposals, culminating in the successful conclusion of individual Memorandums of Understanding between each water authority and government. These agreements will see a significant improvement in infrastructure, sewage effluent quality and environmental outcomes over the next 3 years.

Compliance with licence agreements

3.5.41 There are effectively 3 levels of sewage treatment, namely:

- primary - removal of floatable and settleable solids;
- secondary - reduction of biochemical oxygen demand, suspendable solids and bacteria; and
- tertiary - further reduction of bio-degradable material and significant nutrient removal.

3.5.42 The minimum acceptable treatment of sewage in Victoria is secondary treatment, with standards set for each wastewater treatment plant operated by non-metropolitan urban water authorities in the respective licence agreements.

3.5.43 The report of the above working group also contained the results of the EPA's 1993 assessment of each wastewater treatment plant's compliance with its licence agreement. **Based on the information contained in the report, on average 86 per cent of the conditions contained in the non-metropolitan water authorities treatment plant licensing agreements with the EPA, where discharges were to waterways, were complied with. A follow-up review undertaken by the EPA in late 1997 disclosed a marginal increase to 88 per cent.**

3.5.44 An analysis by audit of information provided by the EPA of these reviews and annual reports of non-metropolitan water authorities disclosed that:

- There was a reduced number of wastewater treatment plants which met effluent discharges standards outlined in their licence agreements in 1997, compared with 1993;
- The EPA's use of non-regulatory measures such as obtaining agreement from authorities to upgrade treatment plants in order to rectify existing deficiencies, education of authority staff, the provision of information, technical advice on licence compliance and promotion of environment improvement plans, and environmental audits did not have any significant impact on improving the quality of discharges from treatment plants;



- **Only 13 per cent of wastewater treatment plants fully met the standards outlined in their licence agreements.** The performance of these plants can be contrasted to that of the 3 metropolitan water companies, where all their wastewater treatment plants have achieved 100 per cent compliance; and
- In respect of 26 treatment plants with compliance of 90 per cent or less, staff from the EPA indicated that these plants were likely to have fundamental deficiencies preventing full licence compliance being achieved and required improvement. Furthermore, the EPA considered that these discharges are likely to have a significant adverse effect on the environment.

3.5.45 In relation to wastewater treatment plants discharging to the ocean and land, no information was available for 1993 regarding their compliance with the licensing agreements. However, the information which was available for 1997 disclosed that 65 per cent of the plants discharging to land and 27 per cent of plants discharging to the ocean met the standards outlined in their licence agreement.

3.5.46 An analysis undertaken by the Department of Natural Resources and Environment concluded that 39 per cent of the rural population served by non-metropolitan urban water authorities had wastewater treated by a complying treatment plant in the 1995-96 financial year, with that per centage increasing to 52 per cent in the 1996-97 financial year.

3.5.47 **The cost of upgrading Victoria's wastewater treatment plants to comply with their licensing agreements has been estimated by the Department to be in the order of \$167 million.** As previously stated, the Government's October 1997 water reform package provided \$410 million to non-metropolitan urban water authorities, part of which was intended to upgrade existing infrastructure in order to reduce the negative impact of discharges from wastewater treatment plants on the environment. With this additional funding, the Department of Natural Resources and Environment expects that these authorities would achieve wastewater treatment standards consistent with their licence standards by 2001.

□ **RESPONSE** provided by Chairman, Environment Protection Authority

In relation to the second dot point of this section, the primary measure used by the EPA to improve compliance by water authorities with their EPS licences has been to obtain agreement from authorities to treatment plant upgrades which rectify existing deficiencies, meet the requirements of the State environment protection policy Waters of Victoria, minimise nutrient discharges to waterways and maximise the safe reuse of treated effluent. These improvements have already been implemented at a number of locations around the State and, with the implementation of works covered by agreements signed last year, will be achieved at all treatment plants by 2001. The overall outcome will be a substantial increase in effluent reuse and a major reduction in phosphorus discharges to our waterways. Short-term, costly band-aid measures have purposely not been pursued in order to achieve more effective and sustainable solutions in the near future.



Water regulation

3.5.48 Under the State Government's reform process, authorities have been given a greater degree of autonomy in relation to their operational management. In this environment, there is a need for an independent regulatory function to ensure that the needs of consumers are safeguarded. The role of such regulatory function in the water sector would be to:

- ensure the maintenance of an efficient and economic water sector;
- protect the interests of consumers with respect to water industry charges and terms and conditions of water industry services;
- protect the interests of consumers with respect to the reliability and quality of water industry services; and
- facilitate the maintenance of a financially viable water sector.

3.5.49 In recognition of the need for independent regulation of the water sector, the Council of Australian Governments' *Strategic Water Reform Framework*, required the roles and functions of service providers to be clearly separated from those of the regulators.

3.5.50 **Although an independent economic regulator has been established for the metropolitan water sector, no such regulator has been established for non-metropolitan retail water authorities.**

□ *RESPONSE* provided by Secretary, Department of Natural Resources and Environment

The regulatory framework will be completed as part of the work program for further water reform. Regulatory oversight of the non-metropolitan authorities by the Department has continued, including development of industry benchmarking and customer participation strategies.

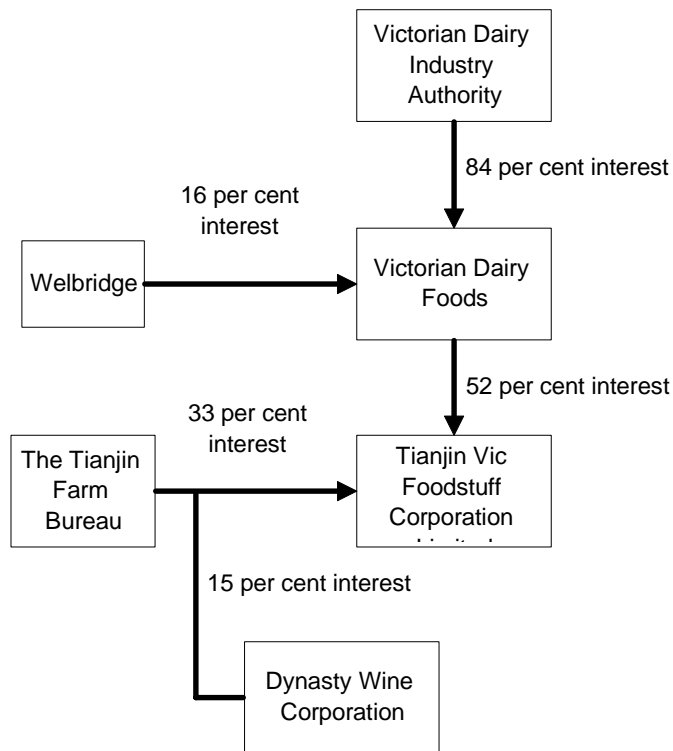


VICTORIAN DAIRY INDUSTRY AUTHORITY CHINESE JOINT VENTURE

3.5.51 In 1992, the Victorian Dairy Industry Authority (the Authority) was approached by the China International Trade Company, on behalf of the Tianjin State Farm Administrative Bureau of China (the Bureau), to participate in a joint venture arrangement involving the manufacture and marketing of “Big M” milk products in China.

3.5.52 Following detailed research, discussions with Chinese representatives, the completion of a financial feasibility study and government approval, the Bureau and the Victorian Dairy Foods Proprietary Limited (a company in which the Authority held an 84 per cent interest) established a joint venture, which operates through Tianjin Vic. Foodstuff Corporation Limited (TVFCL). The ownership structure of the joint venture is outlined in Chart 3.5B.

**CHART 3.5B
JOINT VENTURE OWNERSHIP STRUCTURE**





3.5.53 The key objectives of the joint venture are to:

- generate a significant level of income via royalties and dividends; and
- facilitate a significant increase in the value of the “Big M” brand name.

3.5.54 Following State Government approval, a new factory was opened in Tianjin, China in June 1995. The Authority’s initial investment in the joint venture totalled \$730 000.

3.5.55 In November 1996, following 17 months of operations, a decision was made by the Authority to divest its interest in the joint venture. The Authority’s decision was referred to in an Information Memorandum which stated that:

“The need for this document has arisen as a result of the decision by the Victorian Dairy Industry Authority (VDIA) to sell its shareholding in Tianjin Vic Foodstuff Corporation Limited (TVFCL). This decision is consistent with the changed future direction for the VDIA and the need to underpin TVFCL with a strong commercial shareholder thus adding significantly to the venture and the opportunity for its generation of significant profits in the medium/long term.

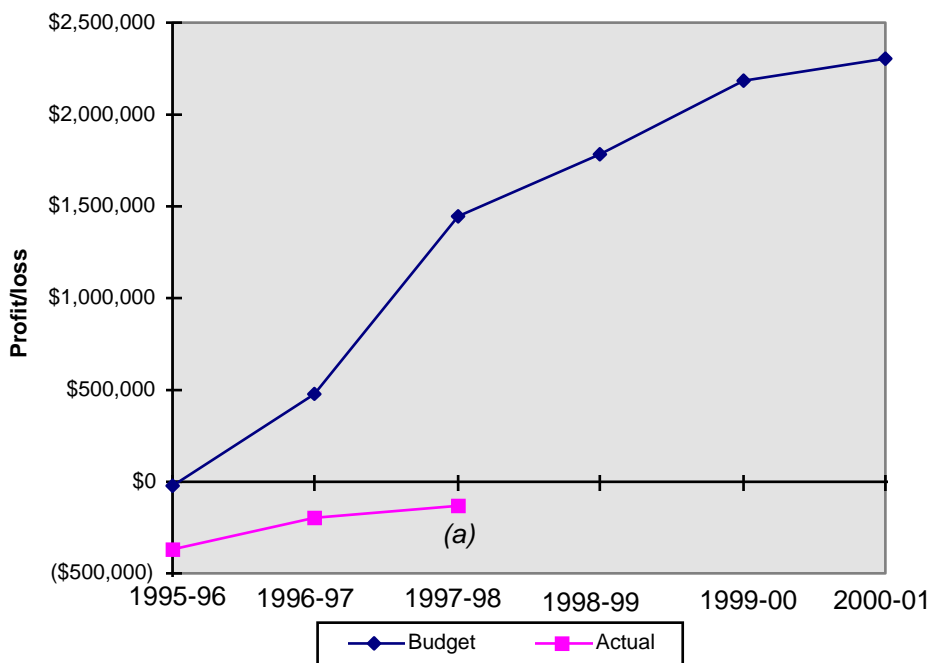
“The VDIA believes the prospects for the brand “Big M” in China in the medium to long term are excellent. The company is established and is producing a consistent high quality product. The main activities of the company requiring attention are promotion, distribution and sales. A company with the appropriate skills and commitment and replacing the VDIA as the major shareholder will assure the success of the venture”.

3.5.56 At the date of preparation of this Report, the Authority was continuing to seek a purchaser for its interest in the joint venture.

Adverse financial impact of joint venture on the Authority

3.5.57 The joint venture has experienced accumulated losses in the order of \$546 000 in its first 2 years of operation, with these accumulated losses expected to increase to \$671 000 by 30 June 1998. Chart 3.5C outlines the annual operating results achieved by the joint venture, compared with the budgeted results for the period 1995-96 to 2000-01 as determined by consultants engaged by the Authority.

CHART 3.5C
JOINT VENTURE OPERATING PERFORMANCE, 1995-96 TO 2000-01



(a) Estimate for current financial year

3.5.58 The Authority’s share of the estimated joint venture losses to 30 June 1998 is expected to be \$564 000. In addition, the Authority has written-off \$530 000 of its initial investment of \$730 000 on the venture, expended a further \$125 000 on the venture and incurred unquantified costs associated with its management. Accordingly, the joint venture has cost the Authority in excess of \$1.2 million. As the joint venture is yet to generate an operating profit, there is also some uncertainty whether the Authority will be able to recover its remaining investment of \$200 000 in the venture.

Operational problems encountered

3.5.59 The audit review identified that the following key factors contributed to the poor financial performance of the joint venture:

- Cash flow difficulties resulting from inadequate capital funding and poor recovery of debts;
- Utilisation of sub-standard packaging materials and inadequate maintenance of equipment. These factors contributed to the rejection of 72 per cent of the milk produced by the joint venture between June 1995 and November 1995 and disruptions to the operations of the plant, which culminated in its closure between 25 October 1995 and 11 November 1995;



- Reliance was placed on local people to manage the joint venture operations in China, in preference to transferring an Authority representative to manage the venture, which impacted on the Authority’s ability to effectively manage the operations in China;
- Inadequate training of staff to operate the plant;
- The “Big M” product was introduced into a culture where milk is not generally consumed as a cold drink in summer months;
- Only a limited range of milk flavours were produced; and
- The joint venture’s marketing plan initially involved the sale of “Big M” milk to 12 different cities in 10 provinces across China instead of establishing a base market in a defined area before expanding into other areas.

3.5.60 In response to the joint venture’s poor financial performance, in the 1995-96 financial year, the Authority initiated a comprehensive review of the operating, financial and market position of the joint venture. Following the completion of the review, joint venture focused its efforts exclusively on the local Tianjin market and made improvements in the areas of product distribution and marketing, which resulted in a significant improvement in “Big M” sales during the first half of 1997. The Authority has also initiated action to improve staff training and product quality.

3.5.61 **Although the joint venture has not been a financial success to date, it has established a new market for “Big M” milk products and enhanced the brand name through its exposure within the Chinese market.**

Legislative power to participate in the joint venture

3.5.62 The objectives of the Authority as defined in the *Dairy Industry Act 1992* are to ensure:

- Victorian milk processors are supplied with sufficient milk to meet the demand for market milk;
- licensed dairy farmers share equitably in returns from market milk;
- opportunities are maximised for the sale of market milk produced in Victoria by securing, maintaining and developing markets;
- standards which safeguard public health and protect the consumer are maintained in the Victorian dairy industry; and
- the Authority performs its functions and exercises its powers efficiently and effectively.

3.5.63 While the main business of the joint venture is to manufacture and market “Big M” milk products in China, the Authority considers the operation of the joint venture to be consistent with its objective to “... *maximise the opportunities for the sale of market milk produced in Victoria by securing, maintaining and developing markets*”. Furthermore, in accordance with the Act, the Authority has the legislative power to enter a joint venture arrangement where “... *in the opinion of the Authority and the Minister it is necessary to do so, in order to achieve its objectives or perform its functions*”.

3.5.64 In order for the Authority to be confident that its participation in the joint venture fell within its legislative authority, it was important to ensure that at least a



portion of the milk sold in China was produced in Victoria. This was consistent with legal advice provided to the Authority by its solicitors in January 1994, which indicated that the joint venture contract must entrench the principle that any shortfall in milk production will be met from milk produced in Victoria.

3.5.65 In the feasibility study undertaken on the proposed joint venture, there was an expectation that within the first 10 years of the project there would be a shortage of milk from within China. To ensure sufficient supplies of milk were available to the joint venture, the agreement entered into in September 1994 between the parties to the joint venture, incorporated the following clause:

“The parties agree that if at any time the Joint Venture Company is unable to obtain sufficient milk or dairy products from within China for processing to meet market demand, the Joint Venture Company shall purchase Victorian milk and dairy products to overcome the shortfall in priority to purchasing milk or dairy products from elsewhere. This shall be subject to Victorian milk and dairy products being price competitive with any alternative source of supply of similar quality goods”.

3.5.66 However, the Authority did not incorporate a provision within the agreement to ensure that a pre-determined percentage of Victorian market milk and dairy products would be exported to China for utilisation by the joint venture. As a result, the Authority created the potential for its participation in the joint venture to be ultra vires to its Act.

3.5.67 In June 1995, the Chinese Farm Bureau guaranteed the supply of raw milk to the joint venture, effectively ensuring that there would be no shortfall. Therefore, no milk produced in Victoria has been sold by the joint venture in China. As a result, by participating in the joint venture the Authority has acted outside the powers conferred on it by the Act.

□ *RESPONSE provided by Chief Executive Officer, Victorian Dairy Industry Authority*

Operational problems environmental

The filling machinery and packaging material utilised by TVFCL was supplied by the Chinese division of a multi-national company which is a leader in UHT equipment and packaging. The company subsequently accepted liability for the faulty packaging material and fully compensated TVFCL for the costs imposed.

Legislative power to participate in the joint venture

Although the VDIA considered, on several occasions, locating a representative in Tianjin, such a step was not cost-effective, particularly in view of the skills of the General Manager. The General Manager, who has held that position since the joint venture commenced, grew up in Tianjin, has studied (obtaining a PhD) and worked in Australia for over 10 years and is an Australian resident. He has a superior command of both English and Mandarin, and an appreciation of the culture and business practices of both Australia and China.



- **RESPONSE** provided by Chief Executive Officer, Victorian Dairy Industry
Authority - continued

Legislative power to participate in the joint venture - continued

Although no Victorian milk or milk powder has been exported to China for use by TVFCL (because sales volumes have been substantially below feasibility study projections), the VDIS has established procedures to manufacture “Big M” in Tianjin using re-constituted Victorian milk powder as soon as sales growth places pressure on availability and price of locally sourced milk. These plans have been put in place notwithstanding the (verbal) guarantee of milk supply by the Tianjin Farm Bureau.





MILK MARKETING

3.5.68 The Victorian Dairy Industry Authority is empowered to undertake milk marketing activities under the *Dairy Industry Act* 1992, including the generic promotion of milk and franchising activities associated with Authority’s milk product brands such as “Rev”, “Skinny Milk”, “Farm House” and “Big M”.

3.5.69 Prior to 1 July 1994, marketing and promotional activities were undertaken directly by the Authority and were funded from:

- brand franchise fees of approximately \$7 million per annum, collected from milk processors who produce the Authority’s brands; and
- a surcharge of approximately one cent per litre levied on all plain milk sold to milk processors for generic promotional activities, which generated approximately \$4 million per annum.

3.5.70 However, on 1 July 1994 Australian Milk Marketing Pty Ltd (AMM) was formed to assume responsibility for marketing plain white milk and various branded specialty milk products. AMM was established as a non-profit organisation with the key corporate objectives of maximising:

- consumer demand for Victorian produced milk products;
- revenue to the milk industry from sales of those products; and
- the effectiveness of the trademarks which AMM markets.

3.5.71 The establishment of AMM was part of the progressive deregulation of Victoria’s dairy industry, with the United Dairy Farmers of Victoria (UDV), the Milk Processors Association of Victoria (MPAV) and the Authority each issued with 2 shares in the company and exercising joint control of the company. The Authority contributed \$490 000 to assist in the establishment of AMM.

3.5.72 It was the Authority’s intention that, following agreement from all 3 shareholders that AMM was operating as planned, the Authority would divest its shareholding, leaving the company to be jointly owned by the UDV and MPAV. Consistent with this intention, in October 1996, the Authority transferred its 2 shares in AMM to the United Dairy Farmers and the MPAV for nil consideration.

Loss of control over marketing function

3.5.73 The contractual arrangements between the Authority and AMM for the supply of marketing services were outlined in a Trade Mark Licence Agreement. In order to safeguard the interests of the Authority, the agreement included a clause which required AMM to use its best endeavours to extensively promote the trade marks and the sale of goods under the trade marks throughout Victoria.



3.5.74 In September 1996, while the Authority still maintained an ownership interest in AMM, a marketing plan was developed to promote “Big M” milk in 600 ml plastic bottles and flavoured “Rev” in 375 ml plastic bottles. However, after several months of inaction by AMM, it became apparent to the Authority that the implementation of the plan was hindered by the milk processors, who had a vested interest in ensuring that the proposed strategy did not adversely impact on the sales of milk products such as “Classic” and “Breaker”.

3.5.75 As the Authority was unable to satisfactorily resolve the matter, in February 1997 it issued a notice of intention to terminate its agreement with AMM. In response, AMM sought and was granted an injunction from the Supreme Court, preventing the Authority from terminating the agreement. The matter was finally heard in the Supreme Court in November 1997, with the court finding in favour of AMM.

3.5.76 By allowing AMM to directly collect revenue generated from the franchise fees and generic promotion levy paid by processors, the Authority was unable to withhold payments to AMM where the services provided were considered to be inadequate. Furthermore, the contract for service entered into between AMM and the Authority cannot be terminated until 2003, unless there has been a fundamental breach of the agreement by AMM or the Authority. As a result, control over the milk marketing function could not be exercised through the purchaser provider arrangement.

3.5.77 **The establishment of AMM by the Authority has created the situation where it has effectively relinquished control over its marketing function. Furthermore, the Authority’s actions in separating the purchaser of marketing services (the Authority) from the provider (AMM) only served to transfer the marketing functions of the Authority from the public sector to the private sector with the Authority losing direct control over the milk marketing function.**

3.5.78 The rationale behind the transfer of the marketing function from the Authority to AMM was based on the premise that the regulatory functions of the Authority were considered incompatible with its milk marketing functions.

3.5.79 However, the establishment of AMM as a supplier of marketing services to the Authority, with 2 of its 4 Board members holding senior management positions with milk processing businesses operating in Victoria, in audit opinion has created the potential for conflicts of interest to occur for these board members. That is, AMM’s activities in promoting the Authority’s milk products, has the potential to adversely impact on the sale of milk products produced by these processing businesses. **Accordingly, the 2 Board members associated with milk processing businesses would have difficulty discharging their fiduciary duties as Board members of AMM.**

Financial impact on the Authority

3.5.80 In order to determine the financial impact on the Authority from the transfer of its shareholding in AMM, it is necessary to determine the value of the AMM business. While such a valuation had not been determined by the Authority, an estimate of the value of the business as a going concern is likely to be the value of its net assets, which stood at \$860 000 as at 30 June 1997. Therefore, **the Authority's actions in forgoing its interest in AMM for nil consideration has resulted in a loss to the Authority of at least \$285 000.**

□ *RESPONSE provided by Chief Executive Officer, Victorian Dairy Industry Authority*

The establishment, ownership structure, functions and funding of AMM was jointly agreed by the United Dairyfarmers of Victoria, the Milk Processors Association of Victoria and the VDIA. The transfer of the Authority's marketing activities to a private company (AMM) was supported by each of the key industry sectors and the Government. In facilitating the establishment of the AMM, the VDIA did not act unilaterally.

The establishment of AMM was not based on the purchaser/provider model, however, Authority control over AMM's marketing activities continues through both the Trade Mark Licence Agreement (covering VDIA branded milks) and the Generic Marketing Agreement (covering generic activities) between the 2 organisations. The obligations on the parties to these agreements remain in place.

The withdrawal of the VDIA as a shareholder in AMM and sale of its shares for (effectively) nil consideration was as specified in the Shareholders Agreement. As the VDIA made no profits from marketing activities it carried out prior to July 1994, the VDIA did not expect to make any profit upon sale of its shares in AMM, which is also a non-profit organisation.



**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>
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MATTERS RESOLVED OR ACTION COMMENCED

DEPARTMENT OF NATURAL RESOURCES AND ENVIRONMENT

<p><i>Second Reports, 1985-86 and 1986-87.</i></p> <p><i>Ministerial Portfolios, May 1989, pp. 45-6. May 1990, pp. 68-70.</i></p> <p><i>Ministerial Portfolios, May 1997, p. 156.</i></p> <p><i>Ministerial Portfolios, May 1997, pp. 158-62.</i></p> <p><i>Ministerial Portfolios, May 1997, pp. 161-2.</i></p>	<p>Deficiencies in the debtors and revenue collection system.</p> <p>While it is recognised that limitations may exist on the Department's ability to increase rental charges and at the same time satisfy community expectations, scope appears to exist to improve financial returns for some of the Department of Natural Resources and Environment's property holdings.</p> <p>There is a clear need for the Department to review the current reporting framework relating to committees of management and trustees, to provide a proper accountability process. The receipt and review of limited financial information once every 3 years, together with the absence of an appropriate departmental program to inspect Crown land reserves, did not ensure that the Department became aware on a timely basis of potential problems arising in committees of management.</p> <p>The Department had not established a formal, systematic and risk based inspection program to ensure that Crown land reserves were not mismanaged or used for other than specified purposes.</p>	<p>The Department has reduced its debtors balance from \$17.9 million at 30 June 1996 to \$16.7 million (7 per cent) at 30 June 1997. Although the debtors balance has decreased, audit still considers that scope exists to further improve the Department's management of debtors.</p> <p>The Department now charges full commercial rental on most of its properties. The only exceptions are where the Department is unable to raise rentals on long-term leases or where the properties provide a community benefit.</p> <p>The Department is investigating the feasibility of devolving all community use crown land of local or regional significance to Municipal Councils or other appropriate bodies. Financial accountability and reporting, public risk liability and the approval to issue and administer leases and licences to specific users for approved uses would be devolved if this initiative proceeds. The Department will also establish an appropriate hierarchy of minimum accountability requirements for the 4 000 delegated management reserves. Reserves of Statewide significance will be identified and retained under the control of the Department.</p> <p>The Department has completed the design of a report to record data during field visits to individual sites, including risks and hazards. Such risks are categorised into levels of severity with estimates of costs to minimise risk. Field visits have been completed for two of the State's 78 municipalities. Enhancements to the Department Land Information System is nearing completion so that site data can be electronically stored and easily retrieved for reporting purposes or analysis.</p>
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SCHEDULE A - continued
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS

<i>Report</i>	<i>Subject</i>	<i>Status at date of preparation of this Report</i>
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MATTERS RESOLVED OR ACTION COMMENCED - continued

ALPINE RESORTS COMMISSION

<p><i>Ministerial Portfolios, April 1992 p. 408.</i></p>	<p>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.</p>	<p>The Alpine Resorts Commission ceased operations on 29 April 1998.</p> <p>The Commission was replaced by 6 new independent boards each representing a different alpine resort.</p> <p>An Alpine Resorts Co-ordinating Council is to be established to co-ordinate the development of the resorts. In addition, an Alpine Resorts Unit within the Department is to be established to provide policy advice and corporate support to the Minister concerning the management of the resorts.</p>
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<p><i>Ministerial Portfolios, May 1997 p. 165.</i></p>	<p>Given the sensitivity of environmental issues within alpine areas, particular attention will need to be given to the continued development of appropriate management plans and strategies to ensure the preservation of these unique areas for the benefit of future generations.</p>	<p>Refer to above comments.</p>
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MELBOURNE WATER INDUSTRY REFORM

<p><i>Ministerial Portfolios, May 1996, p. 219.</i></p>	<p>The Office of the Regulator-General has engaged the services of consultants with international experience to assist in the development of benchmarks, performance indicators and targets. Until these indicators and benchmarks are established, effective independent monitoring and regulation of the industry will not be completed.</p>	<p>The Office of the Regulator-General is continuing to develop suitable performance indicators and benchmarks. A current review by the Department of Treasury and Finance into water policy and industry regulation is expected to help clarify the role of the Regulator-General.</p>
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<p><i>Ministerial Portfolios, May 1996, p. 221.</i></p>	<p>Although the interests of consumers are largely protected by the Government's cap on the fixed component of the water and sewerage charges, until July 1998, delaying the Regulator-General's first price review may leave consumers vulnerable to price increases for a 3 year period to 2001. In addition, until the Regulator-General undertakes a pricing review he is unable to determine the financial viability of the Melbourne metropolitan water industry.</p>	<p>As indicated above, a review by the Department of Treasury and Finance has commenced and the timing at any water pricing reviews by the Regulator-General will be considered as part of this review.</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>
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MATTERS RESOLVED OR ACTION COMMENCED - continued

MELBOURNE WATER INDUSTRY REFORM - continued

<p><i>Ministerial Portfolios, May 1996, p. 222.</i></p>	<p>If the performance of the Melbourne Water 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 rather than historical cost may be more appropriate.</p>	<p>Melbourne Water is in the process of developing strategies to revalue its infrastructure assets. The 3 retail water companies do not plan to revalue their fixed assets in the short-term.</p>
<p><i>Ministerial Portfolios, May 1996, p. 230.</i></p>	<p>In the absence of appropriate information systems to accurately assess the condition and maintenance requirements of infrastructure assets, planned maintenance expenditure may be understated. In addition, the Corporation cannot effectively determine the timing and cost of major capital enhancement and renewal expenditure.</p>	<p>Melbourne Water established a new consolidated asset management system in July 1997, to facilitate more effective economic assessment of its planned asset maintenance programs, particularly in respect of mechanical and electrical plant and equipment.</p>
<p><i>Ministerial Portfolios, May 1997, p. 171.</i></p>	<p>There is a prima facie case to suggest that the current levels of unaccounted water among the retail water companies are too high and can be economically reduced.</p>	<p>The retail water companies are reducing the impact of unaccounted water on their businesses through their meter replacement and leakage reduction programs and public education on water efficiency use.</p>
<p><i>Ministerial Portfolios, May 1997, p. 173.</i></p>	<p>With potential revenues in excess of \$10 million available from the replacement of faulty customer water meters, there is considerable scope for the retail water companies to generate benefits from continuing with their meter replacement programs.</p>	<p>All retail water companies are continuing with their meter replacement programs.</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>
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MATTERS RESOLVED OR ACTION COMMENCED - continued

MELBOURNE WATER INDUSTRY REFORM - continued

<p><i>Ministerial Portfolios, May 1997, p. 175.</i></p>	<p>To enable the effective management of water loss through leakages, the retail water companies need to:</p> <ul style="list-style-type: none"> • finalise the development of their leakage control strategies; • establish adequate systems and procedures to identify where leaks are occurring; • place greater emphasis on preventative maintenance; and • determine an acceptable economic level of leakage, using appropriate cost-benefit analysis. 	<p>Strategies designed to reduce infrastructure leakages have been incorporated into water conservation plans, required under each company's operating licence. All 3 retail companies have undertaken assessments to determine acceptable economic levels for unaccounted water. In addition, retail companies maintenance strategies now place greater emphasis on preventative maintenance.</p>
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MELBOURNE WATER CORPORATION

<p><i>Second Report, 1986-87, pp. 164-5.</i></p> <p><i>Ministerial Portfolios, May 1990, p. 343.</i></p> <p><i>May 1992, p. 432.</i></p>	<p>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.</p>	<p>The charging of interest on overdue accounts is currently under consideration by the Regulator-General as part of the current review of the Benchmark Customer Contract.</p>
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ROYAL BOTANIC GARDENS BOARD

<p><i>Ministerial Portfolios, May 1994, pp. 136-46.</i></p>	<p>Action is required to ensure adequate registration and storage of the National Herbarium collection.</p>	<p>The Board is in the process of completing the registration of and providing adequate storage for the collection.</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>
NO ACTION TAKEN		
DEPARTMENT OF NATURAL RESOURCES AND ENVIRONMENT		
<i>Ministerial Portfolios, May 1997, p. 156.</i>	In relation to a number of forest management areas, the Department is incurring costs to allow operators to remove native trees and wood products, with limited financial benefits accruing back to the State.	Situation unchanged.
MELBOURNE WATER INDUSTRY REFORM		
<i>Ministerial Portfolios, May 1996, p. 221.</i>	In order to strengthen the Regulator-General'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 Melbourne Water Corporation's services.	Situation 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>
COMPLETED AUDITS				
Department of Natural Resources and Environment	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	25 Aug. 1997	29 Aug. 1997
AGRICULTURE AND RESOURCES				
Agriculture Victoria Services Pty Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.53A	26 Sept. 1997	17 Nov. 1997
Australian Food Industry Science Centre	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46	19 Aug. 1997	15 Oct. 1997
Avoca River Management Board	30 June 1997	" "	11 Nov. 1997	28 Nov. 1997
Barwon Region Water Authority	30 June 1997	" "	22 Aug. 1997	9 Sept. 1997 (a)
Broken River Management Board	30 June 1997	" "	22 Sept. 1997	14 Oct. 1997
Bullock Creek River Improvement Trust	30 June 1997	" "	14 Oct. 1997	3 Nov. 1997
Central Gippsland Region Water Authority	30 June 1997	" "	27 Aug. 1997	28 Aug. 1997
Central Highlands Region Water Authority	30 June 1997	" "	26 Aug. 1997	27 Aug. 1997
City West Water Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.53A.	20 Aug. 1997	22 Aug. 1997
Coliban Region Water Authority	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	26 Aug. 1997	26 Aug. 1997
Corner Inlet Waterways Authority	30 June 1997	" "	6 Nov. 1997	6 Dec. 1997
East Gippsland Region Water Authority	30 June 1997	" "	14 Aug. 1997	15 Sept. 1997 (a)
East Gippsland River Management board	30 June 1997	" "	25 Aug. 1997	12 Sept. 1997
Emu Industry Development Committee	30 June 1997	" "	8 Dec. 1997	8 Dec. 1997
First Mildura Irrigation Trust	30 June 1997	" "	31 July 1997	12 Sept. 1997
Gippsland and Southern Rural Water Authority	30 June 1997	" "	9 Sept. 1997	29 Sept. 1997
Glenelg Region Water Authority	30 June 1997	" "	6 Nov. 1997	7 Nov. 1997

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>
COMPLETED AUDITS				
AGRICULTURE AND RESOURCES - continued				
Glenelg River Improvement Trust	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	26 Sept. 1997	15 Oct. 1997 (a)
Goulburn Murray Rural Water Authority	30 June 1997	" "	21 Aug. 1997	22 Aug. 1997
Goulburn Valley Region Water Authority	30 June 1997	" "	12 Sept. 1997	12 Sept. 1997 (a)
Grampians Region Water Authority	30 June 1997	" "	5 Sept. 1997	16 Sept. 1997
Kiewa-Murray Region Water Authority	30 June 1997	" "	15 Sept. 1997	18 Sept. 1997
Lake Wellington Rivers Authority	30 June 1997	" "	16 Nov. 1997	2 Dec. 1997
Lower Goulburn Waterway Management	30 June 1997	" "	9 Sept. 1997	12 Sept. 1997
Lower Murray Region Water Authority	30 June 1997	" "	22 Sept. 1997	23 Sept. 1997
Marine and Freshwater Resources Institute	30 June 1997	" "	17 Oct. 1997	17 Oct. 1997
Melbourne Market Authority	30 June 1997	" "	26 Aug. 1997	19 Sept. 1997
Melbourne Water Corporation	30 June 1997	" "	15 Aug. 1997	15 Aug. 1997
Mid-Goulburn Regional Water Board	30 June 1997	" "	10 Sept. 1997	24 Sept. 1997 (a)
Mitchell River Management Board	30 June 1997	" "	16 Oct. 1997	23 Oct. 1997
Murray Valley Citrus Marketing Board	30 June 1997	" "	23 Sept. 1997	1 Oct. 1997
Murray Valley Wine Grape Industry Development Committee	31 July 1997	" "	28 Nov. 1997	9 Dec. 1997
North East Waterways	30 June 1997	" "	17 Sept. 1997	1 Oct. 1997
Northern Victorian Fresh Tomato Industry Development Committee	30 June 1997	" "	8 Feb. 1998	6 Mar. 1998

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>
COMPLETED AUDITS				
AGRICULTURE AND RESOURCES - continued				
Otway Region Water Authority	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	19 Sept. 1997	22 Oct. 1997
Ovens Region Water Authority	30 June 1997	" "	25 Aug. 1997	29 Aug. 1997 (a)
Pental Island River Management Board	30 June 1997	" "	24 Sept. 1997	10 Feb. 1998
Portland Coast Region Water Authority	30 June 1997	" "	24 Sept. 1997	8 Oct. 1997
Radius Computing Pty Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.53A.	8 Sept. 1997	8 Sept. 1997
Radius Computing Pty Ltd	1 July 1997 to 31 Jan 1998	" "	17 Mar. 1998	18 Mar. 1998
Renewable Energy Authority of Victoria	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	23 Sept. 1997	23 Sept. 1997
Snowy River Improvement Trust	30 June 1997	" "	15 Oct. 1997	17 Nov. 1997
South East Water Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.53A.	25 Aug. 1997	25 Aug. 1997
South Gippsland Region Water Authority	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	25 Aug. 1997	9 Sept. 1997
South West Water Authority	30 June 1997	" "	27 Aug. 1997	12 Sept. 1997
Sunraysia Rural Water Authority	30 June 1997	" "	16 Sept. 1997	25 Sept. 1997
Tambo Nicholson River Management Board	30 June 1997	" "	3 Oct. 1997	8 Oct. 1997
Tarwin Bass Waterways Authority	30 June 1997	" "	6 Nov. 1997	4 Dec. 1997
Upper Goulburn Waterways Authority	30 June 1997	" "	3 Oct. 1997	28 Oct. 1997
Upper North East River Management Board	30 June 1997	" "	26 Sept. 1997	14 Oct. 1997

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>
COMPLETED AUDITS - continued				
AGRICULTURE AND RESOURCES - continued				
Veterinary Practitioners Registrations Board of Victoria	31 Dec. 1997	30 April. <i>Financial Management Act 1994</i> s.46.	15 April 1998	21 April 1998
Victorian Dairy Industry Authority	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	27 Aug. 1997	12 Sept. 1997
Victorian Dried Fruits Board	30 June 1997	" "	15 Sept. 1997	17 Oct. 1997
Victorian Meat Authority	30 June 1997	" "	27 Aug. 1997	27 Aug. 1997
Victorian Plantations Corporation	30 June 1997	" "	15 Aug. 1997	15 Aug. 1997
Victorian Strawberry Industry Development Committee	30 June 1997	" "	29 Jan. 1998	3 Feb. 1998
Water Training Centre	30 June 1997	" "	13 Oct. 1997	20 Oct. 1997
Western Region Water Authority	30 June 1997	" "	10 Sept. 1997	30 Sept. 1997
Westernport Region Water Authority	30 June 1997	" "	29 Sept. 1997	30 Sept. 1997
Wimmera Mallee Rural Water Authority	30 June 1997	" "	5 Sept. 1997	5 Sept. 1997
Yarra Valley Water Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.53A.	25 July 1997	25 July 1997
CONSERVATION AND LAND MANAGEMENT				
Alpine Resorts Commission	31 Oct. 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	22 Dec. 1997	23 Dec 1997
Bairnsdale Regional Waste Management Group	30 June 1997	" "	17 Oct. 1997	13 Nov. 1997
Bundoora Park Committee of Management	1 July 1995 to 19 Jan. 1996	19 May <i>Financial Management Act 1994</i> , s.46	17 Mar. 1997	14 May 1997
Eastern Regional Waste Management Group	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	26 Feb. 1997	4 Sept. 1997
Eco Recycle Victoria	30 June 1997	" "	30 Aug. 1997	30 Sept. 1997

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>
COMPLETED AUDITS - continued				
CONSERVATION AND LAND MANAGEMENT - continued				
Environment Protection Authority	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46	15 Sept. 1997	16 Sept. 1997
Northern Regional Waste Management Group	30 June 1997	" "	22 Oct. 1997	14 Nov. 1997
Parks Victoria	30 June 1997	" "	18 July 1997	18 July 1997
Phillip Island Nature Park Board of Management	30 June 1997	" "	29 Sept. 1997	6 Oct. 1997 (a)
Port Bellarine Committee of Management	30 June 1997	" "	4 Dec. 1997	15 Jan. 1998
Royal Botanic Gardens Board	30 June 1997	" "	15 Sept. 1997	26 Sept. 1997
Shrine of Remembrance Trustees	30 June 1997	No reporting requirements.	29 Jan. 1998	3 Feb. 1998
South Eastern Regional Waste Management Group	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46	25 Sept. 1997	14 Nov. 1997
Surveyors Board of Victoria	30 June 1997	" "	27 Aug. 1997	27 Aug. 1997
Trust for Nature (Victoria)	30 June 1997	" "	25 Sept. 1997	30 Oct. 1997 (a)
Western Regional Waste Management Group	30 June 1997	" "	26 Sept. 1997	15 Oct. 1997
Yarra Bend Park Trust	30 June 1997	" "	30 Sept. 1997	2 Oct. 1997
Zoological Parks and Gardens Board	30 June 1997	" "	20 Aug. 1997	4 Sept. 1997

(a) Qualified audit report issued.

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - continued

<i>Entity</i>	<i>Financial year ended</i>	<i>Reporting to Parliament</i>	
INCOMPLETE AUDITS			
AGRICULTURE AND RESOURCES			
Tungamah Shire Water Board	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46	Financial statements not received
CONSERVATION AND LAND MANAGEMENT			
Alpine Resorts Commission	1 Nov. 1997 - 29 Apr. 1998	29 Aug. <i>Financial Management Act 1994</i> , s.46	Financial statements not received.
State Swimming Centre Committee of Management	30 June 1995	31 Oct. <i>Financial Management Act 1994</i> , s.46	Financial statements not received.
" "	30 June 1996	" "	" "
" "	30 June 1997	" "	" "
" "	31 Dec. 1997	30 April. <i>Financial Management Act 1994</i> , s.46	" "

Part 3.6

Premier and Cabinet

KEY FINDINGS	
Administration of the Community Support Fund	
<ul style="list-style-type: none">Aggregate revenue from the commencement of the Community Support Fund in July 1992 to February 1998 totalled \$326 million, with weekly revenue of the Fund from gaming activities now reaching around \$1.8 million.	<i>Para. 3.6.8</i>
<ul style="list-style-type: none">As at February 1998, distributions from the Fund totalling \$322 million had been approved, with actual cash payments totalling \$169 million.	<i>Para. 3.6.9 to 3.6.10</i>



3.6.1 The Premier, who is also the Minister for the Arts and Multicultural Affairs, has responsibility for operations within the Premier and Cabinet portfolio.

3.6.2 Details of the specific ministerial responsibilities for public bodies within the Premier and Cabinet portfolio are listed in Table 3.6A. These public bodies, together with the Department of the Premier and Cabinet, were subject to audit by the Auditor-General during the 1996-97 financial year.

**TABLE 3.6A
MINISTERIAL RESPONSIBILITY FOR
PUBLIC SECTOR AGENCIES WITHIN THE PREMIER AND CABINET PORTFOLIO**

<i>Ministerial portfolio</i>	<i>Agencies subject to audit</i>
Arts	Council of Trustees of the National Gallery of Victoria Geelong Performing Arts Centre Trust Library Board of Victoria Melbourne 2006 Commonwealth Games Bid Pty Ltd Museums Board of Victoria State Library of Victoria Foundation Victorian Arts Centre Trust
Multicultural Affairs	Victorian Interpreting and Translation Service
Premier	Office of the Ombudsman Office of the Public Service Commissioner Victorian Auditor-General's Office Victorian Relief Committee

3.6.3 Comments on matters of significance arising from the audit of entities within the Premier and Cabinet portfolio is provided below.

ADMINISTRATION OF THE COMMUNITY SUPPORT FUND

3.6.4 The Community Support Fund was established under the provisions of the *Gaming Machine Control Act 1995*. The legislation requires 8 1/3 per cent of the total daily net cash balances (i.e. the total amount wagered less the sum of all prizes paid) derived from electronic gaming machines in hotels (which, to date, includes all approved gaming venues not holding a club liquor licence) to be paid into the Consolidated Fund, and an equivalent amount transferred to the Community Support Fund by way of a standing appropriation.

3.6.5 Up to April 1996, the Minister for Gaming under the provisions of the Act, applied moneys from the Fund in the following manner:

- firstly, for the purpose of research relating to the social impact of gambling;
- secondly, 70 per cent of the remainder to the Ministers responsible for Sport and Recreation and Community Services for various programs within their agencies; and
- thirdly, the balance to the Ministers for Arts and Tourism for the promotion of Arts and Tourism.



3.6.6 In accordance with machinery of government changes, as from April 1996 the Premier assumed responsibility for the Fund. Furthermore, under amendments to the Act which were effective from July 1996, the Fund was authorised to make payments firstly, for the purpose of research relating to the social impact of gambling and, secondly, for the following purposes:

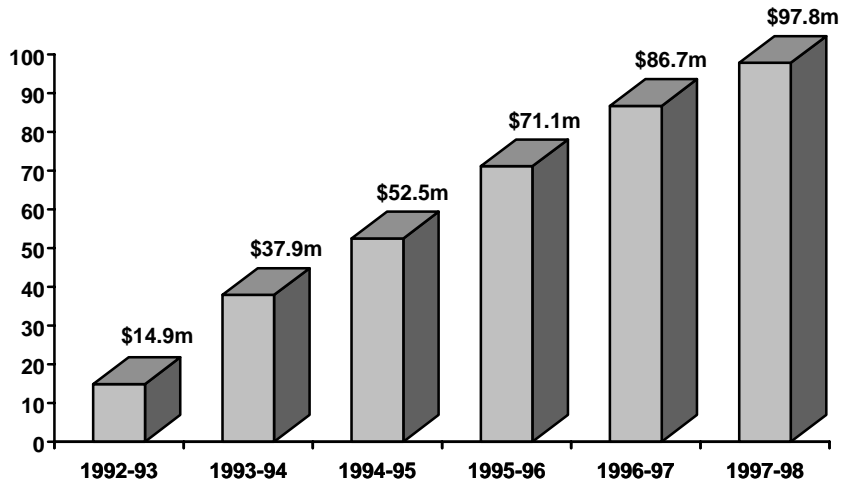
- programs for the prevention of compulsive gambling or for the treatment or rehabilitation of persons who are compulsive gamblers;
- programs for the treatment or rehabilitation of persons who are addicted to, or abuse, drugs;
- education programs relating to drug addiction or drug abuse;
- programs for financial counselling services or support and assistance for families in crisis;
- programs for the benefit of youth;
- research or pilot programs relating to community advancement programs;
- programs for the benefit of sport or recreation;
- programs for the promotion or benefit of the arts;
- programs establishing or developing tourist destinations or facilities or services or for the purposes of promoting tourism; and
- any other programs or purposes relating to the support or advancement of the community as determined by the Minister.

3.6.7 Further amendments to the Act which were effective from 12 November 1996 provided for administrative expenses of the Fund to be paid out of the Fund revenues. These costs amount to approximately \$500 000 per annum.

Fund revenues

3.6.8 My Special Report No. 40, tabled in to the Parliament in May 1996, outlined the significant increase in the level of funding available for distribution to approved projects since the commencement of the Fund in July 1992. This trend has continued with the **aggregate revenue** (including interest and loan repayments) **from its commencement to February 1998 totalling \$326 million. The weekly revenue of the Fund from gaming activities alone has now reached around \$1.8 million** (equivalent to an annual revenue of \$91 million), which represents a 39 per cent increase since the 1995-96 financial year. Chart 3.6B highlights the marked increase in the annual revenue of the Fund over the period 1992-93 to 1997-98.

CHART 3.6B
ANNUAL REVENUE TO THE FUND,
1992-93 TO 1997-98 (a)
 (\$million)



(a) 1997-98 figure is based on an estimate provided by the Department of Premier and Cabinet which has the responsibility for managing the Fund.

Distributions from the Fund

3.6.9 As at February 1998, distributions from the Fund totalling \$322 million had been approved, with actual cash payments totalling \$169 million. By far the largest project financed by the Fund is the Melbourne Sports and Aquatic Centre which was officially opened in July 1997. The total cost of this project was \$65 million, of which \$55.5 million was met from the Fund. The project was managed by the Office of Major Projects which reports to the Minister for Planning and Local Government. The Centre, since its opening, has been managed by a 7 member Trust reporting to the Minister for Sport and Rural Development.

3.6.10 Table 3.6C presents a summary of the approved distributions from the Fund to the end of February 1998 under major expenditure categories.

TABLE 3.6C
COMMUNITY AND SUPPORT FUND, - APPROVED PROJECTS,
AT 28 FEBRUARY 1998
(\$million)

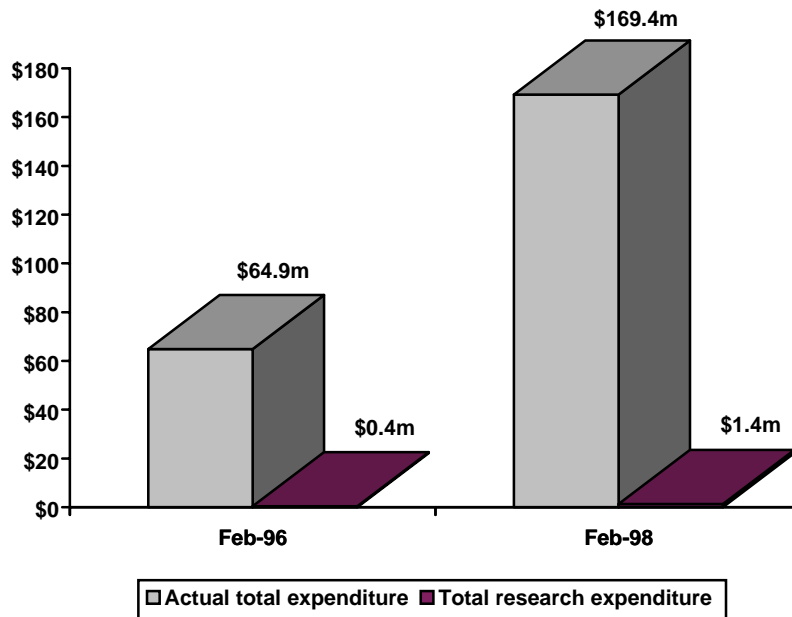
<i>Programs and projects</i>	<i>Amount</i>
<i>Turning the Tide drug initiatives (\$71 million), including -</i>	
Establishment of special court advisory service	15.7
Individual school drug education strategies	11.7
Youth Substance Abuse Service	10.5
Program to increase capability of counselling services	8.6
Development, of and training in, core competencies for key workers dealing with drug affected people	6.0
Upgrade of drug detection, deterrence and treatment	5.3
Investigation of substitute medications	3.2
A program to support local level community	2.3
<i>Sport and recreation (\$70 million), including -</i>	
Melbourne Sports and Aquatic Centre	55.5
Sport and Recreation Minor Facilities Grants Scheme	7.5
Victorian Institute of Sport Athlete Program	2.7
Lifesaving into the 21st Century	2.0
<i>Arts (\$58 million), including -</i>	
Establishment of the Immigration Museum	19.0
Relocation of the Planetarium to Scienceworks	6.0
Victoria State Opera	2.4
The Victoria Commissions - a fund to enable the commission of new major artistic works	2.2
Arts Victoria Touring Victoria Program	2.0
<i>Initiatives to address problem gambling (\$34 million), including -</i>	
Consolidation of problem gambling program - new program to ensure continuation, development and if appropriate refinement of services	7.3
Statewide family skills centre and regional family resource centre	6.6
Problem gambling program expansion - increase in counselling services	4.2
Initiatives to address problem gambling - establishment of counselling services	4.1
<i>Tourism (\$27 million), including -</i>	
Regional tourism signage	3.5
City of Ballarat EUREKA project	2.4
Royal Botanic Gardens	2.0
Port Philip Bay Bid relating to 1998 America's Cup Challenge	1.5
Rialto Sky Show Down Under	1.0
Refurbishment of fruit packing house for promotion of Goulburn Valley's food and wine industry	1.0
<i>Youth (\$25 million), including -</i>	
Intensive training and Employment Support Program	5.1
VRAP 9 - transportation costs for students to participate in Victorian Performing Arts Centre Arts Education Program	3.7
Major infrastructure for homeless youth services	2.0
<i>"Family in Crisis" (\$17 million), including -</i>	
Family and parenting programs	5.9
Families with severely disabled children	5.5
Victim of child abuse - service and support	3.7
<i>Other (\$19 million), including -</i>	
Rural Community Development Scheme	13.0
Provision of trailers and wheelchair hoists for regional mobile libraries	2.5
Bone Marrow Institute Accommodation Centre	1.7

Research into the social impact of gambling

3.6.11 The legislation requires the Victorian Casino and Gaming Authority to commission research into, and advise the Minister on, the social impact of gambling, which is to be financed from the Fund.

3.6.12 The legislation clearly indicates that such research is the first priority for the allocation of moneys from the Fund. Since the commencement of the Fund until 28 February 1998, expenditure totalling \$1.4 million (0.8 per cent of total expenditure to date) had been drawn-down by the Authority for the task of undertaking research into the social impact of gambling. Chart 3.6D shows the level of expenditure spent on funding research into problem gambling.

**CHART 3.6D
LEVEL OF RESEARCH FUNDING
(\$million)**



3.6.13 My Special Report No. 54 of March 1998 titled *Victoria's Gaming Industry: An insight into the role of the regulator* detailed an evaluation of the research funded by the Authority into the social impact of gambling. In that Report, it was concluded that the Victorian Casino and Gaming Authority has overseen in recent years an extensive range of research activity into the social impact of gambling and that the Authority should be commended for arranging during 1997 a research project which analysed and evaluated the results of all past research projects it managed.



**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>
MATTERS RESOLVED OR ACTION COMMENCED		
DEPARTMENT OF PREMIER AND CABINET		
<i>Ministerial Portfolios, May 1997, pp. 294-5.</i>	<p>There is a need for the Department to strengthen its authorisation and verification procedures to ensure the probity and accountability of all Corporate Card payments.</p> <p>Audit identified several instances where Corporate Card transactions had not been independently approved, cardholders had not confirmed the receipt of related goods and services and transactions were not supported by adequate supporting documentation. Consequently it was difficult to determine whether such expenditure was incurred for official purposes.</p>	<p>The Department of has reviewed and re-issued the acknowledgment form for corporate card recipients which contains specific guidelines on usage. The revised form has been signed by all existing cardholders.</p> <p>Comprehensive guidelines on the use of corporate card are currently being developed and include advice on who should have a card, how it should be used, user responsibilities and accountability requirements. Internal procedures have been reviewed and now require the monthly corporate card statement to be authorised by the cardholder and countersigned by another financial delegate to indicate that the transactions are valid for business purposes and are approved for payment. Refer further comments included in this Report under Schedule A for the Department of Treasury and Finance.</p>
VICTORIAN ARTS CENTRE TRUST		
<i>Ministerial Portfolios, May 1994, pp. 58-9.</i>	<p>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 and accountability to the Parliament.</p>	<p>The Trust has been allocating indirect overhead expenses to operating units for management reporting purposes since 1996. However, the anticipated inclusion in the 1996-97 financial statements of a note disclosing the level of activity of the operating units, including an allocation of indirect overhead expenses, did not occur. It is anticipated that this information will be included in the 1997-98 financial statements.</p>
<i>Ministerial Portfolios, May 1994, pp. 68-9.</i>	<p>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.</p>	<p>The hearing of the case commenced in the courts in February 1998. The Trust remains confident of a successful recovery action.</p>

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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>
COMPLETED AUDITS				
Department of the Premier and Cabinet	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	28 Aug. 1997	29 Aug. 1997
ARTS				
Council of Trustees of the National Gallery of Victoria	30 June 1997	" "	27 Aug. 1997	27 Aug. 1997
Geelong Performing Arts Centre Trust	30 June 1997	" "	17 Sept. 1997	30 Sept. 1997
Library Board of Victoria	30 June 1997	" "	29 Aug. 1997	2 Sept. 1997
Melbourne 2006 Commonwealth Games Bid Pty Ltd	Period 1 Jan. to 30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.53A.	26 Sept. 1997	26 Sept. 1997
Museums Board of Victoria	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	25 Aug. 1997	2 Sept. 1997
State Library of Victoria Foundation	30 June 1997	" "	29 Aug. 1997	2 Sept. 1997
Victorian Arts Centre Trust	30 June 1997	" "	29 Aug. 1997	2 Sept. 1997
MULTICULTURAL AFFAIRS				
Victorian Interpreting and Translation Service	30 June 1997	" "	19 Nov. 1997	21 Nov. 1997
PREMIER				
Office of the Ombudsman	30 June 1997	" "	29 Sept. 1997	1 Oct. 1997
Office of the Public Service Commissioner	30 June 1997	" "	11 Sept. 1997	11 Sept. 1997
Victorian Auditor-General's Office (a)	30 June 1997	" "	19 Aug. 1997	19 Aug. 1997
Victorian Relief Committee	30 June 1997	" "	25 Sept. 1997	26 Sept. 1997

(a) The Victorian Auditor-General's Office was audited by a firm of private auditors.

Part 3.7

State Development

KEY FINDINGS

The year 2000 Issue - The Millennium Bug

- None of the entities examined by audit are currently year 2000 compliant. As certain entities examined were yet to begin replacing or converting non-compliant systems and other equipment, these entities face the risk that their businesses may be detrimentally affected by non-compliant systems.

Paras 3.7.11 to 3.7.14

3.7.1 The Minister for Industry, Science and Technology, the Minister for Multimedia, the Minister for Sport and Rural Development and the Minister for Small Business and Tourism have responsibility for operations within the State Development portfolio. 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 portfolio are listed in Table 3.7A. These public bodies, together with the Department of State Development, were subject to audit by the Auditor-General during the 1996-97 financial year.

**TABLE 3.7A
MINISTERIAL RESPONSIBILITIES FOR
PUBLIC BODIES WITHIN THE STATE DEVELOPMENT PORTFOLIO**

<i>Ministerial portfolio</i>	<i>Entities subject to audit</i>
Industry, Science and Technology	Construction Industry Long Service Leave Board (a) Melbourne Convention and Exhibition Trust Overseas Projects Corporation of Victoria Ltd Victorian Medical Consortium Pty Ltd
Multimedia	Film Victoria State Film Centre of Victoria Council
Small Business	Liquor Licensing Commission
Sport	Greyhound Racing Control Board Harness Racing Board Melbourne and Olympic Parks Trust Melbourne Sports and Aquatic Centre Trust Victorian Institute of Sport Ltd Victorian Institute of Sport Trust
Tourism	Australian Grand Prix Corporation Emerald Tourist Railway Board Tourism Victoria

(a) Control and management of the fund transferred to the building industry on 1 November 1997.

3.7.3 Comment on matters of significance arising from the audit of entities within the State Development portfolio is provided below.

THE YEAR 2000 ISSUE - THE MILLENNIUM BUG

3.7.4 My May 1997 *Report on Ministerial Portfolios* commented on a significant issue confronting all organisations that maintained computerised systems which utilise date sensitive software and databases. The issue relates to the capacity of such systems to cope with the changes of dates from the year 1999 to 2000.



3.7.5 This issue is not only relevant to business computer systems, but other equipment with electronic chips which have date functionality, such as lifts, security systems, telephone systems and medical equipment. It is important to recognise that even if systems are year 2000 compliant they can still be affected by this problem if they receive data from non-compliant systems.

3.7.6 In my previous Report, I commented that while the majority of entities who responded to a comprehensive audit survey appeared to have some level of awareness of the issue, little action had been taken to resolve the year 2000 issue problems each entity was facing.

Key initiatives to address the year 2000 issue

3.7.7 Multimedia Victoria, which is a business unit within the Department of State Development, has responsibility to drive and co-ordinate the Government's Victoria 21 Strategy for multimedia, communications and information technology. The business unit works in co-operation with departments across government to ensure a co-ordinated approach to the implementation of the strategy. Consistent with this role, since July 1996, Multimedia Victoria with respect to the year 2000 issue within the inner budget sector has initiated substantial action, the key elements of which include:

- continually raising awareness of the issue;
- establishment of clear policy and technical standards;
- allocation of responsibility and accountability for the issue to chief executive officers within organisations;
- monitoring progress and recommending action where required;
- regularly informing the Minister for Multimedia of progress to date;
- facilitation of cross-departmental co-operation where appropriate; and
- alignment of Victorian Government strategies with national strategies.

3.7.8 Some of the key actions taken since July 1996 include:

- Multimedia Victoria issued the government policy on the year 2000 issue to all departmental secretaries and IT directors, which alerted organisations to the likelihood of problems relating to processing, the non-negotiable time frame for addressing the issues and the potentially high cost of correction. In addition, standard year 2000 warranty clauses were provided for future system acquisition contracts;
- The Minister for Multimedia advised all Ministers of the release of the year 2000 policy and that the responsibility for the maintenance of services rested with departmental secretaries. Subsequently, the Minister for Multimedia wrote to all Ministers expressing concern that the issue was not receiving the level of attention that was required. Ministers were in turn requested to provide details of the plans and actions to address the issue for their portfolios by 31 December 1997;
- A year 2000 seminar for all IT directors and other appropriate officers was conducted by an industry expert in the area and a special interest group for year 2000 project managers was established;

- Victoria joined the joint Commonwealth/States year 2000 working party to establish a national strategy;
- Victorian utilities were polled by the relevant industry regulators in relation to their ability to maintain product supply at the turn of the century;
- Consultants were engaged to review the preparedness of 3 budget sector agencies with this issue;
- The Department of Education commenced the evaluation of the various year 2000 testing tools for personal computers on behalf of all departments;
- A “Time and Date Data Definition Policy” was issued to all departments which provides guidance on the conventions to be utilised for the recording of time and dates;
- Consultants were appointed during January 1998 to review details of the year 2000 plans and actions of portfolios. In April 1998, the consultants completed the review and provided various recommendations to Multimedia Victoria;
- Regular interaction between officers at the State and Commonwealth levels; and
- Re-direction of informative articles, including vendor promotional material, to year 2000 project managers and IT directors.

Audit review

3.7.9 In recognition of the many initiatives within the budget sector to address the year 2000 issue and the importance of the issue to the future operations of government, including the non-budget sector, my Office conducted a review of a small number of non-budget sector agencies to obtain a more in-depth picture on the preparedness of these entities to address the year 2000 issue. The entities selected were:

- Alfred Hospital (one of 10 hospitals in the Inner and Eastern Health Care Network);
- Victorian Superannuation Board (VicSuper);
- Gippsland and Southern Rural Water Authority (Southern Rural Water);
- Manningham City Council;
- State Trustees;
- Knox City Council; and
- Kangan Batman TAFE.

3.7.10 The audit focused on the entities’ progress in relation to the following key elements identified as essential to adequately address the year 2000 issue:

- awareness;
- assessment;
- conversion;
- verification; and
- implementation.

Overall conclusion

3.7.11 With the exception of VicSuper and Manningham City Council, entities are either in the early stages of taking the required action or have not yet reached the stage of determining the work required to make their key systems and critical non-IT equipment year 2000 compliant.

3.7.12 The major concerns identified by audit regarding the status of the respective entities' year 2000 projects and the approaches taken, include:

- none of the entities examined had completed a detailed year 2000 project plan;
- with one exception, entities had not yet completely identified the resources required (both financial and human) to achieve year 2000 compliance;
- while 3 entities were in the process of developing contingency plans, 4 entities did not intend developing such plans for critical systems and activities to ensure continuity of core business processes;
- none of the entities had commenced any testing of existing, converted or replaced systems to identify non-compliant date references; and
- entities intending to place reliance on testing performed by external parties had not developed strategies to ensure that system testing, which will be performed by these parties will be of an appropriate standard.

3.7.13 None of the entities examined are currently year 2000 compliant. As certain entities were yet to begin replacing or converting non-compliant systems and other equipment, these entities face the risk that their businesses may be detrimentally affected by non-compliant systems.

3.7.14 Although all entities had identified project completion deadlines, given the progress at the time of preparation of this Report, the feasibility of all entities achieving this goal is uncertain. This is of particular concern, given there is little scope for slippage which is usually common to other development projects.

Awareness of the issue

3.7.15 It is important that senior management and staff throughout the organisation have a thorough appreciation of the year 2000 issue and its potential effect on the entities ability to continue to perform both core and secondary functions. Each entity should take steps to promote staff awareness and, in particular, should:

- objectively evaluate whether external expert assistance needs to be sought;
- develop a high-level strategy which is approved by the entity's executive;
- establish an executive group with responsibility for co-ordinating and monitoring year 2000 work; and
- establish project teams with responsibility for performing specific tasks.

3.7.16 The audit review identified that Kangan Batman TAFE had not prepared for organisational dissemination any high level internal documentation explaining the year 2000 issue and its potential impact. By contrast, Southern Rural Water, State Trustees, VicSuper, Knox and Manningham City Councils had prepared appropriate documentation providing a straightforward explanation of the problem and indicating how the organisations may be affected. In relation to the Inner and Eastern Health Care Network, it had issued documentation to each hospital within the network which explains the year 2000 problem and, in broad terms, its potential impact on the hospitals.

3.7.17 The Alfred Hospital and VicSuper are both conducting projects which will address compliance issues for certain major systems, with the Alfred Hospital undertaking a particular project called "NxIS", aimed at replacing patient management systems and network infrastructure. VicSuper was converting 4 significant systems to a compliant platform as part of the "Migration Project", with significant upgrades to some of these systems required to achieve that goal.

3.7.18 Manningham and Knox City Councils have sought external expert assistance in managing their year 2000 projects while VicSuper has engaged external expert assistance in managing their "Migration Project". The Inner and Eastern Health Care Network, inclusive of the Alfred Hospital, has performed a detailed analysis of resourcing requirements for the "NxIS" project, has undertaken an assessment of resources required for non-IT work and has acquired the additional identified resources. Although no formal assessments of estimated resource and skill requirements have been undertaken by the remaining 3 entities, they have decided that neither external assistance in management of the project nor further training of in-house staff is required. However, many of the entities examined are participating in information sharing arrangements which provide them with access to external advice.

3.7.19 High-level strategy documents addressing the year 2000 issues have been issued by State Trustees, Inner and Eastern Health Care Network and Manningham and Knox City Councils. While Southern Rural Water management is actively supportive of the year 2000 project and has developed a high-level year 2000 strategy, there had been no formal endorsement of its strategy. The remaining 2 entities had not documented a high-level strategy for tackling the year 2000 problem.

3.7.20 Project managers have been appointed by all entities to be responsible for co-ordinating year 2000 program activities, and they have been involving both technical and user management in these activities.

3.7.21 At the Alfred Hospital, VicSuper, Manningham and Knox City Councils, and Kangan Batman TAFE, regular updates on the progress of the entities' year 2000 projects are provided at Executive or Steering Committee meetings, while Southern Rural Water monitors progress on year 2000 at both its monthly Audit Committee and Board meetings. The remaining 2 entities have not established formal procedures to monitor progress.



3.7.22 To ensure that an appropriate level of awareness of the magnitude and potential affect of the year 2000 issue is established, it is important that any entity with an exposure to problems associated with this issue:

- clearly documents the year 2000 issue and its potential impact for dissemination to the executive and general staff;
- prepares a high level strategy to address the problem which is fully supported executive management;
- performs a formal analysis of the entity’s ability to manage the year 2000 project, and to identify whether external assistance or training is required; and
- as well as appointing a project manager and establishing project teams to perform year 2000 related activities, it is important that formal procedures are established to monitor progress, with executive staff receiving regular updates on the status of the project.

Assessment of the task

3.7.23 As an aid to the assessment of the task, entities need to develop a comprehensive inventory which covers all software, hardware and non-IT equipment with embedded chip technology and then prioritise year 2000 project work to ensure that the entities’ core business processes are able to continue. It is important that a strategy is developed for all inventory items determined to be non-compliant, outlining one of 4 main alternatives available to rectify the problem, namely, retirement, repair, replacement or retention where non-compliance does not effect the entity’s operations.

3.7.24 The audit found that some of the agencies reviewed had undertaken a comprehensive inventory of the hardware, software and non-IT equipment which may be affected by the year 2000 issue. In particular, the review revealed that:

- Manningham City Council, Inner and Eastern Health Care Network, Kangan Batman TAFE and State Trustees have adopted a formal definition of year 2000 conformity, against which inventory items can be assessed for compliance;
- The Alfred Hospital has developed a risk-assessment model which prioritises the year 2000 work according to probability of failure and its resultant impact on the hospital, and has prepared a comprehensive asset listing of all medical and IT equipment within the hospital. However, it has not completed an assessment of the potential impact that failure of systems not covered in its “NxIS” project would have on operations, or determined an approach to rectify these systems; and
- Manningham City Council, Kangan Batman TAFE and Southern Rural Water have prioritised the work to be performed with regard to the potential impact that non-compliance would have on their core business areas. While VicSuper and State Trustees have not formally prioritised the work to be performed with regard to inventory items, they have considered the effect of non-compliance on core business areas.

3.7.25 While none of the entities have completed a comprehensive year 2000 project plan recording details for all tasks and phases of the project, the review found:

- Manningham City Council is the only entity to have comprehensively identified both the financial and human resources required to achieve compliance, while Kangan Batman TAFE, Knox City Council, State Trustees and Manningham City Council have estimated total funds required to achieve year 2000 compliance; and
- VicSuper and the Alfred Hospital have documented a testing approach and determined test facilities required specific to the “Migration” and “NxIS” projects. While Manningham City Council has identified a testing approach and test facilities required, other entities have not yet developed a logical testing approach to identify non-compliance or defined requirements for year 2000 test facilities.

3.7.26 All entities, with the exception of State Trustees and Knox City Council, have written to suppliers of IT components requesting written assurances of year 2000 compliance. In addition, Kangan Batman TAFE, Manningham City Council, VicSuper and Southern Rural Water have written to suppliers of non-IT components requesting written assurances of year 2000 compliance. While the Alfred Hospital has performed this task for medical equipment and services provided by public utilities, it has not as yet addressed other non-IT equipment. In relation to any new IT or non-IT equipment purchased, all entities now require that they be compliant.

3.7.27 Only VicSuper and Manningham City Council have contacted external parties with links to their systems to ensure they will not be adversely affected by non-compliance of external parties systems and data.

3.7.28 To ensure that entities are able to adequately assess the extent of their year 2000 problem and determine appropriate action, it is important that:

- the impact of non-compliance on core business processes is evaluated;
- comprehensive inventories of IT elements and non-IT elements with embedded chip technology are prepared, with items prioritised according to criticality;
- a detailed project plan, covering each phase of the project is established;
- project teams with specific objectives and dead-lines are established;
- specific monetary and human resources required to achieve year 2000 compliance are identified;
- a detailed testing approach for identifying non-compliant date references be developed, which includes determining test facilities and any year 2000 tools needed to assist with testing and conversion;
- warranties and statements of compliance be sought from suppliers to mitigate legal and financial liabilities; and
- links between internal and external systems be identified, and external data providers contacted to obtain assurances that problems will not arise through the receipt of non-compliant data.

Conversion and Verification

3.7.29 The conversion and verification (or testing) phases of the year 2000 projects are of extreme importance. Testing is necessary to validate that products are compliant and will interact properly in the computer environment. Even products for which the entity has received vendor assurances of year 2000 compliance should be subject to some future date testing. Adequate test facilities need to be made available so that software can be thoroughly tested without corruption of operational systems. It has been estimated by year 2000 experts that approximately half the time spent by an entity on the year 2000 issue should be devoted to testing.

3.7.30 The audit review indicated that a significant amount of work remained outstanding relating to the conversion and testing of systems (both IT and non-IT) by agencies. In particular, it was found that:

- VicSuper and State Trustees had substantially completed the process of converting a critical business application while the Alfred Hospital and Manningham City Council have completed converting one critical business application. Other entities have not yet made any substantial progress in converting or replacing major applications, platforms, databases, operating systems or other non-compliant components;
- VicSuper and the Alfred Hospital have documented modifications to systems made to date while the other entities anticipate that documentation will be provided by vendors for the majority of IT changes;
- VicSuper is the only entity reviewed to have established extensive testing schedules specific to the “Migration Project” while Manningham City Council is currently developing detailed test plans. The other entities have not as yet commenced recording test plans;
- With the exception of one major application at Manningham City Council and an application at the Alfred Hospital, none of the entities have as yet eliminated software, platforms or operating systems identified as non-compliant. Both VicSuper and the Alfred Hospital intend to replace their existing non-compliant platforms upon completion of successful testing;
- While the Alfred Hospital and Southern Rural Water intend placing reliance on some testing performed by external parties, they had not developed a strategy to ensure that system testing performed by these parties will be of an appropriate standard; and
- None of the entities had commenced formal testing of systems to identify non-compliant date references. However, the Kangan Batman TAFE, State Trustees, Southern Rural Water and Manningham City Council have performed testing to assess compliance of some personal computers.

3.7.31 In relation to the conversion and verification phases of the year 2000 projects, it is important that entities ensure that:

- modifications to existing systems and their components be documented, and communicated to internal and external users, with training provided where necessary;
- comprehensive system testing be scheduled, with documented test plans developed for each replaced or converted system or IT component;

- a strategy be developed to ensure that any testing performed by external parties is of an appropriate standard; and
- progress throughout the conversion and verification phases be formally monitored to help manage the cost and timing of completions.

Implementation

3.7.32 Subsequent to achieving satisfactory test results, compliant software and hardware need to be implemented. This process will require careful co-ordination to ensure that system inter-dependencies are taken into account. Furthermore, it is important that contingency plans are developed so that critical functions may continue in the event, despite best endeavours, that the year 2000 issue nevertheless causes disruptions. Disaster recovery plans should also be updated to cover any changes that have been made to the computer environments in order to achieve compliance. Audit found that agencies were not well placed in respect to implementation and disaster recovery planning. In particular, it was identified that:

- Only VicSuper and Manningham City Council have developed an implementation schedule;
- VicSuper, Southern Rural Water and State Trustees were the only entities to have commenced conversion of databases;
- Acceptance testing had not commenced at any of the entities reviewed;
- Manningham City Council is in the process of developing contingency plans as part of its year 2000 project and VicSuper and Alfred Hospital intend to develop contingency plans for all systems. However, the other 4 entities have not developed contingency plans and do not intend to do so;
- Only VicSuper and Knox City Council have existing disaster recovery plans which they expect to update in 1998. However, State Trustees and the Alfred Hospital are in the process of developing a disaster recovery plan; and
- With the exception of Manningham City Council and the Alfred Hospital, other entities have not integrated, converted or replaced major systems and related databases.

3.7.33 At the time of the audit review none of the entities examined had achieved year 2000 compliance.

RESPONSE provided by Secretary, Department of State Development

As noted in your Report, Multimedia Victoria has had an active year 2000 role for nearly 2 years. The most recent Year 2000 review by Multimedia Victoria (April 1998) into the preparedness of the budget sector has come to similar overall conclusions to yourself that insufficient progress has been made towards year 2000 compliance by departments and agencies. Multimedia Victoria is now preparing further recommendations for consideration by the Government.



❑ **RESPONSE** provided by Chief Executive Officer, Kangan Batman, TAFE

I believe the Report to be fair and accurate.

I take the opportunity to thank you for the advice provided in your Report and throughout the audit. Kangan Batman has found the recommendations and comments to be most helpful in assisting us to address the Y2000 issue.

❑ **RESPONSE** provided by Chief Executive Officer, Knox City Council

It is fair to say that the document accurately reflects the position of this Council as at the date that the review was undertaken.

Of course work is being undertaken on a regular basis in regard to this issue and I would like to take this opportunity to highlight works that have been undertaken since the initial round of interviews.

Awareness

As your report correctly identified, Council has engaged Arthur Andersen and Unisys Australia to provide expert assistance and support. Arthur Andersen has completed the development of our I.S. Strategy and Council has appointed an I.S. Manager (new position) to oversee both the strategy and the year 2000 program.

Council has more recently engaged Arthur Andersen to undertake a process of developing a Business Case, in line with Council's Information Systems Strategy, for the replacement of the WCS Property and Rating system. This is the one major system that Council uses, that is not currently compliant. This process will provide for the upgrade of this system with considerable buy-in from end-users and those people affected by the relevant applications. This is in addition to the applications that have already been upgraded and are now year 2000 compliant, namely, the Financial and H/R systems.

Generally, Council believes that staff are aware of the year 2000 issue, particularly Executive and Senior Managers. Staff will be used in developing solutions throughout the process.

Progress reports are made fortnightly to the I.T. Steering committee and the Executive team on a regular basis.

Assessment

The engagement of Unisys to carry out a compliance assessment of equipment and software on Council's network includes a process of formally defining year 2000 compliance. This is now complete and has been incorporated into the project plan with Unisys.

The work being undertaken by Unisys includes testing of all equipment on the network including bridges, routers and network and mainframe components.

A preliminary report has been received by Unisys on both hardware and software which is being evaluated and remedial works prioritised.

All staff have been asked to provide details of any equipment that they have within their working environment that they believe has any embedded chip technology. This information is required so that the equipment can be tested and remedial works programmed.

❑ **RESPONSE** provided by Chief Executive Officer, Knox City Council - continued

Assessment - continued

The I.S. Strategy provides funding over the next 3 years to address all I.S. issues, including the year 2000 issue. The additional budget provision over this period is \$2.5 million.

The approach used by Unisys in evaluating our hardware and software compliance is "state-of-the-art" technology and will utilise all year 2000 tools needed to assist in identifying non-compliance.

In addition, staff have been requested to provide details of all external data providers and letters will be sent to all identified providers to enable Council to assess and monitor their compliance.

Conversion and Verification

Council, as part of the Business Case for the upgrade of the WCS system, will be including a detailed analysis and selection process. The specification that is developed will require training to be included and will also seek indemnifications against any losses as a result of the disruption to business caused by any non-compliance on selected systems.

The output provided by Unisys will include a list of all non-compliant components and provide details of what remedial works, including options where available, can be undertaken. A program will be put in place to ensure this occurs.

Implementation

As previously indicated, one of the main responsibilities of the I.S. Manager will be to develop an implementation plan, to ensure compliance by Council. This plan will include issues such as acceptance testing and the update of our Disaster Recovery Plan. Council is still considering engaging Arthur Andersen in an audit role to overview the entire process. Quotations have been sought from Arthur Andersen to undertake this role.

As can be seen from this response, Council is taking the issue of the year 2000 very seriously. This includes allocating resources, both financial and physical, towards the project.

□ RESPONSE provided by Chief Executive Officer, Manningham City Council

With the exception of the omission of any reference to Council's Office Disaster Recovery Plan (published in October 1996), Council endorses the Auditor-General's Report and fully supports the recommendations made therein.

Council has identified the year 2000 Issue as a high priority and has made considerable progress in a short period of time, as evidenced by your very favourable Report.

Council is fully committed to its year 2000 Project.

The Project enjoys the complete support of Council, the Executive Management Team, I.T. Steering Committee and Audit Committee. Council has allocated sufficient resources, both human and financial, to ensure that its Year 2000 Project receives the high profile it deserves.

Council has every intention of ensuring that all year 2000 deadlines and commitments are accommodated within time and to budget.



❑ **RESPONSE** provided by Director of Administration, Southern Rural Water

SRW sees itself as unique in many ways in the context of the Report and as typifying many organisations, both public and private, whose capacity to deal with Y2K is limited and, therefore, whose ability to plan and prepare for Y2K is similarly restricted.

The Report focuses on 5 key factors in assessing the extent to which the surveyed organisations are adequately addressing Y2K. The following sections of this paper look at the findings, recommendations made and other comments relevant to SRW in respect of those 5 factors.

Awareness

The report notes that SRW has prepared a high level Y2K strategy but that “there has been no formal endorsement of the strategy”.

In this context, the statement “formal endorsement” requires definition, specifically by whom such endorsement should be made and what formal endorsement represents.

The Y2K project within SRW falls under the management responsibility of the Director Administration, who reports to the Chief Executive. The Y2K strategy and associated planning and activities are managed at that level. It has never been considered that any higher endorsement was needed, primarily due to the nature of the Y2K issue within SRW.

Unlike larger agencies and organisations SRW is effectively entirely dependent upon third party technology, whether computing hardware, software or other devices and resources. The strategy as such for SRW is therefore very simple; get confirmation from the third party supplier that the resource in question is Y2K compliant and then get them to prove it. Development and management of a strategy to do this at Director level has always been considered sufficient.

Similarly with external assistance; it is most unlikely that external experts could add greatly to the exercise for SRW. We obtained expert advice on how we should structure our program for Y2K compliance. Beyond that, there is very little of an “expert” nature that could be contributed to a program that is basically very simple.

The same arguments hold good for the propositions that executive co-ordination groups and project teams should be established to co-ordinated and perform specific tasks. These structures are only relevant to large organisations looking to upgrade in-house custom systems or to ensure the compliance of specially developed software unique to the organisation or its core business functions.

SRW is not such an organisation. It has 100 staff, one Technical Support person responsible for systems support, no in-house custom systems or large applications developed specially for it, and only one system developed specially for the industry sector, in which we are a minor partner and which will still be dependent upon third party suppliers to render compliant.

- **RESPONSE** provided by Director of Administration, Southern Rural Water
- continued

Assessment

While SRW has not developed contingency plans for critical systems and activities, it has considered the capacity for its current contingency plans to meet Y2K failures.

It is contended that it is impossible in practical terms to develop such contingency plans, to estimate the resource requirements of Y2K compliance, to document testing approaches and facilities or to develop logical testing approaches, when the core problem for the entity is to seek proof from third parties that supplied resources are or will be compliant. It is certainly not reasonable to spend time and money on investigating possible alternative systems solutions from other suppliers before knowing whether they will be needed (and, presumably, also with no greater guarantee that they, in their turn, will turn out to be compliant on the day).

Again, the problem with the comments and recommendations is that they focus on in-house programs of modification and not on the world of third party reassurance. So far as warranties and guarantees are concerned, this will in fact be the only assurance which SRW will receive from many suppliers. There is a marked reluctance to give even this at this stage, and there is likely to be a still greater unwillingness among third party vendors to develop and put to the test tools, routines or other mechanisms designed to prove compliance.

Indemnity is similarly a weak stick. In practical terms it is only as valuable as the asset and resource backing of the indemnifier. In all probability, the more likely tack for many small third party vendors will be a quiet exit from business prior to 1 January 2000 and a complete failure to address compliance as an issue, whether or not the resource in question is believed to be compliant or easily made so.

In the Y2K context, the capacity to test compliance is itself a problem both in regard to third party and in-house resources. It is predictable that even the most rigorous test program will miss some instances of non-compliance. The history of software development in particular is an excellent demonstrator of this assertion. If software development was a perfect process, then beta testing would not have been invented. That it is not is demonstrated by the existence of such test programs. It would be naive to assume that fixing such a complicated problem as Y2K would be any more universally successful than cutting original code.

So far as links to external systems are concerned, SRW has deliberately not wasted its time pursuing utility, banking and similar suppliers to seek assurances that their services can still be supplied or will still operate after 1/1/2000. Our status as a single customer is not going to influence their need and determination to solve their Y2K problems. They have their own overwhelming business imperatives to do so. Their success or failure will be societal in impact, not local.



- **RESPONSE** provided by Director of Administration, Southern Rural Water
- continued

Conversion and Verification

While the importance of testing is recognised, the capacity of small organisations such as ours to undertake testing of third party resources without provision of test tools by the third parties will, as already noted, be very limited. In-house development by an organisation such as ours of such tools is most unlikely.

It is clear from the examples given and evaluations made that this factor is again very focused on in-house systems and thus has limited relevance to SRW. It is worth noting, however, that;

- *SRW has in fact already replaced one significant business application (Microsoft Access v2.0) with a compliant replacement (Access v7). This involved testing of the later version to ensure compliance and then conversion of existing version 2 database into the new version; and*
- *SRW has identified and utilised a Y2K test tool (MLLCHK) to test compliance of all its personal computers. It already had in place a strategy for PC replacement which meant that basically only 2 representative machines needed to be tested. SRW is, however, confident that its PC hardware is Y2K compliant.*

Implementation

SRW considers that this section, like the previous 2, is very focused on the Y2K issue as it relates to in-house resources. SRW is also amused by the last statement in the Report which, in our opinion, both typifies the simplistic approach to Y2K which too many organisations and people are taking and highlights the real problem with Y2K.

With regard to the simplistic approach, we would be astonished if any organisation could state with confidence that it considered itself to be Y2K compliant today, unless it had begun operation with current (hopefully provably) compliant resources in the last 12 months. With regard to the real problem, it is that no organisation faced with proving Y2K compliance of its resources is really going to be able to confirm compliance until the functionality of the resource concerned has been proved in a genuine operational environment, post-1 January 2000.

- **RESPONSE** provided by Chief Executive Officer, Inner and Eastern Health Care Network

The Alfred Hospital has been undertaking an assessment of year 2000 exposure over the last 4 years. This has already resulted in 2 major initiatives to replace non-compliant information systems, incorporated within the PARIS and NxIS Projects, which have required a combined investment of approximately \$20 million. Under the umbrella of the Network Year 2000 Project, all areas of possible exposure across the Inner and Eastern Health Care Network continue to be under intense review, with the final assessment of exposure to be completed by 30 June 1998.

The Review by the Auditor General of Victoria was conducted in March 1998, and since that time the Network Year 2000 Project has significantly progressed at the Alfred Hospital.

□ **RESPONSE** provided by Chief Executive Officer, Inner and Eastern Health Care Network - continued

The Network Year 2000 Project has been divided into 2 major phases. Phase 1 - Assessment is the development of the Inventory lists, together with prioritisation of possible risk exposure and planning activities to ensure Year 2000 compliance. Phase 1 is to be completed by June 1998. Phase 2 - Compliance includes performing the year 2000 compliance testing, obtaining year 2000 compliance certificates from suppliers and updating contracts to include year 2000 compliance clauses covering liability. Phase 2 will be prioritised depending on the risk assessment, with critical exposures to be covered by December 1998 and all exposures to be dealt with by 30 June 1999.

A Network Year 2000 Project Quality Plan has been developed and implemented to define Project Overview, Project Scope, Project Organisation, Reporting Requirements, Roles and Responsibilities, Project Methodology, Project Plan, Change Control Process and Risk Management. I&EHCN Internal Auditors, Coopers & Lybrand, are monitoring and reporting year 2000 progress to the Board.

As part of the Phase 1 - Assessment, the Inner and Eastern Health Care Network, inclusive of the Alfred Hospital, has established a methodology for progressing the assessment phase and ensuring a consistent approach across all I&EHCN hospitals. As part of the Assessment, the year 2000 Inventory is identifying:

- computer hardware such as servers, network components;
- computer software, both major applications and department specific software;
- medical equipment with microchip processes that are date-dependent;
- interfaces to medical equipment, software and/or hardware;
- general infrastructure items such as lifts, phones, security systems;
- external suppliers whose inventory control systems are date dependent; and
- external suppliers who provide services that are date dependent.

Within Phase 2 – Compliance, testing of all equipment and software is a complex and time-consuming task, given the volume of items to be tested at each hospital. The hospitals are testing critical equipment and systems in conjunction with suppliers. The Department of Human Services is providing direct support to the I&EHCN to help overcome year 2000 risk exposures and is co-ordinating testing of common equipment and systems by the I&EHCN and other health care networks and rural health care facilities.

□ **RESPONSE** provided by Chief Executive Officer, State Trustees

Overall conclusion

- STL has an overall plan. Detailed plans will vary with the activity and will be written as required.
- STL has not identified the need for external resources. Some internal resources will inevitably be diverted to work on this issue.
- Contingency plans will be developed later based on a testing/evaluation giving us a better understanding of the risks.



□ **RESPONSE** provided by Chief Executive Officer, State Trustees - continued

Overall conclusion - continued

- We have not yet commenced testing apart from some PC testing as part of the evaluation of testing tools. We have converted our major system to a Year 2000 compliant base.
- We do not plan to outsource testing.
- State Trustees intends to prepare contingency plans for all foreseeable contingencies, including Year 2000 issues, as part of its Disaster Recovery Planning.

Awareness

- STL have subsequently evaluated the need for external assistance and at this stage do not believe it is necessary.
- STL have subsequently developed a high level document.
- The Executive Group now receives regular reporting. At this stage they have not been required to organise activities apart from the Executive Manager IT. As project manager he will co-ordinate their activities as necessary. The Managing Director has overall review of the project. Regular reporting now occurs at STL at Executive and Board level.
- A project team has worked on the Oracle upgrade, and technical teams are evaluating testing tools for the desktop and applications testing. Other teams will be formed as necessary.

Assessment

- Compliance has subsequently been formally defined.
- Impact from major system non-compliance has been assessed. Other impacts will be assessed when the risks and options are better understood.
- Inventories are almost completed.
- Detailed plans will be prepared for each activity. At this stage we are concentrating on preparing for the high risk/long lead time issues (testing the major application and the desktop).
- This will happen, initially for the above major activities. Planning for these in detail will not be possible until we have established methods and tools. This is currently under way for the desktop and just about to start for the application.
- Although there is some contingency for added contract expense in this year's budget and in next year's, this project is primarily to be resourced from existing budgets. This will inevitably divert resources from other projects. The organisation must successfully address its Year 2000 issues, but this must be done in the context of normal budgetary limitations.
- STL has written compliance /warranty statements from most of our major suppliers. We have not written to minor suppliers as yet.
- Legal advice is to be sought on STL's indemnification.

□ **RESPONSE** provided by Chief Executive Officer, State Trustees - continued

Assessment - continued

- *Identifying links and external dependencies is part of the inventory process. Discussions with the third parties is a high priority issue which will be commenced once the current priority projects have been organised.*

Conversion and Verification

- *All of the suggested requirements are standard practice.*
- *STL has substantially completed the conversion of a critical application - we have now completed the conversion of two major applications.*

Implementation

- *We will not be able to prepare implementation schedules until our evaluation is more advanced.*
- *The major database conversion is now completed.*
- *Acceptance testing excluding specific Year 2000 issues is now completed.*
- *STL will develop a DRP plan in conjunction with the establishment of its DRP/Year 2000 test facility. This will include contingency for Year 2000 specific issues.*
- *STL does intend to prepare contingency plans.*
- *STL's converted application and database is in production. This has not yet been tested for Year 2000 compliance.*

□ **RESPONSE** provided by Chief Executive Officer, Victorian Superannuation Board (VicSuper)

To date VicSuper's approach to the year 2000 issue has been to identify and commence treatment of the areas with the greatest potential exposure to the millennium bug. Accordingly, a number of steps have been taken by VicSuper to address the issue. In particular, an inventory of all software, hardware and non-IT components was taken and suppliers were requested to confirm their year 2000 compliance. Furthermore, the year 2000 issue was a major catalyst for the migration project which has been allocated extensive management effort and resources.

Having identified, addressed and implemented a project to address the key concerns in relation to the year 2000, a project team has been set up to now document and formalise VicSuper's approach to the year 2000. The team is currently undertaking a formal risk assessment with a view to preparing a high level strategy document and a series of detailed action plans. The project team reports fortnightly to the Executive Committee and a written report is provided monthly to the Board.



- **RESPONSE** provided by Chief Executive Officer, Victorian Superannuation Board (VicSuper) - continued

Awareness

All VicSuper staff are aware of the existence of a year 2000 project team. Regular staff forums will be held over the next 18 months to keep staff aware of emerging issues and the Board's progress with respect to the year 2000. Furthermore, due to the significance of the migration project all staff are acutely aware of its existence and necessity.

To ensure VicSuper is kept up-to-date project team members have attended (and will continue to attend) various year 2000 seminars. Further, team members are networking with personnel from other organisations (both public and private sector) to share ideas and solutions. Accordingly, the need for further external assistance will be reviewed as required.

Directors are kept informed of the Board's progress via monthly progress reports.

Assessment

As noted earlier, VicSuper's approach to date has been to identify and focus on the areas with the greatest potential exposure to the millennium bug. The risk assessment currently being undertaken by the project team will assist in allocating priorities for non critical systems. The Australian Standard HB104:1997 "A Guide to Year 2000 Compliance" is being applied for this purpose. All future work of the Project Team will be conducted by reference to this Standard.

Further, to ensure that VicSuper's compliance status is not compromised by future purchases of goods or services, a standard year 2000 compliance clause is to be inserted into all future purchase contracts.

Finally, with the exception of the migration project which has been budgeted for the 1997-98 and 1998-99 years, most Year 2000 expenditure will be incurred in the 1998-99 financial year and will be budgeted for accordingly.

Conversion and Verification

VicSuper supports audit's recommendations regarding the importance of a comprehensive test strategy. Accordingly, VicSuper has, and will continue to, place considerable emphasis on testing.

Implementation

As noted by audit, VicSuper is currently converting a non-compliant database to a compliant database as part of the migration project. The implementation schedule developed by VicSuper allows time for contingency planning and disaster recovery planning.

Conclusion

Management believe that the work undertaken by VicSuper to date, together with the work proposed for the next 2 years, will place VicSuper in a sound position with respect to the year 2000 bug.

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>
COMPLETED AUDITS				
Department of State Development	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	29 Aug. 1997	29 Aug. 1997
INDUSTRY, SCIENCE AND TECHNOLOGY				
Construction Industry Long Service Leave Board (a)	30 June 1997	" "	12 Aug. 1997	18 Aug. 1997
Construction Industry Long Service Leave Board (a)	Period 1 July 1997 to 30 Nov. 1997	31 Mar. <i>Financial Management Act 1994</i> , s.46.	7 April 1998	9 April 1998
Melbourne Convention and Exhibition Trust	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	29 Aug. 1997	11 Sept. 1997
Overseas Projects Corporation of Victoria Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.53A.	3 Oct. 1997	6 Oct. 1997
Victorian Medical Consortium Pty Ltd	30 June 1997	" "	7 Aug. 1997	7 Aug. 1997
MULTIMEDIA				
Film Victoria	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	18 Sept. 1997	19 Sept. 1997
State Film Centre of Victoria Council	30 June 1997	" "	18 Sept. 1997	19 Sept. 1997 (b)
SMALL BUSINESS				
Liquor Licensing Commission	30 June 1997	" "	4 Sept. 1997	12 Sept. 1997
SPORT				
Greyhound Racing Control Board	30 June 1997	" "	24 Sept. 1997	25 Sept. 1997
Harness Racing Board	30 June 1997	" "	30 Sept. 1997	3 Oct. 1997
Melbourne and Olympic Parks Trust	30 June 1997	" "	25 Feb. 1998	26 Feb. 1998
Melbourne Sports and Aquatic Centre Trust	30 June 1997	" "	28 Oct. 1997	28 Oct. 1997
Victorian Institute of Sport Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.53A.	26 Sept. 1997	10 Oct. 1997

SCHEDULE A
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>
COMPLETED AUDITS - <i>continued</i>				
<i>SPORT - continued</i>				
Victorian Institute of Sport Trust	30 June 1997	31 Oct. <i>Financial Management Act 1994, s.46.</i>	26 Sept. 1997	10 Oct. 1997
<i>TOURISM</i>				
Australian Grand Prix Corporation	30 June 1997	" "	29 July 1997	29 July 1997
Emerald Tourist Railway Board	30 June 1997	" "	20 Aug. 1997	23 Sept. 1997
Tourism Victoria	30 June 1997	" "	12 Aug. 1997	15 Aug. 1997

(a) Control and management of the fund transferred to the building industry.

(b) Qualified audit report issued.

Part 3.8

Treasury and Finance

KEY FINDINGS

Clearance of Yallourn Power Station site

- The potential cost to the State for the clearance of the Yallourn Power Station site is estimated at \$44.5 million, which represents an increase of \$5 million over the original estimate for this project.

Paras 3.8.39 to 3.8.40

- The overall cost to the State for the clearance of the Yallourn Power Station site may increase by an additional amount of up to \$25.9 million as a result of a statement of claim lodged by the original contractor which was subject to litigation in the Supreme Court. However, a counter claim amounting to \$10.8 million has been lodged against the contractor on behalf of the State.

Paras 3.8.39 to 3.8.40

Trends in performance of public sector superannuation funds

- The State's unfunded superannuation liabilities which totalled \$15.6 billion as at 30 June 1997 represent the largest component of the State's liabilities after State debt.

Paras 3.8.47 to 3.8.53

- All of the State's superannuation funds achieved high investment returns, a proportion of which was represented by unrealised gains, during the 1996-97 financial year, due to the strong equities and fixed interest securities markets.

Paras 3.8.54 to 3.8.60

- An important element of the Government superannuation reforms was the modification of benefits available to employees with the closure of defined benefits schemes to new entrants and the establishment of accumulation schemes.

Paras 3.8.63 to 3.8.67

- Notwithstanding the Government reforms, defined benefit schemes have been retained for operational emergency services employees, judges, senior law officers and parliamentarians.

Paras 3.8.63 to 3.8.67

KEY FINDINGS - continued

Trends in performance of public sector superannuation funds - continued

- While the Auditor-General has responsibility for auditing the water industry and municipal councils, and the Boards of the associated superannuation funds have responsibility for managing liabilities arising from defined benefit schemes with the ultimate risk resting with Victorian taxpayers, these funds should be subject to audit by the Auditor-General and remain subject to parliamentary scrutiny.

Paras 3.8.77 to 3.8.78

Local Authorities Superannuation Board unfunded superannuation liability

- While the Local Authorities Superannuation Board's (LASB) unfunded superannuation liability increased significantly during the 1995-96 financial year, the liability slightly declined during the 1996-97 financial year.

Paras 3.8.82 to 3.8.83

- The reduction in the LASB's liability during the 1996-97 financial year was substantially due to unusually high investment returns achieved during the year as a result of the favourable prevailing investment market with 55 per cent (\$121 million) of the return represented by unrealised gains at year end.

Para. 3.8.90

Financial standing of WorkCover

- The percentage of the WorkCover Scheme's net assets in relation to its outstanding claims liability has decreased from 102.9 per cent at 30 June 1995 to 92.4 per cent (deficit of \$292 million) at 31 December 1997.

Para. 3.8.95

- The key factors contributing to the reduced funding level of the WorkCover Scheme as at 31 December 1997 was a cumulative increase of \$1.2 billion, or 50 per cent, in the Scheme's outstanding claims liability since 30 June 1995 without the same corresponding increase in net assets.

Para. 3.8.96

- Based on projections by the Victorian WorkCover Authority's consulting actuaries, the Scheme will return to a fully funded position by 31 December 2000.

Para. 3.8.98

- Given the significant emerging claim cost pressures on the Scheme, the Authority needs to continue to closely monitor and manage the Scheme to ensure its financial viability.

Paras 3.8.101 to 3.8.106

Utilisation of government property

- While acknowledging that recent refurbishment and upgrading of certain city precinct properties have reduced the risk of short-term building deterioration and reduction of service potential, high priority should be given to the development of a costed and comprehensive longer-term preventative maintenance program for those State-owned properties which are to be retained.

Paras 3.8.119 to 3.8.123

KEY FINDINGS - *continued***Utilisation of government property** - *continued*

- In September 1995, it was estimated that rental savings arising from the implementation of the Government's City Precinct Strategic Plan would progressively increase to \$32 million per annum by the 1999-2000 financial year compared with 1992-93 financial year rental levels, but in July 1996 the rental savings target was revised to \$22 million per annum.
Paras 3.8.124 to 3.8.127
- The average space allocation per public servant remains excessive based on the target established by the Government.
Paras 3.8.128 to 3.8.131
- There has been a significant improvement in the level of dead rent which is estimated at \$6.8 million for the 18 month period to December 1997 compared with \$12 million for the same period to December 1995.
Paras 3.8.136 to 3.8.137

Victorian electricity industry privatisation

- PowerNet Victoria's revenues are substantially secured, with the company currently deriving in excess of 95 per cent of its total revenues from its regulated transmission business.
Paras 3.8.146 to 3.8.148
- The total proceeds of \$2.7 billion received from the sale of PowerNet Victoria compared favourably with valuations obtained prior to the sale and was \$1.2 billion in excess of the book value of the business.
Paras 3.8.159 to 3.8.161
- The State obtained total proceeds of \$400 million in relation to the sale of Southern Hydro Ltd which compared favourably with valuations obtained prior to the sale and was \$115 million in excess of the book value of the business.
Paras 3.8.182 to 3.8.184
- Total proceeds from the sale of all electricity businesses (including the present value of franchise, licence and lease fees receivable) were \$21.7 billion.
Paras 3.8.198 to 3.8.203
- It is estimated that the State will derive annual net savings of approximately \$760 million during the 1997-98 financial year from the electricity privatisation that has occurred to date.
Paras 3.8.204 to 3.8.206

Cost of Tricontinental failure

- The aggregate cost of Tricontinental to Victorian taxpayers as at 31 December 1997 totalled \$2.3 billion.
Paras 3.8.215 to 3.8.216
- The key residual activity of Tricontinental is the orderly realisation of the remaining loan and receivables portfolio which at 31 December 1997 had an estimated net realisable value of \$39 million.
Paras 3.8.217 to 3.8.219



3.8.1 The Treasurer and the Minister 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 1996-97 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>
Finance	Emergency Services Superannuation Board Hospitals Superannuation Board Local Authorities Superannuation Board Port of Geelong Authority Superannuation Fund (a) Regulator General, Office of the Victorian Superannuation Board, administering: <ul style="list-style-type: none"> • Coal Mine Workers' Pensions Fund • Parliamentary Contributory Superannuation Fund • State Superannuation Fund • Victorian Superannuation Fund Victorian WorkCover Authority Water Industry Superannuation Fund Water Industry Superannuation Fund Pty Ltd
Gaming	Tattersall Gaming Machine Division Tattersall Sweep Consultation Tattersall's Club Keno Victorian Casino and Gaming Authority
Treasurer	Aluminium Smelters of Victoria Pty Ltd and its 5 subsidiaries Australian Power Exchange Pty Ltd Chief Electrical Inspector, Office of the Ecogen Energy Ltd Electricity Services Victoria (b) Everton Dell Pty Ltd (c) Gas Transmission Corporation GASCOR Generation Victoria Melbourne Port Corporation National Power Exchange Pty Ltd Port of Geelong Authority Port of Melbourne Authority Port of Portland Authority PowerNet Victoria Quiet Life Ltd Rural Finance Corporation Securities Finance Corporation Ltd Southern Hydro Ltd (d) State Electricity Commission of Victoria State Trustees Ltd STL Financial Services Ltd The Albury Gas Company Ltd Transport Accident Commission and its 5 subsidiaries Treasury Corporation of Victoria

TABLE 3.8A
MINISTERIAL RESPONSIBILITY FOR
PUBLIC BODIES WITHIN THE TREASURY AND FINANCE SECTOR - continued

<i>Ministerial portfolio</i>	<i>Entities subject to audit</i>
Treasurer - cont.	Tricontinental Australia Ltd Tricontinental Corporations Ltd Tricontinental Holdings Ltd Twin Waters Resort Pty Ltd Vicfleet Pty Ltd Victorian Channel Authority Victorian Funds Management Corporation Victorian Managed Insurance Authority Victorian Power Exchange

- (a) Final audit - members' funds transferred to Victorian Superannuation Fund.
- (b) Final audit - entity dissolved July 1997.
- (c) Final audit - entity deregistered October 1997.
- (d) Sold to private sector entity as at 18 December 1997.

3.8.3 Comment on matters of significance arising from the audit of entities within the Treasury and Finance sector is provided below.

CLEARANCE OF YALLOURN POWER STATION SITE

3.8.4 The original Yallourn Power Station which is situated in the Latrobe Valley, 145 kilometres east of Melbourne, was progressively constructed over a 40 year period commencing in 1921. The complex, which was originally owned and operated by the State Electricity Commission of Victoria (SECV), comprised 5 individually designated power stations, known as A, B, C, D and E. The first power station commenced electricity generation in 1924 and the last in 1962. The combined power generating capacity of the complex was 621 megawatts.

3.8.5 From the mid-1960s, the importance of the Yallourn Power Station as the State's supplier of electricity declined as a result of the gradual commissioning of the Hazelwood Power Station between 1964 and 1971 and the Yallourn W Power Station in the 1974-75 and 1981-82 financial years. In addition, major technical problems, hazards associated with the levels of asbestos and the greater efficiencies of the other power stations had a negative impact on the economic viability of the Yallourn Power Station. Consequently, the individual power stations which made up the Yallourn complex were progressively decommissioned by the SECV, commencing with power stations A and B in the late 1960s and power stations C, D and E between 1984 and 1989.



View of the Yallourn Power Station clearance work.

3.8.6 As the date of preparation of this Report, the major structure of the Yallourn Power Station still remained substantially intact, with the generating plant of the power stations housed in a continuous turbine hall, which is abutted by the boiler houses for power stations C, D and E. The boilerhouses and associated power stations A and B were removed in the 1968-69 and 1976-77 financial years, respectively. The turbine plant of power station A was also removed in the 1968-69 financial year.

3.8.7 The site is particularly sensitive, both industrially and environmentally, as it is located near the Latrobe River and is in close proximity to the Yallourn W Power Station, which is owned and operated by Yallourn Energy Ltd, and major electricity switchyards controlled by GPU PowerNet and Eastern Energy Ltd. The power stations also straddle the water supply lines to Loy Yang Power Ltd from the Latrobe River. In addition, the Yallourn North township is located less than one kilometre from the power stations.

3.8.8 As early as 1989, the SECV identified the need to recognise the future cost of restoring the site of the power stations.

3.8.9 In June 1994, Generation Victoria, one of the entities created with the split-up of the SECV, approved the appointment of a contractor for the clearance of the power stations' site. The contract was formally entered into in February 1995 at which time responsibility for the project had passed to the SECV. However, the SECV subsequently terminated the contract as a result of a dispute arising between the parties and appointed a new contractor to finalise the required works. Audit has undertaken a review of the processes associated with the appointment of these contractors and the arrangements established for the clearance of this site.

Tendering, evaluation and selection process

3.8.10 A number of proposals were considered by the SECV in 1990 under a registration of interest process. Some of these proposals involved options for the redevelopment of the power stations but, at the time, projected power generation costs made the proposals uneconomical, and it was decided to delay a decision until future power requirements were clarified. In March 1994, this matter was re-assessed and it was concluded that a refiring option would remain uneconomical well into the future, during which time Generation Victoria would have to incur rising maintenance expenditure for an unused power station. Accordingly, it was decided that the Yallourn Power Station should be removed and Generation Victoria invited tenders for the clearing of the power stations' site.

3.8.11 The tender document advised the interested contractors that they were required to examine the site and its surroundings and that the price tendered was expected to cover the costs of complying with all the proposed obligations and all matters necessary for the proper performance and completion of the works. The interested tenderers were also advised that all bids would be evaluated using the following criteria:

- experience in the management of large-scale projects;
- experience in the removal of asbestos and other hazardous materials from major power plants;
- experience in the dismantling and clearing of large and heavy industrial facilities;
- financial capability; and
- an ability to formulate and implement a quality assurance program.

3.8.12 In April 1994, Generation Victoria received 11 tenders which were evaluated by an assessment team comprising of senior management employees of Generation Victoria. Shortly thereafter, the assessment team recommended the short-listing of 7 tender submissions for detailed evaluation as they provided substantially conforming tenders and were competitive in price.

3.8.13 Following a detailed assessment of the 7 short-listed tenderers by the assessment team and an evaluation by Generation Victoria's Tender Review Board of the team's recommendation, in June 1994 the Board determined that the tender from the consortium comprising the Australian Defence Industries Ltd (ADI), a company owned by the Commonwealth Government specialising in project management, and Bains Harding Ltd (Bains), a specialist insulation, cladding and asbestos removalist company, be accepted for the clearance of the site of the power stations.

3.8.14 Subsequently, consistent with the above recommendation, the ADI-Bains consortium was selected to undertake the required works by the Board of Directors of Generation Victoria.



3.8.15 The cost of works was estimated at \$33.3 million, which compared with a range of \$10.9 million to \$45.9 million for the other unsuccessful tenders. However, those tenders which were lower in price than the successful tenderer were deemed to be non-conforming bids. Table 3.8B summarises the main components and value of the works.

TABLE 3.8B
COMPOSITION AND VALUE OF WORKS
((\$million))

<i>Component</i>	<i>Amount</i>
Main lump sum	26.4
Expenditure under priced schedule of rates -	
Landscaping	1.8
Disposal of certain materials	0.1
Provisions -	
Disposal of certain materials	2.1
Contract variations	2.8
Additional insurance	0.1
Total	33.3

Source: Minutes of meeting of Board of Directors of Generation Victoria, June 1994.

3.8.16 The works were to commence in July 1994 for expected completion in December 1996. The total cost of this project was expected to be up to \$39.5 million, comprising:

- ADI-Bains contract of up to \$33.3 million;
- other contracts associated with the clearance of the site of \$3 million; and
- direct costs incurred by Generation Victoria of \$3.2 million.

3.8.17 Following extensive negotiations with the Heritage Council, in September 1994, it granted a conditional permit for the complex's demolition.

3.8.18 Subsequently, in January 1995 responsibility for the power stations' site together with contractual arrangements for the clearance of the complex were allocated to the SECV, in preparation of the privatisation of the brown-coal fired power stations in the Latrobe Valley.

3.8.19 The Administrator of the SECV entered into an agreement with the contractor in February 1995, which was principally the same contract approved by the Board of Generation Victoria for the **clearing of the site by a revised date of August 1997, for a lump sum price at \$26.7 million**, and a schedule of rates for the completion of other works, as directed by SECV's engineer.

Key terms and conditions of the arrangements

3.8.20 The terms and conditions for the clearing of the power stations' site were set out in the abovementioned agreement. Under this agreement, the scope of the works, which were to be completed by the contractor within a period of 30 months, included:

- the location, identification and quantification of all hazardous and benign materials;
- the removal and disposal of asbestos and other hazardous materials, clearing, removal and disposal of all plant, structures, buildings, debris and materials of the power stations including associated coal handling plant at the periphery of the Yallourn Open Cut mine and other miscellaneous buildings;
- management and operation of the Yallourn North asbestos and hard rubbish dumps, which are owned by Yallourn Energy Ltd and were not available for use by the public;
- an investigation into the condition of water conduits which are currently in service and supply "low quality" water to the pumps housed in the turbine hall for Loy Yang Power Ltd; and
- site rehabilitation activities.

3.8.21 The agreement provided for the contractor to submit invoices to the SECV on a monthly basis for works performed, however, prior to payment the SECV's engineer, who had wide discretionary powers, was responsible for the certification of the value of the work referred to in the invoices, the payment due to the contractor and the nomination of amounts to remain unpaid. Other key rights and obligations of the contractor under the agreement included:

- The contractor was expected to comply with the requirements of the contract. However, if the contractor encountered physical conditions which could not have been reasonably anticipated by a contractor experienced and competent in carrying out work of the type to which the contract related, excluding the consequences of weather conditions or the activities of labour, and they differed materially from those conditions at the date of the agreement, the contractor was required to provide the SECV's engineer with notice of such conditions including the estimated cost of the measures necessary to address the conditions. The engineer would then investigate the matter and decide if any variation was required;
- The contractor was able to lodge a notice of claim to the SECV for the payment of additional funds arising out of work performed under the contract, an extension of time, a change in a direction issued by the engineer or amendments to the terms and conditions of the agreement. Any such claims lodged with the SECV would be assessed and where applicable the engineer would issue a notice of rejection or a modification order; and
- Where the contractor failed to carry out the works by the completion date, then the contractor was required to pay to the SECV liquidated damages for every day which elapsed from the completion date. The rate of liquidated damages was \$2 000 per day up to an aggregate of \$730 000.



3.8.22 Under the agreement, the SECV also retained certain key rights and obligations, including:

- The SECV could suspend payment to the contractor, suspend the works, apply a security deposit supplied by the contractor or occupy the works or any part thereof prior to the practical completion of the works where the contractor caused the realisation of one of the following key events:
 - failure to commence the work within the time set out in the contract or to order materials or plant in a reasonable time;
 - assignment of part of the contract without the approval of the SECV;
 - works not carried out in accordance with the contract program or the quality assurance program;
 - removal of material or plant from the site without the approval of the SECV;
 - failure to rectify work when required to do so by the SECV;
 - refusal to comply with a direction of the SECV;
 - failure to complete the work or any part of the work by the completion date;
 - failure to perform, fulfil or observe any obligations under the contract; or
 - the contractor becomes insolvent or bankrupt.
- Any suspension would continue until the contractor remedied the default. Furthermore, the SECV was entitled to complete the work without payment or compensation to the contractor and take possession of the contractor's plant and equipment on the site. If the cost of works performed by the SECV exceeded the cost that would have been payable to the contractor then the difference between the 2 amounts would have been deducted from any funds which may have been owed to the contractor.
- If the SECV decided to suspend the works for reasons other than the contractor's default or omission, the SECV would have been required to pay all reasonable costs to the contractor arising from a suspension; and
- The agreement could have been terminated by the SECV at any time and for any reason, by giving written notice of such termination to the contractor. However, the contractor would receive a payment for works performed to the date of termination and compensation for any reasonable losses and expenses, incurred as a consequence of the termination of the contract.

Termination of original contract

3.8.23 Although the contractor commenced works on the site in March 1995, by early 1996, it became apparent to the SECV that the contractor was not meeting the approved contract program and hence discussions between the parties were held to attempt to rectify the situation.

3.8.24 In November 1996, the contractor provided a memorandum of dispute to the SECV which included claims totalling \$68 million representing the contractor's estimated cost to complete the works, off-site overheads and profit calculated at a rate of 27 per cent of the estimated cost of the works. The memorandum also claimed that:

- the contractor encountered physical conditions or obstructions on the site which were considered to have differed materially from those which would have been ascertainable or anticipated at the date of the contract;
- certain works which were required by the SECV and its project engineer were outside the scope of works under the agreement;
- the SECV and its project engineer failed or refused to provide adequate information in respect of the site; and
- the SECV failed to ensure that its project engineer administered the agreement reasonably or fairly.

3.8.25 The SECV rejected the above claims and in December 1996, the contractor lodged a statement of claim which was subsequently discontinued. In February 1997 the contractor lodged a statement of claim totalling \$67 million against the SECV in the Supreme Court of Victoria.

3.8.26 Following a request from the SECV for the preparation of a recovery program setting out a sequence of events for the completion of the outstanding works, in March 1997 the contractor advised the SECV that the approved contract program was out of date and not relevant to the work on the project, and a recovery program was not possible at that stage. In addition, the contractor stated that the time for completion of the works was no longer enforceable and that the contractor's obligation was therefore to complete the works within a reasonable time.

3.8.27 In May 1997, the contractor lodged an amended statement of claim in the Supreme Court against the SECV. In the statement of claim, the contractor advised that:

- as only 42 per cent of the total works had been completed, it would take a further 30 months to November 1999 to complete the works; and
- the changed nature of the works required by the SECV would necessitate a cost of \$70.5 million compared with the original contract sum of \$26.7 million.

3.8.28 Shortly thereafter, the Administrator determined to terminate the contract and to establish tender arrangements for the selection of another contractor to complete the remainder of the works as soon as possible.

3.8.29 At that time, the Administrator considered that although the contract was required to be completed within 30 months, the contractor was 12 months behind schedule with significant cost over-runs and the contractor had commenced court proceedings against the SECV for claims now totalling \$77 million. The increase in the value of claims lodged by the contractor reflected revisions to the statement of claim. Subsequently, the SECV issued a notice of termination to the contractor.

3.8.30 As a result of the termination of the contract, in December 1997 the contractor lodged an amended statement of claim against the SECV reducing the



contractors claim to \$25.9 million, representing the alleged value of the works executed to the date of termination of the contract and the alleged reasonable losses and expenses incurred as a result of the termination.

3.8.31 The SECV denied any liability for such claims and, in March 1998, the SECV lodged a counter-claim totalling \$10.8 million against the contractor for the cost of completing the site clearance, including costs associated with the preparation of a new tender.

New arrangements for the completion of the works

3.8.32 Following the termination of the above contract and the desire by the SECV to complete the demolition of the power stations, in July 1997 the Administrator approved a selective tendering process for the appointment of a new contractor to complete the site clearance of the power stations. Under the approved procedure, consultants engaged by the SECV approached 13 contractors from whom registrations of interest were sought. These contractors were deemed to have the requisite skills and financial capacity to undertake the works and were drawn with reference to the following:

- companies recommended by the Demolition Contractors Association of Victoria;
- entities which tendered for the original works;
- companies recommended by Pacific Power, a generation entity owned by the Government of New South Wales, who had experience in the demolition of power stations; and
- organisations which made inquiries since the termination of the agreement with the previous contractor.

3.8.33 The Treasurer of Victoria approved the above strategy but required a public advertisement calling for registration of interests for the site clearance. Following the public advertisement, interested parties received a registration of interest brief which outlined the key selection criteria which would be used to evaluate tender submissions, which included:

- the organisation's financial, human and physical resources;
- technical and management capacity;
- proposed methodology for the conduct of works;
- relevant experience and record of performance;
- ability to obtain adequate insurance;
- quality assurance proposal; and
- proposed sub-contractors and suppliers.

3.8.34 Following the assessment of registrations of interest received from the interested contractors, the SECV short-listed 7 potential tenderers which fulfilled the above criteria and forwarded to them an invitation to tender document.

3.8.35 During the tendering process, 2 parties withdrew from the process, and 2 tenderers submitted a joint bid. Following an assessment of the 4 tenders, the



consultants recommended that the contract be awarded to Vac-Tech Group Pty Ltd, at a cost of \$21.1 million.

Terms and conditions of new agreement

3.8.36 In February 1998, the Administrator announced that the contract for the clearance of the site would be awarded to Vac-Tech Group Pty Ltd which engaged Guilfoyle Wreckers Pty Ltd as its sub-contractor.

3.8.37 The contract for the clearance works was for a firm lump sum of \$21.1 million and included a firm schedule of rates for works which may be carried out on the direction of SECV's engineer, which is in addition to the works included in the lump sum price. The scope of the works under the new contract generally matched the scope of the balance of the works remaining to be completed from the previous contract and included certain site rehabilitation works which would have been carried out under the schedules of rates in the original contract.

3.8.38 The terms and conditions of the agreement entered into between the SECV and the new contractor are broadly similar to the previous terminated agreement. The key rights and obligations of the parties which differ from the terms and conditions of the original agreement are as follows:

- The works to be completed by February 2000 and if the works continue after that date, the contractor will incur a daily charge of \$2 000, up to a maximum of \$730 000; and
- The SECV has at its own expense arranged for insurance against all loss or damage to the works and all of the SECV's plant and materials provided to the contractor. In addition, the SECV has obtained legal liability insurance, including asbestos liability in respect of any damage to, or loss of, any property other than the works, and any injury or death suffered by any person associated with the works. This insurance will also provide cover to the contractor's liability for all omissions or defects which are due to any cause including materials, workmanship or design and for any loss of, or damage to, the works for a period of 12 months from the date of practical completion, subject to the stated conditions and exclusions of the policies.

Overall cost to the State

3.8.39 Table 3.8C outlines the key components of the projected overall cost to the State of the Yallourn Power Station site clearance.

TABLE 3.8C
PROJECTED COST OF SITE CLEARANCE, AT FEBRUARY 1998
 (\$million)

<i>Item</i>	<i>Amount</i>	
Original arrangements -		
Payments to contractor	13.8	
Legal expenses	2.1	
Payments to other contractors	2.2	
Miscellaneous expenses	3.0	21.1
New contract -		
Payments to be made under new contract	21.1	
Miscellaneous expenses	2.3	23.4
Total (a) (b)		44.5

- (a) In December 1997 the original contractor lodged an amended statement of claim against the SECV for \$25.9 million, representing the alleged value of the works executed to the date of termination of the contract and the alleged reasonable losses and expenses incurred as a result of the termination.
- (b) In March 1998 the SECV lodged a counter-claim with a total of \$10.8 million against the original contractor for the cost of completing the site clearance, including costs associated for the preparation of the new tender.

3.8.40 As indicated in the above table, the projected cost for the clearance of the Yallourn Power Station site is estimated at \$44.5 million, which represents an increase of \$5 million over the original estimate for this project. Given that a statement of claim has been lodged by the original contractor, the overall cost to the State may increase by an additional amount of up to \$25.9 million, but this claim has not been accepted by the SECV and was subject to litigation in the Supreme Court. Furthermore, the SECV has lodged a counter-claim totalling \$10.8 million against the original contractor for the cost of completing the site clearance, including costs associated with the preparation of a new tender.

RESPONSE provided by Deputy of the Administrator of the SECVS

In view of the current legal proceedings, the SECV does not wish to make any formal comment.

TRENDS IN PERFORMANCE OF PUBLIC SECTOR SUPER FUNDS

3.8.41 In my 1992 *Report on Ministerial Portfolios*, I commented on the operations and financial position of public sector superannuation schemes as at 30 June 1991. At that time, there were 95 separate public sector superannuation funds and superannuation arrangements in Victoria, providing lump sum payments, pensions and disability payments to employees of State Government departments and public bodies. The number of public sector superannuation funds has subsequently been reduced to 14 as at 30 June 1997, with the key remaining funds being:

- Victorian Superannuation Fund (VSF);
- State Superannuation Fund (SSF);
- Parliamentary Contributory Superannuation Fund (PCSF);
- Emergency Services Superannuation Scheme (ESSS);
- Hospitals Superannuation Board (HSB);
- Water Industry Superannuation Fund (WISF); and
- Local Authorities Superannuation Board (LASB).

3.8.42 Given the significant developments impacting on public sector superannuation schemes since 1992, audit undertook a review of the operation and performance of these schemes with particular emphasis on:

- government reforms to the Victorian public sector superannuation industry since 1992;
- level of unfunded superannuation liabilities;
- investment performance;
- administration costs;
- benefits paid; and
- prudential and regulatory framework.

Profile of public sector superannuation schemes

3.8.43 Table 3.8D outlines the membership, investments managed and the accrued superannuation benefits of key public sector superannuation schemes as at 30 June 1991 and 30 June 1997.

TABLE 3.8D
PROFILE OF MAJOR PUBLIC SECTOR SUPERANNUATION SCHEMES,
30 JUNE 1991 AND 30 JUNE 1997

Scheme	No. of members		Total investments		Liability for accrued benefits	
	30 June 1991	30 June 1997	30 June 1991	30 June 1997	30 June 1991	30 June 1997
	(no.)	(no.)	(\$m)	(\$m)	(\$m)	(\$m)
City of Melbourne Superannuation Fund (a)	3 000	-	69	-	88	-
Emergency Services Superannuation Scheme	14 000	21 310	440	1 888	1 113	2 687
Gas and Fuel Superannuation Fund (b)	6 000	-	355	-	276	-
Hospitals Superannuation Board	135 000	165 828	436	1 459	801	1 610
Local Authorities Superannuation Board	35 000	71 113	1 032	1 223	1 300	1 152
Metropolitan Fire Brigades Superannuation Fund (c)	409	-	29	-	109	-
Water Industry Superannuation Fund	6 315	2 657	223	166	291	175
MTA Superannuation Fund (d)	1 000	-	1	-	5	-
Parliamentary Contributory Superannuation Fund	221	244	64	121	77	120
SEC Superannuation Fund (e)	17 000	-	1 267	-	1 442	-
State Casual Employees Superannuation Fund (f)	60 000	-	10	-	23	-
State Employees Retirement Benefits Fund (g)	11 000	-	107	-	388	-
State Superannuation Fund	131 000	193 466	1 395	3 683	16 741	18 232
Transport Superannuation Fund (g)	16 000	-	69	-	258	-
Victorian Superannuation Fund (h)	-	84 153	-	441	-	438
Total	435 945	538 771	5 497	8 981	22 912	24 414

(a) On 31 October 1995, the Fund ceased to exist and all members of that Fund were transferred to the LASB.

(b) On 1 July 1996, the Fund ceased to exist when all members were transferred to the Victorian Electricity Industry Superannuation Scheme.

(c) Fund was merged with the ESSS on 1 January 1992.

(d) On 30 June 1994, the Fund ceased to exist and all members were transferred to the Transport Superannuation Fund.

(e) On 1 July 1996, the Fund was renamed the Victorian Electricity Industry Superannuation Fund which is now a private sector fund.

(f) Fund ceased to exist on 31 March 1996 with the members' assets and liabilities transferred to the VSF.

(g) Fund ceased to exist on 31 May 1996 with the members' assets and liabilities transferred to the SSF.

(h) Fund is an accumulation-based superannuation fund which was opened to members on 1 January 1994.

Source: Annual reports of above entities.

3.8.44 The increase in member numbers since 30 June 1991 of around 103 000 is mainly attributed to the introduction of accumulation-based superannuation schemes opened to new members on 1 January 1994, in particular the Victorian Superannuation Fund. These schemes were established to conform with Commonwealth superannuation guarantee legislation which requires superannuation to be provided for all staff including part-time and casual employees.

Government reform of the public sector superannuation industry

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3.8.45 Over recent years, the major focus of Government reforms has been to manage the growth in the unfunded liabilities of public sector superannuation schemes. The Victorian Commission of Audit in its Report of May 1993, made a number of key recommendations including:

- the Government should aim to eliminate the existing unfunded liabilities over the next 40 years by making additional specific contributions from the Consolidated Fund;
- existing defined benefit schemes should be closed to new members who should be provided with superannuation guarantee contribution legislation benefits as a minimum; and
- departments should meet the employer share of future benefits as they accrue, with these costs being reflected in program costs.

3.8.46 Following consideration of the above recommendations, the Government has undertaken significant superannuation reforms over recent years including:

- ***Closure of defined benefit schemes and establishment of accumulation plans*** - All defined benefit schemes were closed to new employees from 1 January 1994, except for schemes involving the judiciary, parliamentarians and operational emergency services employees. Since 1 January 1994, all other new employees have been required to join relevant accumulation plans. Typically, the defined benefit schemes offer greater member benefits than the accumulation plans and therefore are more expensive for the employer to provide, particularly if funded only on the retirement of the employee. As a result of the reform, the Government's effective employer superannuation contribution in respect of new employees, decreased from between 10 per cent and 22 per cent of salaries for existing employees to the legislative minimum of 6 per cent;
- ***Contributions to reduce unfunded superannuation liabilities*** - In the 1993-94 financial year, the Government made a one-off payment of \$1.4 billion from the Consolidated Fund to reduce its liability to the SSF. In particular, this payment extinguished the liability that had arisen from a practice adopted by previous governments of requiring superannuation schemes to initially meet the employer share of lump sum payments to retiring employees, with progressive reimbursement provided from the Consolidated Fund to the schemes, as if these benefits were being paid in the form of pensions. In addition, further payments have been made from the Consolidated Fund since the 1993-94 financial year to assist in reducing the level of the State's unfunded superannuation liabilities for all defined benefits superannuation schemes; and



- The introduction of new funding methods for employer agencies - Until 1994, government departments were not responsible for meeting the cost of superannuation obligations to the respective superannuation funds as this was met from the Consolidated Fund and was based on actual benefits paid. However, as from 1994 departments were given the responsibility for making the required superannuation payments to the accumulation schemes. Since November 1995, employer contributions for accruing superannuation benefits of employees in defined benefit schemes have been paid by employer agencies on a regular basis directly to the SSF. One major by-product of this change has been the improvement in the integrity of member data provided by departments to the SSF.

In addition, since 1 November 1995 contributions towards the unfunded liabilities have been made from the Consolidated Fund based on a determination made by the Minister for Finance, on the advice of the actuary, which is subject to the approval of the Treasurer.

While the overall method of calculating and paying employer contributions has changed, the actual level of employer funding on an annual basis has not substantially altered.

- **Disability benefit management** - Revised disability claims management procedures were introduced in 1992 by all Victorian public sector superannuation schemes which encouraged members to remain in the workforce (where possible) rather than to seek disability retirement. These procedures resulted in a once-off reduction in accrued member benefit liabilities due to lower projected rates of disability retirement assumed by the actuary. The impact of this reform on accrued benefits in relation to the SSF was estimated savings of between \$800 million and \$900 million; and
- **Rationalisation of superannuation schemes** - As mentioned previously, the number of major funds and superannuation arrangements has reduced from 95 in 1992 to 14 in 1997 via the merger and wind-up of superannuation funds.

Unfunded superannuation liability

3.8.47 The State's unfunded superannuation liabilities which totalled \$15.6 billion as at 30 June 1997 represent the largest component of the State's liabilities after State debt. Unfunded superannuation liabilities have arisen as a result of current and previous Government decisions to meet the employer cost of superannuation entitlements at the time the employee retired or became eligible for the benefit rather than as benefits accrued over the working lives of employees. These financial obligations comprise employer superannuation contributions yet to be paid by the Government to superannuation schemes in respect of services previously provided by employees.

3.8.48 Table 3.8E provides details of the aggregate superannuation liabilities and the unfunded component of these liabilities for the major public sector superannuation schemes as at 30 June 1997.

TABLE 3.8E
UNFUNDED SUPERANNUATION LIABILITIES, 30 JUNE 1997

<i>Scheme</i>	<i>Liability for accrued benefits</i>	<i>Net assets available to pay benefits</i>	<i>Unfunded liability</i>	<i>Percentage of net assets to liability for accrued benefit</i>
	(\$m)	(\$m)	(\$m)	(%)
Budget sector -				
State Superannuation Fund	18 232	3 727	14 505	20.4
Emergency Services Superannuation Scheme	2 687	1 793	894	66.6
Hospitals Superannuation Board Parliamentary Contributory Superannuation Fund	1 610	1 425	185	88.5
Victorian Superannuation Fund	120	122	(2)	101.7
	438	438	-	100
	23 087	7 505	15 582	32.5
Non-budget sector -				
Water Industry Superannuation Fund	175	164	11	93.4
Local government -				
Local Authorities Superannuation Board	1 152	1 147	5	99.6
Total	24 414	8 816	15 598	36.11

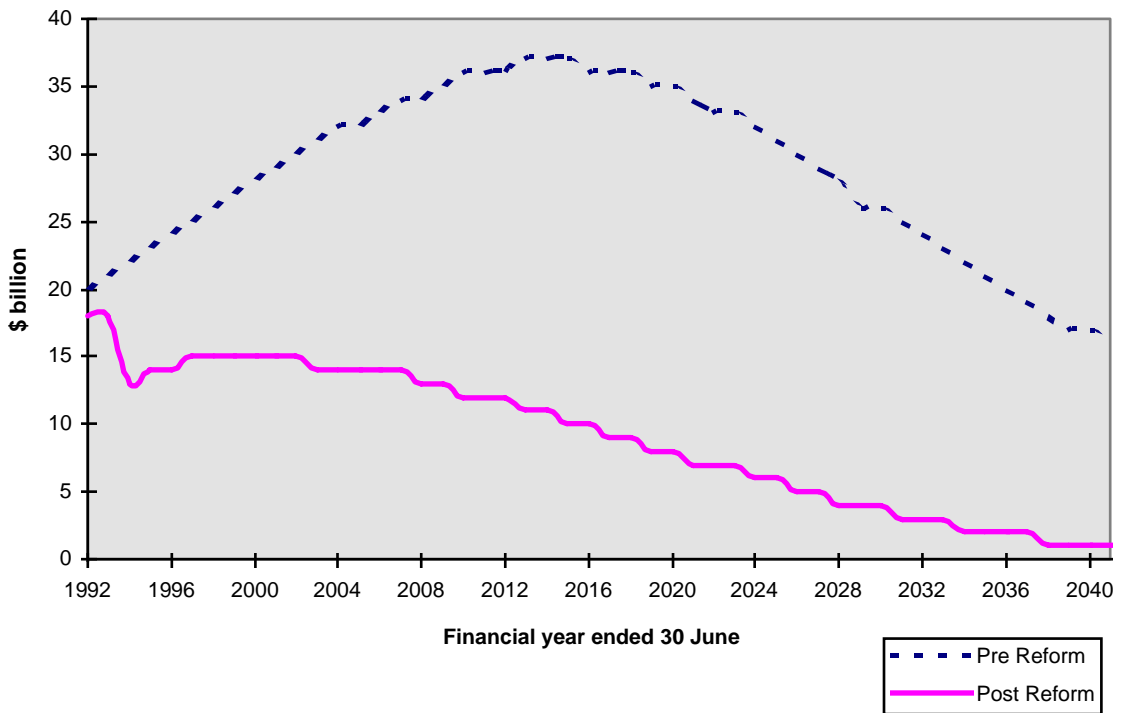
Source: Annual Reports of above entities.

3.8.49 The above table indicates that the largest component of the State's unfunded superannuation liability resides with the SSF. This Fund, which is the largest and oldest Victorian public sector superannuation scheme, accounts for 93 per cent of the State's total unfunded liability as at 30 June 1997. The level of solvency which represents the net assets of the Fund compared with the liability for accrued benefits is considered unsatisfactory. The actuary identified a shortfall of approximately \$1 200 million in the level of assets held by the Fund relating to the residual value of accumulated member contributions for former contributory members who are now pensioners. The actuarial investigation as at 30 June 1994 recommended funding targets be introduced which gradually improved the solvency position over the next 30 or 40 years. The actuary indicated that, if the recommended contributions targets are made to the SSF, the ratio of the assets to accrued benefit liabilities is expected to increase to approximately 27 per cent as at 30 June 2003 and to 40 per cent by approximately 2020. However, the VSB has been assured by the Minister for Finance that the Government will continue to meet its share (employer share) of the unfunded liability of the SSF.

3.8.50 It needs to be recognised that the LASB's unfunded superannuation liability at 30 June 1997 was substantially eliminated as a result of the liability being allocated to the participating employers. Further comment on this issue is included elsewhere in this Report.

3.8.51 Chart 3.8F shows the change in the projected unfunded superannuation liability measured in real dollars for the SSF, following the implementation of the government reforms as previously mentioned. The chart identifies that despite the government reforms, the level of unfunded superannuation liabilities, measured in real terms (1997 dollars) is only expected to decline marginally over the next 5 years. However, after that period, the level of unfunded liabilities is expected to reduce more significantly as the number of beneficiaries decline in the defined benefit schemes.

CHART 3.8F
IMPACT OF REFORMS ON SSF PROJECTED UNFUNDED LIABILITY (REAL DOLLARS)
 (\$billion)



Source: Data provided by Towers Perrin.

3.8.52 The primary reason for the projected long-term reduction in the level of unfunded superannuation liabilities has been the closure of the defined benefits pension scheme in 1988 and the closure of the lump sum scheme in 1993.

3.8.53 The unfunded liability of the SSF has decreased from \$16 471 million at 30 June 1992 (the figure has been adjusted to include the unfunded superannuation liabilities of the former Transport and State Employee Retirement Benefits Scheme) to \$14 505 million at 30 June 1997. The key factors for the decrease in the unfunded liability are:

- the Government’s one-off payment of \$1.4 billion to SSF in 1993-94;
- the transfer in June 1994 of 2 619 pensioners from SSF to ESSS, which resulted in \$552 million in unfunded liabilities being shifted from SSF to ESSS;

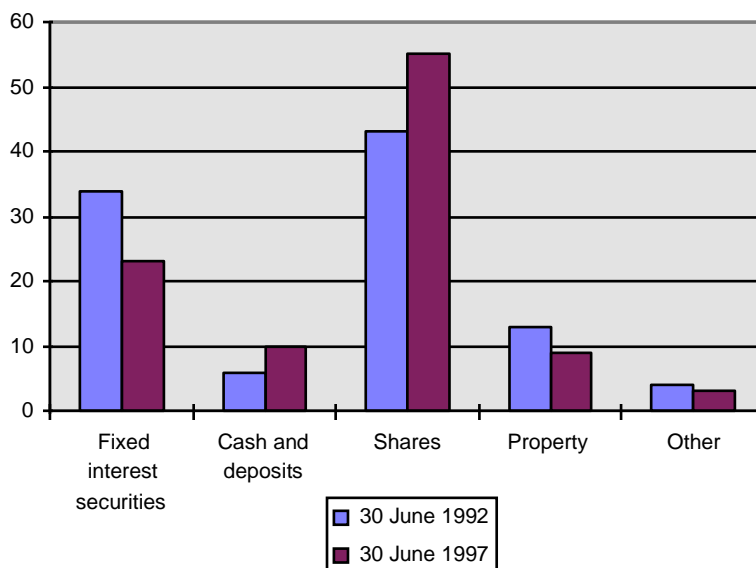
- the changes to calculations of defined benefit entitlements from 1 January 1994 to be based on employee average salary over the last 2 years of service, instead of being based on final salary, and additional reductions due to the changes in death and disability benefits which resulted in savings to SSF to the value of \$521 million;
- the voluntary transfer of 18 240 members (approximately 32 per cent of the revised scheme members) from the revised scheme to the new scheme, which had the one-off impact of reducing the unfunded liability by \$226 million;
- the achievement of a rate of investment return greater than projected by the actuary over recent years;
- the reduction in the level of general administration costs;
- the commencement, in June 1995, of benefits paid from a taxed source which provided an estimated savings to the Fund of \$300 million in present value terms; and
- reduction in the public sector workforce since 1992 and the payment to the members exiting the workforce of resignation superannuation benefits.

Investment performance

3.8.54 As at 30 June 1997 the major public sector superannuation schemes held investments with an aggregate value of around \$9 billion. These investments were managed by a combination of internal resources and external fund managers appointed by individual schemes to handle specific segments of the investment portfolio.

3.8.55 To optimise returns and minimise investment risk, superannuation funds hold diversified investment portfolios, with investments comprising a mixture of short-term deposits, fixed interest securities, property, mortgages and equities, both in Australia and overseas. The investment portfolios should be structured in line with the risk profile of the superannuation scheme as reflected through expected maturity dates of liabilities to members. Chart 3.8G shows the allocation of public sector superannuation schemes investment between classes of investment as at 30 June 1992 and 30 June 1997.

CHART 3.8G
INVESTMENT HOLDINGS BY CLASS,
30 JUNE 1992 AND 30 JUNE 1997
 (per cent)



3.8.56 The chart shows that since 1992 trustees of public sector superannuation funds have increased the allocation of investment funds towards Australian and overseas shares and have reduced the investment holdings in fixed interest securities and property. Members and beneficiaries have benefited from this investment strategy as the equities market over recent years has produced good investment returns, especially for the 12 months ended 30 June 1997.

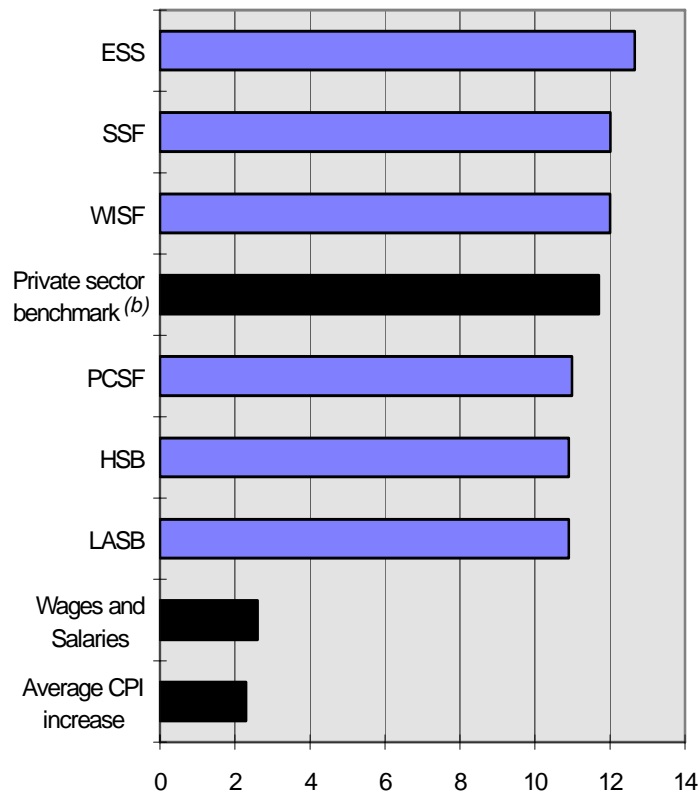
3.8.57 In assessing the investment performance of public sector superannuation funds, it is important to recognise that the performance of individual funds is dependent on trustee decisions relating to investment strategies based on the profile of the superannuation liabilities payable to members and the risk profile that a fund is willing to accept.

3.8.58 The audit review assessed the investment performance of the major Victorian public sector superannuation funds with reference to the following benchmarks:

- annualised investment return, after taking account of tax and management fees, over a rolling 5 year period, compared with the asset weighted average return for average volatility funds achieved by the superannuation pooled investment funds in Australia; and
- annualised investment return, after taking account of tax and management fees, over a rolling 5 year period in comparison with movements in the consumer price index and movements in the level of average wages and salaries.

3.8.59 Chart 3.8H depicts the investment performance of public sector superannuation schemes over the 5 year period to 30 June 1997, compared with the previously mentioned benchmarks.

CHART 3.8H
ANNUALISED NET RETURN ON INVESTMENTS OF MAJOR SUPERANNUATION FUNDS
FOR THE 5 YEAR PERIOD TO 30 JUNE 1997 (a)



(a) The VSF has not been included as the Fund has been in operation for only 4 years and the Fund offers its members choice of investment strategy to suit their risk and return preferences.

(b) Represents the asset weighted average return for average volatility funds as contained within Towers Perrin Superannuation Pooled Funds survey.

Source: The above net figures provided by respective superannuation schemes.

3.8.60 The chart shows that the investment returns achieved by the SSF, WISF and ESSS have been greater than that achieved by the private sector Australian superannuation pooled investment funds while the remaining public sector superannuation schemes have achieved a net investment return close to the private sector average. All funds achieved high returns during the 1996-1997 financial year due to the strong equities and fixed interest securities markets. However, it should be recognised that a proportion of investment returns was represented by unrealised gains at year-end.

Administration cost of the schemes

3.8.61 Since my May 1992 *Report on Ministerial Portfolios*, the average administrative costs of all schemes, that is, **the cost to operate the funds excluding investment and taxation expenses, has substantially reduced from an average of \$92 per member in the 1991-92 financial year to \$48 per member in the 1996-97 financial year.** This reduction is partly due to the amalgamation of superannuation funds which has led to a larger membership base for each fund and therefore the achievement of economies of scale. Table 3.8I outlines the administration costs, including actuarial and legal expenses, for the major public sector schemes for the year ended 30 June 1997.

TABLE 3.8I
ADMINISTRATION COST OF SUPERANNUATION FUNDS, 30 JUNE 1997

<i>Scheme</i>	<i>Administration resourcing</i>	<i>No. of members</i>	<i>Administra- tion cost</i>	<i>Average annual cost per member</i>
			(\$'000)	(\$)
Emergency Services Superannuation Fund	In-house	21 310	1 592	75
Hospitals Superannuation Fund	In-house	165 828	6 991	42
Local Authorities Superannuation Board	In-house	71 113	3 891	55
Parliamentary Contributory Superannuation Fund (a)	Outsourced	244	338	1 385
State Superannuation Fund	In-house	193 466	10 401	54
Victorian Super Fund	In-house	84 153	2 300	27
Water Industry Superannuation Fund (b)	Outsourced	2 657	583	219
Total		538 771	26 096	48

(a) Actuarial and legal services provided by the private sector with member benefits and accounting services undertaken by Victorian Superannuation Board.

(b) Fund administration undertaken by a private sector superannuation administrator.

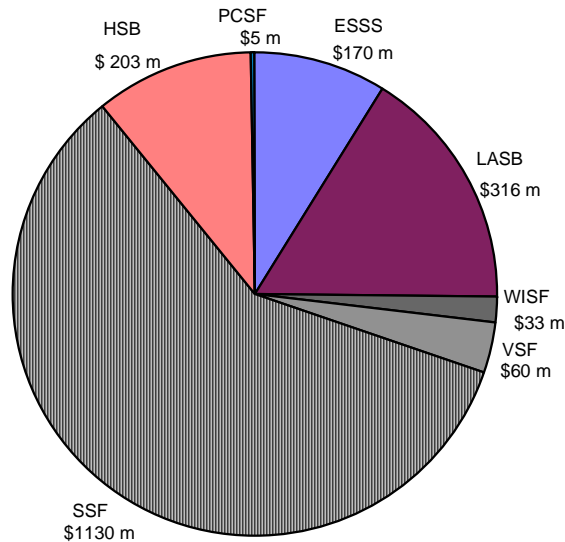
3.8.62 In analysing variations between schemes in administrative costs per member, it should be recognised that differences in the structure of the schemes, mix of the scheme's membership between pensioners and contributors, and the range of services offered to members significantly effect this ratio. Therefore, care should be taken when comparing these ratios between schemes.

Level of superannuation benefits paid

3.8.63 Public sector superannuation schemes provide a range of benefits to members and beneficiaries which become payable as a result of age retirement, retrenchment, resignation, disability, ill health and death. Benefits are payable in the form of pensions and lump sum payments, or a combination of both.

3.8.64 Total benefits paid by the major Victorian public sector superannuation schemes during the 1996-97 financial year were in the vicinity of \$1.9 billion and are depicted in Chart 3.8J.

CHART 3.8J
SUPERANNUATION SCHEME BENEFITS PAID
FOR YEAR ENDED 30 JUNE 1997
 (\$millions)



Source: Annual reports of above entities.

3.8.65 An important element of the government superannuation reforms, as mentioned previously in this Report, was the modifications of benefits available to members of public sector defined benefit schemes. These revisions included:

- Defined benefit entitlements to be based on employee average salary over the last 2 years of service, instead of final salary;
- Future member benefits to be adjusted so that the taxation costs are borne from members' funds and not by the Government. The impact of this change is that members' accrued benefits are reduced in gross terms but not in net terms, i.e. after taking account of taxation; and
- Member contributions to the State Superannuation Revised Scheme to be increased.

3.8.66 With the closure of defined benefits schemes to new entrants and the establishment of accumulation schemes, the public sector superannuation benefit entitlements to new members are broadly consistent with retirement benefits provided by the private sector to non-executive staff.



3.8.67 Notwithstanding these reforms, defined benefit schemes have been retained for operational emergency services employees, judges, senior law officers and parliamentarians. Benefits payable to these members are summarised below:

- The ESSS provides operational emergency services employees with access to member contribution rates ranging up to 8 per cent. The average member contribution rate is 5.5 per cent resulting in the accruing of benefits at the average rate of 22 per cent of final average salary per annum. The maximum lump sum benefit of 8.4 times of final average salary is achieved after approximately 35 years service;
- Judges who retire after age 60, having completed 10 year's service, are entitled to an indexed pension of 60 per cent of salary for the remainder of their life and a pension to their spouse on the member's death. The judges make no contributions, so their benefits are met entirely by the Government; and
- Parliamentarians are generally eligible to a pension after 8 years of service, with the value of the pension commencing between 36 per cent and 50 per cent of back-bencher's salaries. In the first 8 years of service, Parliamentarians are entitled to a reduced lump sum benefit equivalent to a multiple of their contributions. Where a pension entitlement arises, the pension amount normally increases at a rate of 2.5 per cent of basic salary for each year after 8 years of service to a maximum of 75 per cent of back-benchers' salaries. An additional pension amount is payable where a Parliamentarian has held a position of office.

A reduction of benefits occurred in 1993 as a result, in part, of the Fund paying benefits from a taxed source to compensate for the taxation payable on the Government's contributions. However, benefit entitlements increased in 1996 for new Members of Parliament, and for current Members who elect to transfer, with the introduction of a new scheme that was similar to the Commonwealth Parliamentarian's superannuation scheme.

The legislative changes made in 1996 also provided for Parliamentarians to cease contributing to the Fund once they had completed 20.5 years of membership and where benefits had stopped accruing. Since July 1996, all new members (and some current members who elect to transfer their membership) will have their benefit entitlements calculated under the terms and conditions similar to those set down in the Commonwealth Parliamentarian Superannuation Act 1948. As the Parliamentary Superannuation Fund pays benefits from a taxed source, the benefits payable to some members of the Fund will be greater than those payable under the Commonwealth Parliamentarian Superannuation Act 1948.

Prudential and regulatory framework

3.8.68 The *Borrowing and Investment Powers Act 1987* and the Investment Management Guidelines were introduced by the Government to establish a consistent management framework for public sector superannuation funds and public bodies with significant investment portfolios and long-term liabilities. To enhance the management framework in relation to these bodies, in December 1994, the Department of Treasury and Finance issued the *Prudential Statement - Victorian Public Sector Investments*, which replaced the previous Investment Management Guidelines and established a revised framework for the prudential supervision of these investment activities.

3.8.69 The December 1994 Prudential Statement was updated and replaced in June 1997 to incorporate the Insurance and Superannuation Commission's (ISC) guidelines for *Risk Management Statements for Superannuation Entities Investing in Derivatives*. The purpose of the Prudential Statement is to ensure that investments are prudently and responsibly managed, that the relevant bodies have access to a wide range of investment products and that maximum advantage is taken of available returns within acceptable risk parameters.

3.8.70 Broadly, the Statement requires superannuation funds to:

- Observe maximum exposure, asset and currency limits relating to investment portfolio composition;
- Set financial and investment objectives which form the basis for the establishment of investment strategies and establish risk and return targets;
- Prepare long-term investment strategies consistent with the financial and investment objectives adopted;
- Establish appropriate internal controls for the management of the key risks, and policy and procedures manuals to ensure the effective implementation of the investment objectives and strategies;
- Regularly report to the Treasurer to provide assurance that the investment portfolios are prudently and professionally managed. These reports include details of the investment objectives and strategies (including progress on their implementation), risk management statements for the use of derivatives, quarterly statistical reports on monthly returns and annual board of management certifications of compliance with the Statement; and
- Provide independent assurance to the Treasurer as to the compliance by major superannuation funds subject to these requirements. The Treasurer is provided with an annual report from the external auditor or an agent appointed by the Treasurer to ensure that the funds are complying with the prudential statement. Over recent years, the Victorian Financial Institutions Commission has been responsible for ensuring that the funds comply with the Prudential Statement.

3.8.71 These initiatives have been effective in establishing a management framework for the prudential supervision of public sector superannuation fund investment activities. Given the pending abolition of the Victorian Financial Institutions Commission, there will be a need to determine how the prudential compliance reviews will be conducted in the future.



3.8.72 In May 1996, the State and Commonwealth Government signed a Heads of Government Agreement relating to certain public sector superannuation schemes exempted from the Commonwealth *Superannuation Industry (Supervision) Act* 1993 (SIS).

3.8.73 Pursuant to section 45(6) of SIS, the following Victorian public sector superannuation schemes are exempt and thus are deemed to be complying funds for taxation purposes and are therefore eligible to be taxed at the concessional rate of 15 per cent:

- State Superannuation Fund;
- Victorian Superannuation Fund;
- Parliamentary Contributory Superannuation Fund;
- Emergency Service Superannuation Schemes;
- Local Authorities Superannuation Board; and
- Hospitals Superannuation Board.

3.8.74 Under the Agreement, the Insurance and Superannuation Commission relinquished responsibility for the regulatory control of the above State superannuation schemes with the regulatory responsibility now vested in the State Government under the Agreement.

3.8.75 While the State Government is required to ensure that the governing legislation of these schemes is consistent with the principles of SIS, a formal regulatory framework has yet to be established by the Department of Treasury and Finance.

3.8.76 **To ensure compliance with the State’s commitment under the Heads of Government Agreement, a formal regulatory framework needs to be established which, inter alia:**

- ensures that the governing rules of each of the abovementioned schemes are consistent with the principles of SIS as reflected in the agreement;
- establishes a mechanism for reporting compliance with the Agreement by the trustees; and
- appoints an independent party to assess whether the framework is appropriate and is operating effectively.

3.8.77 Over recent years, action has been taken or commenced to place certain superannuation funds, such as WISF and LASB, under the Commonwealth SIS legislation and remove myself as auditor of these Funds. I have advised the respective boards of these Funds, together with the Department of Treasury and Finance, that my authority to undertake the audit of such Funds is derived from the *Audit Act* 1994 and not from the above stated legislation.

3.8.78 I am of the view that while I have responsibility for auditing the water industry and municipal councils, and the Boards of the associated superannuation funds have responsibility for managing liabilities arising from defined benefit schemes with the ultimate risk resting with Victorian taxpayers, the Funds should be subject to audit by the Auditor-General and remain subject to parliamentary and public scrutiny. Accordingly, it would be of concern if the Auditor-General as Parliament's auditor, is removed as auditor of the Funds.

□ **RESPONSE** provided by Assistant Director, Superannuation, Department of Treasury and Finance

It is pleasing to note the Auditor-General's recognition of the State's substantial reforms in superannuation over the past 6 years. While the Department supports the majority of his comments, the following issues have been identified for response.

In relation to the solvency level of the State Superannuation Fund (SSF), as noted by the Auditor-General, the State Government has been receiving actuarial advice since 1 November 1995 on the amount of contributions it must make to the SSF in respect of its unfunded liabilities. Based on this actuarial advice, the State Government is continuing to meet the employer cost of superannuation entitlements as benefits are paid. The Auditor-General's concern regarding the solvency level of the SSF is not justified in the context of the assurance given by the Minister for Finance that the Government will continue to meet its share of the unfunded liability.

In referring to the chart on the impact of reforms on SSF projected unfunded liability, the Auditor-General states that "despite the Government's reforms, the level of unfunded superannuation liabilities, measured in real terms (1997 dollars) is only expected to decline marginally over the next 5 years". Surprisingly, the Auditor-General fails to highlight to Parliament the most important message of that chart, which is the immense reduction in unfunded liabilities already achieved by the reforms. For example, it is projected that had our reforms not taken place, unfunded liabilities would have peaked at approximately \$37 billion in real terms by 2013. As a result of the State's reform, unfunded liabilities have already peaked in real terms at around \$15 billion. Clearly, this reduction in State liabilities represents a substantial benefit to all Victorians.

Investment performance

It is important trustees take a long-term view in managing their investment portfolios. The primary aim of superannuation fund's investment strategy is to achieve a set of long-term (i.e. 10 years) financial and investment objectives which are, so far as it is possible, consistent with its liability profile. The risk tolerance of the trustees and the risk and return trade-off are important factors in determining the structure of the investment portfolio.

The statement "Members and beneficiaries have benefited from this investment strategy as the equities market over recent years has produced good investment returns, especially for the 12 months ended 30 June 1997" could be interpreted as implying that superannuation funds should be monitored on a short-term basis, i.e. 12 months, by reference to short-term market outcomes. This can lead to "short-termism" and can result in funds moving away from their long-term investment strategies as fluctuations occur in the financial markets. The real benefits to members and beneficiaries will only materialise over the long-term and on the basis a superannuation fund's can consistently achieve its long-term investment objectives.

- **RESPONSE** provided by Assistant Director, Superannuation, Department of Treasury and Finance - continued

Investment performance - continued

Ideally, the performance of superannuation funds should be measured over the longer-term, 3 years and 5 years against their long-term investment objectives. On a short-term basis (e.g. monthly, quarterly and annually), it is important to monitor to ensure that the funds and/or fund managers are complying with the long-term investment strategy and individual fund managers are meeting their market benchmarks and are complying with their mandated investment style.

In looking at the return performance across different funds, it is important to take into account both net and gross returns. Gross returns take out the effect of varying taxation rates and fund management fees providing a consistent comparison of returns across the funds.

Concerning the Parliamentary Superannuation Fund benefits, the Auditor-General states that benefits payable to some members of the Parliamentary Superannuation Fund will be greater than those payable under the Commonwealth Parliamentary Superannuation Act 1948. It should be noted that this anomaly is not a result of the Fund's benefit design, but the application of the Commonwealth's taxation laws.

Prudential and regulatory framework

At present, the Treasurer is not receiving a report from the external auditor of the fund or an agent appointed by the Treasurer that the fund is complying with the Prudential Statement. As an interim step, however, the Victorian Financial Institutions Commission (VicFIC) is reviewing the internal controls of the bodies subject to the Prudential Statement. Consideration is being given to whether or not ongoing external supervision of the type currently referred to in the Prudential Statement should be implemented. The Treasurer, however, has been receiving and will continue to receive quarterly and annual certifications from the Boards as to their compliance with the Prudential Statement and investment powers.

The Auditor-General's comments and recommendations concerning the Heads of Government Agreement do not take into account the Department of Treasury and Finance's previous advice that there is a specific provision contained within the Heads of Government Agreement (HOGA) which sets out how compliance is to be monitored by the States and the Commonwealth. The provision states that "The State and Territories agree to facilitate the exchange of information with the Insurance and Superannuation Commissioner to enable the Agreement to be monitored. The Commonwealth, States and Territories further agree that this exchange of information with the Commissioner will be the mechanism by which the Agreement is to be monitored". Contrary to the Auditor-General's perception, the State is already abiding by this framework.

As also previously advised to the Auditor-General, the Trustees of the State's public sector superannuation funds are statutory authorities that operate independently of Government. As the Trustees are not a party to the HOGA, they have no obligation to report their compliance with that Agreement. This is not a concern, however, as their governing legislation, which is subject to regular review by the Department of Treasury and Finance, already requires that they comply in all material respects with the principals contained in the HOGA.



□ *RESPONSE* provided by Assistant Director, Superannuation, Department of Treasury and Finance - continued

Prudential and regulatory framework - continued

In relation to the audits of the Water Industry Superannuation Fund (WISF) and Local Authorities Superannuation Fund (LASF), once these funds made a valid election to become regulated under the Commonwealth's Superannuation Industry (Supervision) legislation (SIS), the State could no longer supervise their operations. Among other things, this means that the State can no longer legislate to ensure that the WISF and LASF are audited exclusively by the Auditor-General. Under SIS, it is their responsibility of the Trustees of these funds to appoint an approved auditor to conduct their financial audits. SIS permits the Auditor-General to tender for these audits.



**LOCAL AUTHORITIES SUPERANNUATION BOARD
UNFUNDED SUPERANNUATION LIABILITIES**

3.8.79 The Local Authorities Superannuation Board provides superannuation services to Victorian local government entities, non-metropolitan water bodies and cemetery trusts. My May 1997 *Report on Ministerial Portfolios* outlined the causes for a 51 per cent increase during the 1995-96 financial year in the level of the Board's unfunded superannuation liabilities relating to the defined benefit scheme which stood at \$329 million at 30 June 1996. In particular, it was identified that the key factor that affected the funding position of the scheme was the greater than forecast number of retrenchments within the local government sector during the latter part of 1995 and in 1996.

3.8.80 During June 1997, the Government considered a series of recommendations, as to the proposed methods of funding the liability, made by a consultant it appointed to investigate the accuracy of the scheme's unfunded liability and the suitability of the Board's proposed measures to improve the scheme's solvency position. Subsequently in that month, the Acting Minister for Finance, in accordance with section 7(4) of the *Local Authorities Superannuation Act 1988*, requested the Board to consider a Statement of Government Policy in relation to the elimination of the scheme's unfunded liability, under which it was proposed that the Board:

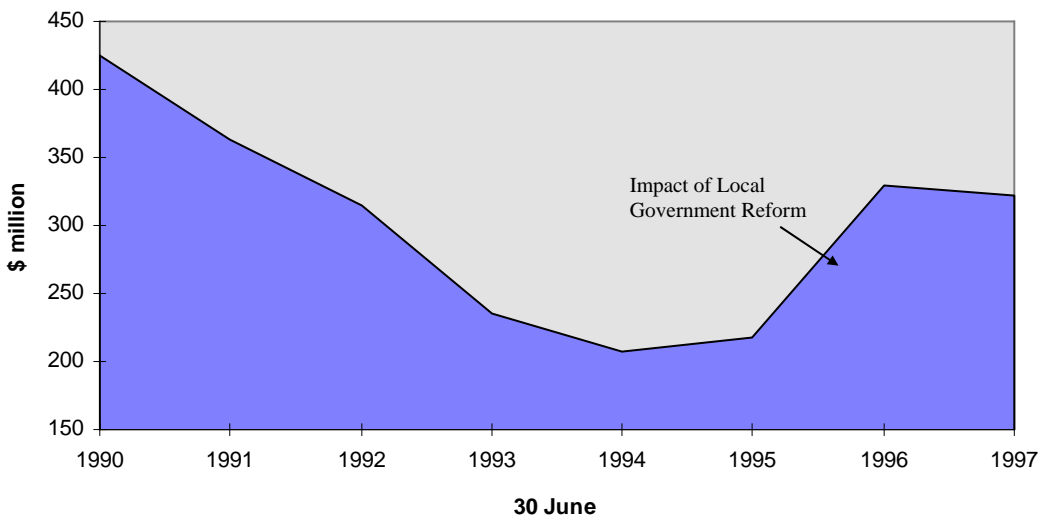
- Continue to require employers to fund the accruing superannuation costs at the rate of 9.25 per cent of employee salaries;
- Remove the existing 4 per cent surcharge on active employee salaries which had been previously established to meet the unfunded liability;
- Apportion the unfunded liability as at 30 June 1997 to each local government entity based on their share of the liability as at 30 June 1993, adjusted for any amounts subsequently paid into the scheme to address the unfunded liability and any additional costs of individual employers associated with employee retrenchments;
- Establish a recommended horizon of 10 years for the elimination of the unfunded superannuation liability, but any local government entity could choose to extend the horizon to 15 years in the event that the additional annual repayments exceeded 3 per cent of rate income. However, any local government entity could elect to exceed the 15 year horizon by confining repayments to 3 per cent of its rate revenue;
- Make each local government entity responsible for any increase in the liability arising from retrenchment benefits paid to its employees as from July 1997 (referred to as the retrenchment increment), with the resulting increase in the liability payable over the period up to 2007; and
- Seek immediate payment of any retrenchment increment incurred after June 2007, at the time of the retrenchment.

3.8.81 On 27 June 1997, the Board resolved to adopt, with certain minor modifications, the Statement of Government Policy effective from July 1997 and to apply it uniformly to all participating employers.

Financial position of Scheme

3.8.82 The annual report of the Board for the year ended 30 June 1997 disclosed an actuarially-determined unfunded superannuation liability of \$321 million for the defined benefits scheme, excluding the Scheme's liability of \$53 million relating to Commonwealth Government tax on superannuation contributions. Since the previous year, the unfunded superannuation liability decreased by approximately \$8 million. Chart 3.8K shows the movement in the Board's unfunded liability for the defined benefits scheme since 30 June 1990.

**CHART 3.8K
LASB DEFINED BENEFITS SCHEME
UNFUNDED SUPERANNUATION LIABILITY,
30 JUNE 1990 TO 30 JUNE 1997
(\$million)**



3.8.83 While the Board's unfunded superannuation liability increased significantly during the 1995-96 financial year, the liability slightly declined during the 1996-97 financial year, mainly as a result of:

- the achievement of a high rate of return on investments for the year (21 per cent), representing the highest annual return on investments recorded in the history of the scheme; and
- a significant reduction in the number of retrenchments within the local government sector during the year.



3.8.84 As indicated previously, the Board determined that the unfunded liability at 30 June 1997 was to be progressively funded by participating employers. In addition, the liability was allocated to current participating employers on the basis that they have become the successors in law and have assumed the respective liabilities relating to bodies that existed at June 1993 which was prior to the amalgamations of councils.

3.8.85 In particular, following the restructuring of the local government sector, council numbers declined from 210 to 78. Subsequent to the restructure, a number of councils entered into settlement agreements with neighbouring municipalities to address the consequences of changes in council boundaries, which resulted in the transfer of certain assets, liabilities and employees between these entities. However, at that time, the responsibility for the unfunded superannuation liabilities in respect of employees transferred between councils was not included in these agreements and accordingly were not transferred. It has only been since late 1997 that councils commenced negotiating with neighbouring municipalities to determine their respective share of the unfunded superannuation liabilities.

3.8.86 Similarly, the water industry has been reformed which resulted in a reduction in the number of non-metropolitan water boards from 108 to 37 entities, and the transfer of responsibility for the provision of water services from councils to the relevant bodies within the water sector. Due to the considerable changes brought about by local government restructuring, difficulties were encountered by the Board in accurately apportioning the unfunded superannuation liabilities to the respective water bodies. Consequently, the Board requested water bodies affected by the re-organisation of the industry to provide a list of employees transferred from councils to the water bodies, including the dates of transfer, in order to accurately determine the unfunded superannuation liability of each respective water body. At the date of preparation of this Report, 4 rural water bodies in consultation with the Board were still in the process of determining their share of unfunded liabilities.

3.8.87 The allocation of unfunded liabilities to individual employers is dependent on the accuracy of the Board's membership records. The audit review determined that the maintenance of the Board's records had been adversely impacted by the restructuring of the aforementioned sectors as a result of the Board not pro-actively seeking advice from participating employers as to movements of employees arising from restructuring. In October 1997, the Board advised participating authorities that the apportionment of the unfunded superannuation liabilities would be based on notification from those entities of transferred employees and their transfer date.

3.8.88 **The integrity of the Board's member records is critical, given their impact on the actuarial calculation of the liability for accrued benefits and its ultimate recovery from responsible participating employers. It is imperative that reconciliations of the Board's records to employer payroll records be performed on an ongoing basis.**

Employer responsibility for unfunded superannuation liabilities

3.8.89 The allocation of the unfunded superannuation liability for the defined benefits scheme which totalled \$321 million as at 30 June 1997 to participating employers does not remove their responsibility to compensate the scheme for any future adverse movements in this liability.

3.8.90 In this regard, the Board and participating employers need to be cognisant that the reduction of the liability during the 1996-97 financial year was substantially due to unusually high investment return achieved during the year as a result of the favourable prevailing investment market. In particular, it should be noted that 55 per cent (\$121 million) of the 1996-97 investment return was represented by unrealised gains at year-end, representing the movement in the market value of investments held at 30 June 1997, since the previous year or their date of purchase if acquired during the year. In the event that the market value of investment holdings declines over subsequent years, then the value of the unfunded superannuation liability is likely to be adversely impacted.

3.8.91 During the 1997-98 financial year, a number of participating employers determined to fund their share of the outstanding liability as at 30 June 1997 by way of a lump sum payment. Nevertheless, these employers will retain the obligation to meet any additional liabilities resulting from the future experience of the scheme, particularly where the retrenchment experience and the investment returns of the scheme adversely vary from actuarial projections. However, if the future experience of the scheme is more favourable than projected, the employers will be entitled to a reduction in their ongoing contributions in the scheme.

3.8.92 In this context, since the 1997 actuarial review of the scheme, the Board has implemented an ongoing monitoring process to identify unusual trends in the scheme. **The introduction of this arrangement as from the December 1997 quarter has enhanced the Board's capacity to monitor the financial position of the scheme on a retrospective basis. However, there remains a need for the Board to implement a pro-active strategy to anticipate unfavourable movements in retrenchments which may occur as a consequence of future competitive tendering within participating employers.**

□ *RESPONSE provided by President, Local Authorities Superannuation Board*

The observations about the importance of investment performance are most valid. However, the Board has been concerned to ensure that employers also understand the importance of other interacting financial and demographic factors which will impact on the future performance of the fund, particularly inflation, salary growth and benefit claims experience.

Notwithstanding that the new funding arrangements have limited the financial impact of future retrenchments, certain related financial risks remain for the fund and these were taken into account when the Board considered the Statement of Government Policy.



□ **RESPONSE** provided by President, Local Authorities Superannuation Board
- continued

The Board adopted a 10 year employer retrenchment increment financing period, “... on the basis that the Board will invoke an earlier repayment date in the event that it considers it prudent to do so in light of the financial impact that future retrenchments are having on the fund”.

In respect to other matters raised in the Report, I advise that it was the completeness and accuracy of the Board’s records which enabled the new funding arrangements to be implemented. The municipal boundary agreements were few in number and should be viewed in the context of the exceptional circumstances of the local government reform process.

Furthermore, the difficulties in apportioning unfunded liabilities to the water industry are a reflection of complex historical employment and administrative arrangements between councils and non-metropolitan water bodies, rather than any deficiency in the Board’s record keeping processes.



FINANCIAL STANDING OF WORKCOVER

3.8.93 My May 1997 *Report on Ministerial Portfolios* commented on the financial standing of the WorkCover scheme which is administered by the Victorian WorkCover Authority. In that Report, it was identified that the Government’s key financial objective to maintain the scheme’s full-funding position had been met for the previous 2 financial years. This Report provides an update of the financial position of the WorkCover scheme.

3.8.94 While the Government’s key financial objective to maintain the WorkCover scheme in a fully-funded position had been achieved in the past years, the financial position had deteriorated as at 31 December 1997 with the scheme no longer being fully-funded.

3.8.95 Table 3.8L highlights the financial position of the scheme for the period 30 June 1995 to 31 December 1997. **In particular, the table shows that the percentage of the scheme’s net assets in relation to its outstanding claims liability has decreased from 102.9 per cent at 30 June 1995 to 92.4 per cent at 31 December 1997.**

TABLE 3.8L
FINANCIAL POSITION OF THE WORKCOVER SCHEME,
30 JUNE 1995 TO 31 DECEMBER 1997
 (\$million)

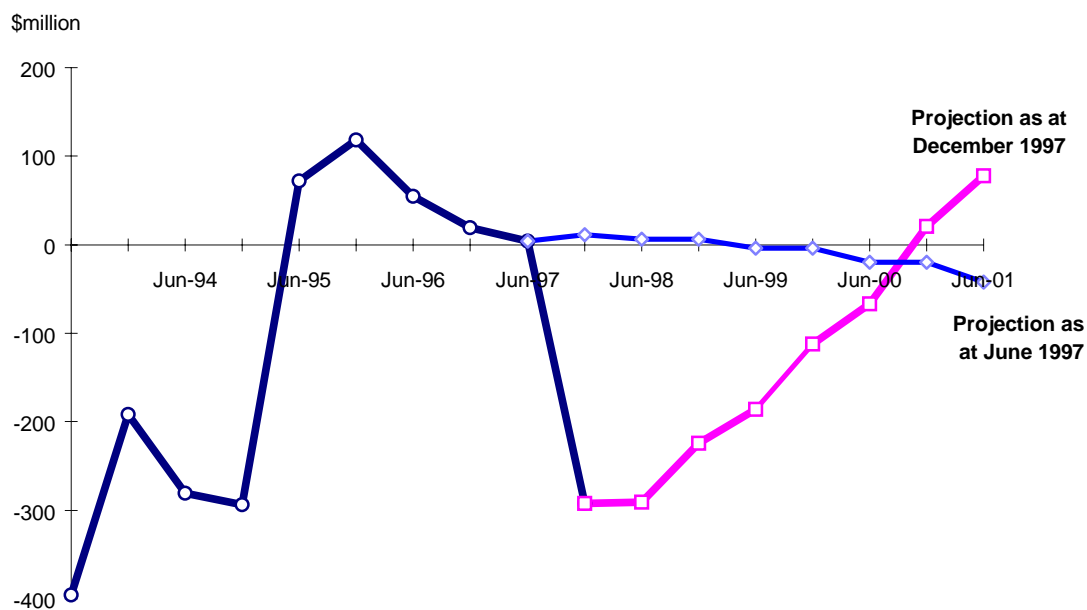
	30 June 1995	30 June 1996	31 Dec. 1996	30 June 1997	31 Dec. 1997
Outstanding claims liability(a)	2 486	2 876	3 127	3 445	3 727
Net assets	2 558	2 931	3 146	3 449	3 445
Surplus assets / (Deficiency)	72	55	19	4	(292)
Funding level (per cent)	102.9	101.9	100.6	100.1	92.4

(a) Represents net present value.

3.8.96 The key factor contributing to the reduced funding level of the WorkCover scheme as at 31 December 1997 was a cumulative increase of \$1.2 billion, or 50 per cent in the Authority’s outstanding claims liability since 30 June 1995 without the same corresponding increase in the Scheme’s net assets. The majority of the increase in the Authority’s outstanding claims liability was not projected and was mainly caused by the cost of common law claims previously incurred being higher than originally projected and an increase in the value of those claims incurred over the last 12 months.

3.8.97 The increase in the outstanding claims liability of the WorkCover scheme has in turn placed substantial pressure on the Authority to maintain its full funding position. Chart 3.8M shows the scheme’s funding position since June 1993 and the Authority’s actuarial projections of the funding position of the scheme to June 2001.

CHART 3.8M
WORKCOVER SCHEME'S FUNDING POSITION FROM JUNE 1993 TO DECEMBER 1997,
AND ACTUARIAL PROJECTIONS TO JUNE 2001
 (\$million)



Source: Victorian WorkCover Authority financial statements and consulting actuary reports.

3.8.98 The chart highlights that the scheme's financial position substantially improved from a deficit of \$396 million (82 per cent funding level) in June 1993 to a surplus of \$118 million (104 per cent funding level) in December 1995, with the position stabilising at around a 100 per cent funding level from June 1996 to June 1997, but returning to a deficit of \$292 million (92.4 per cent funding level) in December 1997. However, the chart also shows that, **based on projections provided by the Authority's consulting actuaries, taking account of the November 1997 legislative changes and utilising current claimant information, the scheme will return to a fully-funded position by 31 December 2000.** The projected turnaround in the deficit assumes an increase in average premium rates to counter-balance the increasing costs of claims.

3.8.99 For the 2 year period to June 1997, the scheme's fully-funded position was maintained mainly due to the impact of the following factors which were outlined in my May 1997 *Report on Ministerial Portfolios*:

- legislative reforms in December 1996 which, inter alia, removed the eligibility of injured workers to claim for secondary psychological impairment as a component of serious injury, thereby reducing the outstanding claims liability estimate;
- transfer to the scheme of \$320 million from the Supplementation and Guarantee Insurance Funds;
- favourable investment performance by the Authority over the period; and
- earlier settlement of claims.

3.8.100 While in June 1997, the Authority's consulting actuary projected that the scheme would remain in a fully-funded position, the following major factors were



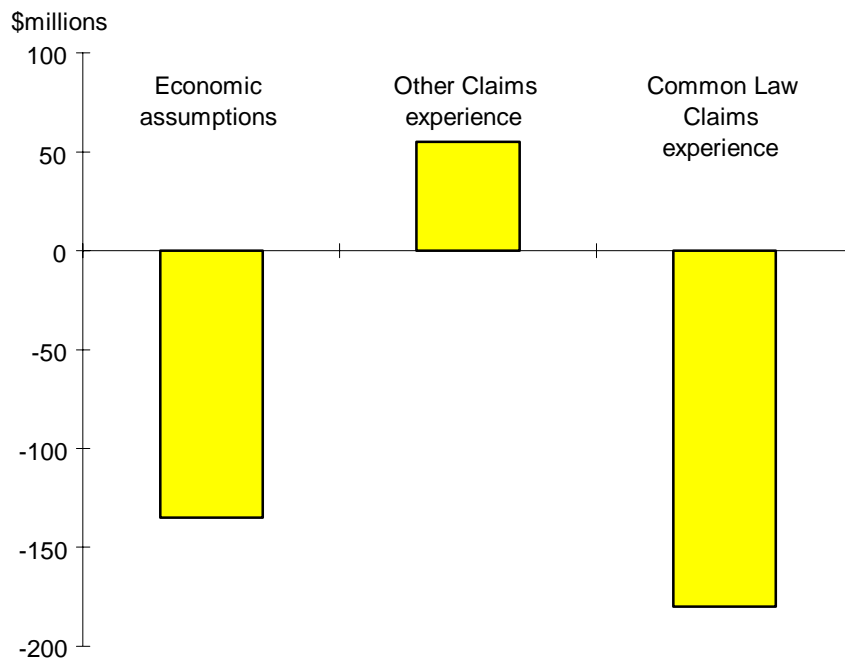
identified as contributing to the deterioration of the scheme’s financial position to a level below fully-funded as at December 1997:

- volatility in economic assumptions;
- development of the scheme’s claims experience; and
- deterioration in the area of common law claims experience.

Measurement of scheme claim liabilities and its impact on its financial position

3.8.101 Given that the WorkCover liabilities extend to 40 years, there is a level of uncertainty in the projection of the value of the scheme’s liabilities. The economic assumptions utilised such as inflation rates and investment earnings have a significant impact on the measurement of the liabilities and more importantly, on the funding position of the scheme. Chart 3.8N provides an analysis of the key factors impacting on the changes in the level of the outstanding claims liability for the 6 month period ending 31 December 1997.

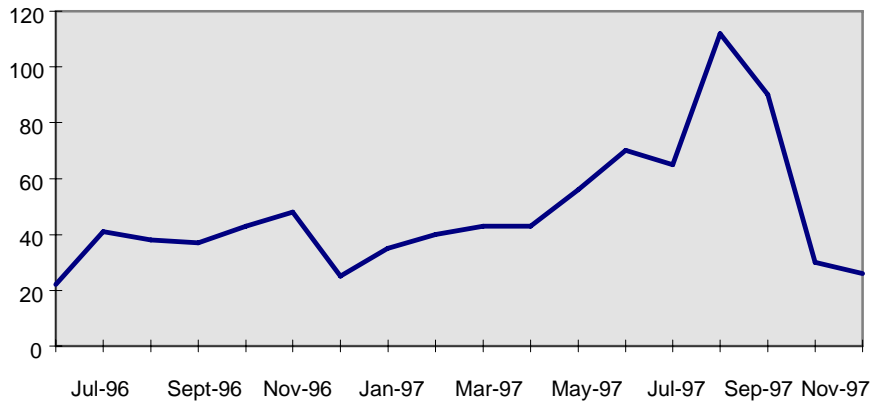
CHART 3.8N
COMPOSITION OF THE MAJOR CHANGES IN THE OUTSTANDING CLAIMS LIABILITY
FOR THE 6 MONTH PERIOD ENDED 31 DECEMBER 1997
 (\$millions)



Source: Victorian WorkCover Authority consulting actuaries valuation report.

3.8.102 As the chart indicates, a key factor contributing to the worsening trend in claims experience was an increase in common law writs lodged, higher average settlements for such cases and the maturity of the new common law system. Chart 3.8O also highlights the increased activity in common law writs for the 6 month period ending 31 December 1997.

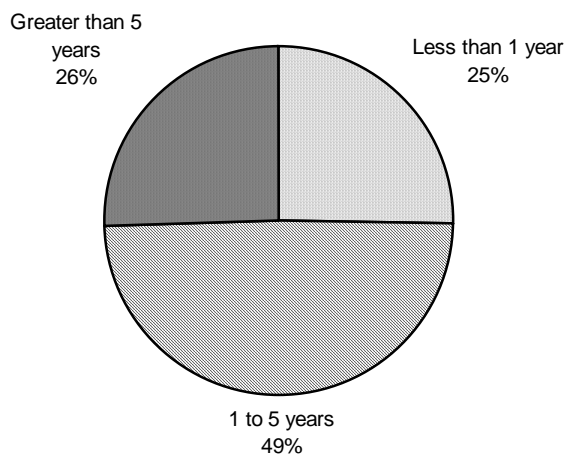
CHART 3.80
NEW COMMON LAW WRITS LODGED AT COURT AND REPORTED TO THE AUTHORITY
 (number)



Source: Victorian WorkCover Authority monthly statistical data.

3.8.103 A further factor adversely impacting on the trend in claims experience has been the increased duration of benefit payments made to claimants. Chart 3.8P indicates that as at 31 December 1997 the majority (i.e. 75 per cent) of the outstanding claims liability extends beyond 2 years.

CHART 3.8P
COMPOSITION OF OUTSTANDING CLAIMS LIABILITY AS AT 31 DECEMBER 1997
 (per cent)



Source: Victorian WorkCover Authority consulting actuarial valuation report

3.8.104 The majority of the legislative amendments enacted in November 1997 have not significantly affected the outstanding claims liability at 31 December 1997, but rather will have more of an impact on the scheme's liabilities in the future. However, it should be recognised that the prior year legislative amendments have provided some reduction in the overall costs of the scheme.

3.8.105 To ensure WorkCover's financial stability, an increase in premium revenue was deemed necessary by the Government in light of the increased costs associated with the run-off of common law over the next 3 years. From 1 July 1998, the Government will increase the average premium from 1.8 per cent to 1.9 per cent of remuneration paid by employers. In addition, from 1 January 1998, employee superannuation payments were required to be incorporated in the determination of the remuneration base for premium calculation purposes. The additional premium revenue expected to be collected for the scheme as a result of these changes, over the 18 month period to 30 June 1999, is around \$160 million. The impact of the increased premium revenue has been reflected in the consulting actuary's funding position projections provided in December 1997 as illustrated in Chart 3.8M.

3.8.106 Given the significant emerging claim cost pressures on the Victorian workers' compensation scheme, the Authority needs to continue to closely monitor and manage the Scheme to ensure its financial viability.

Recent legislative reforms

3.8.107 Since my previous *Report on Ministerial Portfolios* to the Parliament, a number of further amendments have been made to the *Accident Compensation Act 1985* for the purposes of changing the compensation payable by the scheme, which are summarised as follows:

- Workers injured on or after 12 November 1997 will not be able to sue for common law damages. Common law payments have been replaced by a no fault system which includes lump sum payments of up to \$300 000 for permanent impairment together with ongoing weekly payments for as long as the employee is unable to work;
- Weekly benefit payments for claims made on or after 12 November 1997 are to be based on the inability of the injured claimant to return to work rather than the claimant's injury classification;
- Death benefit lump sum payments are to increase for families, with the deceased worker's spouse and dependent children, for the first time, being eligible to obtain a pension in addition to a lump sum;
- Substantial increases to penalties for employers who breach health and safety laws or if the employer has not established an occupational rehabilitation program;
- Dispute resolution powers of conciliation officers are to increase, with disputes only to be taken to court when the conciliation officer is satisfied that all reasonable steps have been taken by the worker to resolve the dispute; and
- As highlighted earlier in this Report, premium rates will increase from 1 July 1998 and the basis of determination of the premium has changed as from 1 January 1998.



3.8.108 In relation to these legislative amendments, the Authority has assessed that they will be generally cost-neutral in relation to the level of benefits, with estimated cost savings of \$24 million per annum in common law transaction costs.

National Competition Policy review of the WorkCover legislation

3.8.109 The Department of Treasury and Finance Legislative Review Steering Committee released its final report for comment in January 1998 in relation to the National Competition Policy Legislative Review on the Workplace Accident Compensation Legislation. The objectives of the review were to clarify the objectives of the legislation, identify the nature of the restrictions on competition, analyse the likely effects of the restriction on competition and the economy in general, and consider alternative means of achieving the identified objectives. In summary, the report identified that there are currently the following 2 broad elements of competitive restrictions in the workers' compensation legislation:

- public underwriting and centralised premium setting and funds management; and
- licensing of authorised insurers and the approval of occupational rehabilitation providers.

3.8.110 The Review Panel made a number of recommendations which, if adopted, will constitute a significant change to the existing Scheme's administration. In summary the recommendations, include:

- The Victorian WorkCover Authority to cease to be a provider of re-insurance;
- premium setting to be more decentralised, with insurers competing at a minimum on the basis of administrative costs, with premium funds to be managed and owned by the private insurers; and
- an independent regulator to replace the Authority and to licence insurers, underwriters and self-insurers, facilitate the collection and dissemination of information, and monitor the quality of service by insurers, self-insurers and occupational rehabilitation providers.

3.8.111 The Review Panel's report findings and recommendations are currently being considered by the Government.

NO RESPONSE provided to matters raised.



UTILISATION OF GOVERNMENT PROPERTY

3.8.112 In 1990, an audit was undertaken of accommodation management across the public sector which identified substantial scope for improved management of available accommodation within both the budget and non-budget sectors. A further audit was undertaken in 1996 to follow-up the issues raised in the earlier review with the key findings reported to the Parliament in my May 1996 *Report to Ministerial Portfolios*. The key issues included in that Report were:

- while a strategic plan had been prepared for the management of the State's leased and owned accommodation located in the Central Business District and the city fringe, the plan did not incorporate a costed long-term preventative maintenance program;
- there had been an increase in the average space allocation per public servant since the audit in 1990, indicating continuing inefficient utilisation of accommodation;
- even if key objectives contained in the Government's City Precinct Strategic Plan were realised by 1999, including a 36 per cent reduction in leased and owned accommodation space, the forecast average space allocation per public servant would still remain excessive;
- regular monitoring of public sector agencies' property utilisation was not undertaken by a central agency, to facilitate the realisation of forecast rental savings and the efficient and effective utilisation of accommodation; and
- actual or imputed rent on vacant accommodation of a lettable size, (generally referred to as "dead rent") of around \$12 million was identified for the 18 month period to December 1995.

3.8.113 More recently, a further review was undertaken by audit to follow-up certain issues previously raised in Reports to the Parliament regarding the utilisation of State-owned and leased properties under the management of the Victorian Government Accommodation Group (the Accommodation Group). Key services of the Accommodation Group include:

- development and implementation of the Government's City Precinct Strategic Plan for the consolidation and rationalisation of State office accommodation in the Melbourne Central Business District and the city fringe (the city precinct);
- refurbishment and fit-out of core State-owned and leased office buildings, and the minimisation of vacant space;
- development of an office accommodation policy;
- management of leased accommodation arrangements and implementation of commercial occupancy agreements with departmental clients;
- management and rationalisation of State-owned offices in regional Victoria and the co-ordination of regional office accommodation for government departments; and
- management of State-owned and multi-tenant leased office premises in the city precinct and suburbs.

Property portfolio

3.8.114 Table 3.8Q provides a summary of the property portfolio under the management of the Accommodation Group as at 31 December 1997. This portfolio included 43 State-owned properties, providing some 157 000 square metres of accommodation with an annual imputed rental value of approximately \$20 million, and 258 property leases providing approximately 494 000 square metres of accommodation with annual rental costs of \$101 million.

**TABLE 3.8Q
PROPERTY PORTFOLIO MANAGED BY THE ACCOMMODATION GROUP
AS AT DECEMBER 1997**

<i>Location/property type</i>	<i>No. of buildings owned and leased</i>	<i>Area</i>	<i>Actual and imputed annual rental</i>
		<i>(sq.m)</i>	<i>(\$m)</i>
CBD -			
Owned	8	42 577	3.4
Leased	40	208 724	51.9
City fringe -			
Owned	14	69 124	12.6
Leased	30	121 474	25.0
Suburban -			
Owned	3	18 063	0.6
Leased	82	123 704	15.5
Country -			
Owned	18	27 362	3.0
Leased	97	39 105	4.7
Interstate -			
Owned	-	-	-
Leased	9	1 294	3.9
Total	301	651 427	120.6

Source: Accommodation Group property records.

3.8.115 The properties located within the city precinct represent 68 per cent by area or 77 per cent by actual and imputed rental cost of all properties managed by the Accommodation Group. Since the last audit review in 1996, there has been a decrease in the number of buildings occupied by the Government within the city precinct.

City Precinct Strategic Plan

3.8.116 In 1995, a City Precinct Strategic Plan (the Plan) for the management of the State's leased and owned accommodation in the Melbourne CBD and in the city fringe was developed to:

- provide directions and a strategic context for future accommodation decision-making to the year 2000; and
- achieve significant rental savings through the Government occupying less office space while operating in modern, open plan productive office environments.



3.8.117 The Plan, which has an estimated aggregate implementation cost of \$107.7 million, provides for:

- the rationalisation and consolidation of government office accommodation in the city precinct;
- disposal of redundant State-owned buildings;
- leasing of minimum commercial office accommodation space; and
- the refurbishment and re-fit of core State-owned buildings to commercial standards.

3.8.118 Regional accommodation strategies are also being developed by the Accommodation Group. According to the Accommodation Group's records, there has been a significant decrease in the number, area occupied and rent paid for non-city precinct properties over recent years.

Long-term preventative maintenance program

3.8.119 In my May 1996 *Report on Ministerial Portfolios*, it was found that a long-term preventative maintenance program had not been developed or costed for incorporation in the Strategic Plan. As a result, in audit opinion, there was a risk that those properties which had received significant funding for renovation, particularly in the Treasury Reserve, may again fall into disrepair over the longer-term, while other property holdings may continue to deteriorate and remain underutilised. The need for long-term preventative maintenance programs had also been raised in previous Auditor-General Reports to the Parliament.

3.8.120 Audit was advised in 1996 that a high priority was being given to the development of a long-term preventative maintenance program for core State-owned offices that were to be retained in State ownership.

3.8.121 In May 1997, engineering consultants were appointed by the Accommodation Group to develop a comprehensive maintenance management plan for 12 State-owned properties located in regional Victoria. Another consultant was subsequently appointed in November 1997 to prepare management plans for building services in 8 of the State's 22 owned city precinct buildings. However, the brief for this later consultancy was not as extensive as that in respect of regional properties and focused solely on building services. In particular, in relation to all city precinct properties it did not require:

- an audit and maintenance management plan to be developed which lists and prioritises works required to bring the properties to an acceptable commercial standard, and to comply with relevant legislation; and
- a consolidated and prioritised works program to be developed which integrates all recommended upgrade and refurbishment works for the total portfolio, together with a strategy for implementing a cyclical works program.



3.8.122 Subsequently, in February 1998 the Accommodation Group outsourced its property management services. Under the related Service Level Agreement, the contractor is required to prepare annual maintenance programs for specified properties and to submit them for approval to the Accommodation Group prior to implementation.

3.8.123 While acknowledging that recent refurbishment and upgrading of certain city precinct properties have reduced the risk of short-term building deterioration and the reduction of service potential, audit remains of the opinion that the Accommodation Group should give high priority to the development of a costed and comprehensive longer-term preventative maintenance program for those State-owned properties which are to be retained. Such a program is a necessary prerequisite for obtaining longer-term budgetary commitment and should form an integral part of strategic accommodation planning.

Rental savings target

3.8.124 In September 1995, it was estimated that rental savings arising from the implementation of the Strategic Plan would progressively increase to \$32 million per annum by the 1999-2000 financial year compared with 1992-93 financial year rental levels. This estimate became a key target of the Strategic Plan and was based on the realisation of certain strategic assumptions, in particular a 36 per cent reduction in leased and owned accommodation by the State.

3.8.125 However, in July 1996, the Accommodation Group revised the rental savings target to \$22 million per annum by the 1999-2000 financial year, representing a reduction in the target of \$10 million or 31 per cent.

3.8.126 The 2 key factors advised to audit which led to the significant reduction in the annual rental savings target were:

- an increase in the estimated cost of rentals between the 1996-97 and 1999-2000 financial years of \$7.9 million per annum; and
- an additional 8 000 square metres of accommodation space required for certain government departments that were amalgamated in 1996, at an estimated annual rental cost of \$2.2 million.

3.8.127 The Accommodation Group expects that the main benefits from the Strategic Plan will accrue over the years 1998 to 2000, when the expiry of certain accommodation leases are expected to cause substantial reductions in area occupied and rent paid.

Accommodation standard and usage levels

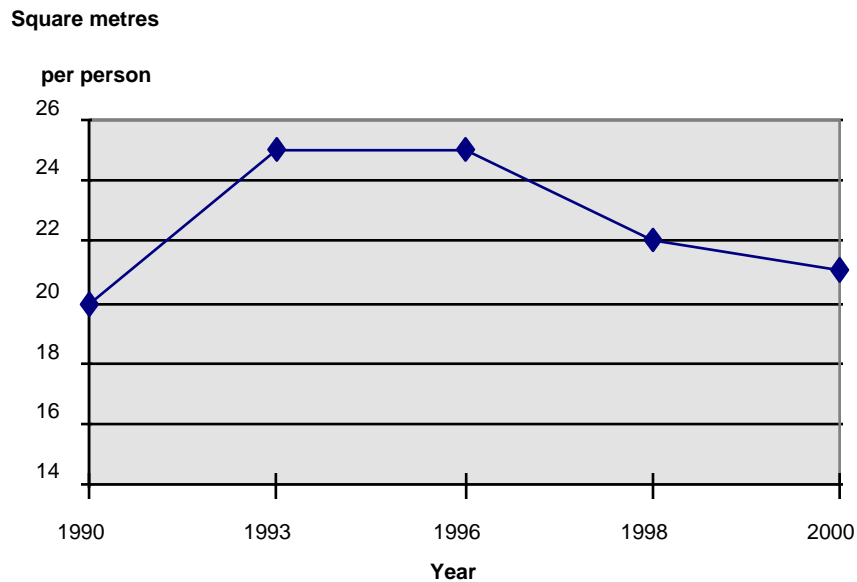
3.8.128 The Government guidelines relating to design, development and procurement of office accommodation which were promulgated in 1984 have adopted as a standard a maximum average office space allocation of 15 square metres per person. This space allocation target was subsequently reviewed by the Accommodation Group, however, the target was retained and formed the basis on which the Government's accommodation strategy was framed.



3.8.129 Nevertheless, the previous audit reviews identified that the overall average accommodation space per person for the city precinct had increased from 20 square metres per person in 1990 to 25 square metres in 1993, then remained stable at that level until 1996. **Furthermore, the recent audit review during February 1998 of a significant portion (205,000 square metres or 46 per cent) of city precinct accommodation indicated that the average utilisation of space was 22 square metres per person at that time.**

3.8.130 Chart 3.8R provides audit’s estimation of actual overall average office space per person for the city precinct in the period 1990 to 2000.

CHART 3.8R
CITY PRECINCT - AVERAGE ESTIMATED OFFICE SPACE PER PERSON (a)



(a) Audit estimates for the years 1990 to 1996 are as previously reported to the Parliament while the revised estimate for the year 2000 is based on the July 1996 revision to the Plan.

3.8.131 While the chart indicates that the implementation of the Strategic Plan may deliver an improved average space allocation per public servant should its key assumptions be realised, this average space allocation is still excessive based on the target established by the Government.



Monitoring of the implementation of the Strategic Plan

3.8.132 The Accommodation Group is responsible for the achievement of rental savings targets and other accommodation related targets envisaged under the Strategic Plan. Accordingly, it is important that the Accommodation Group undertakes an ongoing monitoring role over the effective implementation of the Strategic Plan to ensure key targets remain achievable and are in fact achieved to ensure the efficient and effective utilisation of available space.

3.8.133 The 1996 audit review found that the Accommodation Group did not undertake any regular or formalised monitoring function over property utilisation levels throughout the period of agencies' accommodation occupancy. In the resulting Report to the Parliament, it was recommended that there should be:

- routine monitoring and reporting by a responsible central agency on the level of utilisation of accommodation through regular information requests and random space audits;
- periodic reporting of findings on accommodation usage to the Minister responsible for the implementation of the city precinct strategic plan; and
- formal adoption by the Minister of revised workspace guidelines.

3.8.134 It is pleasing to report that, in July 1997, the Victorian Government Office Accommodation Guidelines were issued, which include accommodation strategies and policy principles, guidelines for workspaces, and provide for the conduct of accommodation surveys.

3.8.135 A further positive initiative, commencing from the 1997-98 financial year, is that all departments and agencies within the budget sector are required, pursuant to the Guidelines, to carry out an annual survey of their utilisation of office accommodation, initially for the city precinct only. Departments, once they have collected detailed space usage data for each floor of each building, are required to forward that data to the Accommodation Group for analysis. Reports are required, in turn, to be provided by the Accommodation Group to departments to allow assessment against accommodation standards and benchmarks and a summary of these reports is to be provided to the Minister for Finance. The deadline for the submission by departments of the first data set to the Accommodation Group is 30 June 1998. The Accommodation Group anticipates that the accommodation surveys will:

- assist departments and agencies to manage their office accommodation in the most efficient and effective manner;
- facilitate assessments of compliance with the relevant government policy; and
- better identify opportunities for rental savings and productivity improvements.

Dead rent and vacant space

3.8.136 It is also pleasing to report that my 1996 recommendation for improved reporting practices on dead rent has been accepted by the Accommodation Group. The Group now reports to the Minister for Finance each quarter on dead rent and rent paid for vacant areas under refurbishment, undergoing fit-out and changed usage.

3.8.137 Since the previous audit review, there has been a significant improvement in the level of dead rent which is estimated at \$6.8 million for the 18

month period to December 1997 compared with \$12 million for the same period to December 1995.

Specific property utilisation

3.8.138 In my previous Reports to the Parliament on the utilisation of property, comment was included on the deterioration in the condition and utilisation levels of buildings within the Treasury Reserve. Following a long period of neglect and underutilisation, it is pleasing to report that key State-owned buildings in the Treasury Reserve, particularly 2 Treasury Place and certain buildings in St Andrews Place, have been refurbished and fitted-out, and the surrounding area landscaped.

3.8.139 In previous Reports, it was identified that the use of the property at 27 Francis Street, Melbourne, valued at \$2.4 million, as a laboratory and storage facility was inappropriate and highly inefficient. The principal tenant of the property is the Environment Protection Authority. While the property was identified for sale early in 1997, it will not be vacated until December 1998.

□ *RESPONSE provided by Secretary, Department of Treasury and Finance*

Long-term preventative maintenance program

It is acknowledged that a long-term preventative maintenance program is required to ensure appropriate asset management of the Government's office accommodation portfolio.

Since 1996, the Victorian Government Accommodation Group (VGAG) has developed and implemented a strategy to upgrade and maintain core government-owned office buildings to a commercial standard and in accordance with building legislative requirements.

The following 4 steps have been followed:

- identification of core buildings;*
- progressive refurbishment of core buildings;*
- disposal of non-core buildings; and*
- development of building services management plans for all core buildings.*

The above steps are drawing to completion in the City Precinct and are well under way for the Country Offices portfolio.

The next step in the strategy is to develop cyclical maintenance plans for all core buildings. These plans will be prepared under direction between May and October 1998 by an external service provider recently contracted by government to undertake property management services in office buildings managed by VGAG. These plans will form the basis of maintenance program funding proposals for consideration as part of the 1999 Budget.

Rental savings target

Rental increases have been factored in to provide a current picture of savings. In addition, areas were adjusted to reflect new structures as departmental headquarters were amalgamated following machinery of government changes in 1996.



□ **RESPONSE** provided by Secretary, Department of Treasury and Finance - continued

Rentals are now predicted to rise at a faster rate than originally included in the model and the percentage reduction in area is now estimated to be 31 per cent instead of 36 per cent. The change in area is due mainly to lower than expected reductions in the space requirements of the Department of Human Services (DHS) over the next 2 years. As DHS engages in further outsourcing and contracting-out, their space requirements are anticipated to decrease further.

Audit need also to recognise that the asset sales program is a key component of the City Precinct Strategic Plan. Revenue of \$28 million has been raised from sale of redundant offices for vacant possession and a further sum of \$108 million has been raised from the sale and lease-back of office properties.

Accommodation standards and usage levels

In achieving the Government's target for average space allocation, audit has not recognised the process of continuous change, contracting-out and downsizing being followed by government departments in delivering their programs. Following the 1996 amalgamation of departments, office accommodation usage reflects an immediate increase as the diverse functions of the new mega-departments are brought together in new locations and the separate locations are considered for backfill or sub-leasing before staff numbers are subsequently reduced.

The process of amalgamation, review of organisation and structure takes place first, rationalisation then follows. Audit needs also to recognise that some functions of government which have increased while others have reduced.

The 1998 space audit program will form the basis for an ongoing assessment, department by department, of fluctuations in space use both on a permanent and temporary basis. The capital costs of re-organising office areas in response to organisational churn can be considerable and needs to be carefully assessed before backfill strategies are implemented.

VGAG is currently analysing departmental space utilisation audits and will report to the Minister for Finance on this subject following receipt of all departmental returns in June 1998. Comparisons against benchmarks will highlight space utilisation in individual properties and comparative performance by individual departments.

Strategies will be developed in consultation with departments to improve space utilisation where it can be cost-effectively achieved through such steps as backfill, sub-lease or lease renewal.

With budget rental funding now allocated to departments rather than held centrally and the ability of departments once they achieve their budget targets to retain savings, there now exists a real incentive for departments to economise in the use of office space.



VICTORIAN ELECTRICITY INDUSTRY PRIVATISATION

3.8.140 A feature of my previous Reports to the Parliament has been the provision of detailed comment on the Government's wide ranging electricity industry restructure program. The program, which commenced in 1994, involved the disaggregation of the State Electricity Commission of Victoria (SECV) to a new competitive structure, mainly comprising electricity distribution businesses and generation companies and, subsequently, the progressive privatisation of these businesses.

3.8.141 Under the restructure program, the State's 5 electricity distribution businesses were privatised during the 1995-96 financial year, followed by the privatisation of the State's major electricity generation companies during the 1995-96 and 1996-97 financial years. Comprehensive analyses of these sales, including the financial results achieved by the State and their impact on Victoria's finances, have been provided to the Parliament in my past *Reports on Ministerial Portfolios* and my *Reports on the Government's Annual Financial Statement* (referred to prior to the 1996-97 financial year as my *Reports on the Statement of Financial Operations*).

3.8.142 Following the sale of the major generation companies, the State's remaining interest in the electricity generation industry comprised a number of smaller entities, generally supplying power to meet intermediate and peak load requirements, including:

- *Southern Hydro Ltd* - which owned and operated 3 hydro-electric schemes at Kiewa, Dartmouth and Eildon, as well as some minor plants at other locations. The Government announced the sale of this company in November 1997;
- *Generation Victoria* - which owns and operates 2 gas-fired stations, one located in the Melbourne suburb of Newport and the other at Jeeralang in the Latrobe Valley. The Government plans to privatise these power stations when the national electricity and gas markets become more established; and
- *Snowy Mountains Hydro-Electric Authority* - which owns and manages the Snowy Mountains Hydro-electric Scheme through a Council comprising representatives from the Commonwealth, New South Wales and Victorian Governments. The Authority operates and maintains the Scheme's assets and delivers energy on a full-cost recovery basis to the New South Wales government business enterprise Pacific Power (which has a 58 per cent entitlement in the energy produced), the SECV in Victoria (which has a 29 per cent entitlement in the energy produced) and the Commonwealth Government (which has a 13 per cent entitlement in the energy produced).

3.8.143 In addition, as at the commencement of the 1997-98 financial year, the following 2 entities in the Victorian electricity industry remained in government ownership:

- *Victorian Power Exchange* - which is responsible for the provision of a wholesale electricity market to Victorian electricity participants and the operation of the electricity transmission network; and



- *PowerNet Victoria* - which owned and maintained the high voltage electricity transmission grid which provides transmission services to electricity market participants by transmitting electricity from the generators to the distributors. The Government announced the sale of this business in October 1997.

3.8.144 In this Report, I have set out below a comprehensive analysis of the 2 electricity business sales announced during the current financial year, namely, **PowerNet Victoria and Southern Hydro Ltd.**

3.8.145 Consistent with my previous Reports on the electricity privatisation program, audit has conducted a financial analysis of the sale results, however, the audit did not extend to an examination of the extent to which the Government's economic policy objectives were achieved. In particular, the long-term nature of government reforms may prevent audit in the short-term from forming firm conclusions on this issue, given that the success or otherwise of privatisation will not, in many cases, be fully known for many years.

PowerNet Victoria

3.8.146 PowerNet Victoria (PowerNet) was established in October 1994 following the disaggregation of the SECV. The primary function of the business which, at 30 June 1997, had a book value of around \$1.3 billion, was to own and maintain the existing high voltage electricity transmission system in Victoria, including:

- 5 300 kilometres of overhead transmission lines;
- 10 kilometres of underground cable;
- 13 000 galvanised steel towers; and
- 7 power station switchyards and 36 terminal and transformation stations.

3.8.147 PowerNet received the bulk of its revenue from Victorian Power Exchange (VPX) which operates the transmission system under the terms of a network agreement between the various parties. The next largest source of revenue for the business comprised network connection fees which are levied on the electricity distribution companies, the electricity generation companies and the large customers which are directly connected to the network. **Under the regulatory arrangements established for the Victorian electricity supply industry, PowerNet's revenues are substantially secured, with the company currently deriving in excess of 95 per cent of its total revenues from the above customers (relating to its regulated transmission business) under regulated tariff arrangements based on forecast maximum summer power demand.**

3.8.148 According to the Government's Information Memorandum which was issued to prospective purchasers of the business in August 1997:

- The business has an effective hedge against inflation, given that its regulated income base is linked to annual movements in the consumer price index and the business has a fixed cost base and relatively low cash costs;



- As the sole provider of a high voltage transmission system in Victoria, the business may in future face competition from new market entrants for the provision of major extra capacity to the system. However, the entity will have an advantage in tendering for new projects due to its considerable expertise in the transmission of electricity, its knowledge of the local industry and the likelihood that any future capital works for the expansion of the transmission system within the State will be required to complement the existing network;
- The general level of economic activity and the associated demand for electricity only has a marginal impact on PowerNet’s profitability in the short to medium-term; and
- The Government does not envisage that it will impose any cross-ownership rules which will prevent the purchaser of the business from acquiring any of the retail or distribution gas bodies formed from the disaggregation of GASCOR and the Gas Transmission Corporation.

Transmission system pricing

3.8.149 As PowerNet is the sole supplier of high voltage transmission services in Victoria, the fees to be charged by the business for system connections and utilisation are regulated under a Tariff Order which was established in October 1994 under the provisions of the *Electricity Industry Act 1993*. In particular, under the Tariff Order, the revenues to be derived by PowerNet from the provision of “prescribed services” could not exceed a specified level, which is adjusted annually for inflation. Prescribed services are defined as:

- network services to VPX relating to the transmission system existing at October 1994;
- connection services to the electricity distribution businesses, generators and directly connected customers, relating to the facilities existing at October 1994; and
- provision of certain specified additions to the transmission system prior to June 2000.

3.8.150 In the Information Memorandum which was provided to prospective purchasers of the business, the Government indicated that the pricing regime under the Tariff Order, which is operative until December 2002, was established to reflect the efficient levels of operating and maintenance costs and to provide a return on capital to the business based on a weighted average cost of capital. The Government also identified that, as the pricing regime applies to the entity’s revenue and not its profits, the business will generally benefit from any productivity gains made during the regulatory period in excess of those assumed in setting the above specified annual revenue level. However, any efficiency gains earned by PowerNet above the levels assumed, are to be taken into account over the subsequent regulatory period in a manner which ensures that such efficiency gains are shared between the business and its customers.



3.8.151 The Information Memorandum also outlined the Government's intentions in respect of transmission system pricing beyond December 2002. In particular, during the period January 2003 to December 2007, it was indicated that the regulated prices will be set in accordance with the following key principles:

- the level of revenue for each financial year to continue to be adjusted for movements in the consumer price index and to provide an appropriate return on capital, based on a weighted average cost of capital to investors in a business similar to that of PowerNet;
- the fees to be set having regard to the costs incurred by the business in the provision of the prescribed services, the maintenance of the transmission system and the provision of appropriate incentives for capital expenditure; and
- the benefit of efficiency gains to be shared between PowerNet Victoria and its customers.

3.8.152 For the period commencing from January 2008, the Government stated that the pricing regime is to be based on the above key principles provided that they are not inconsistent with the laws and regulations established for the operation of the national electricity market which is planned to commence in May 1998.

3.8.153 Finally, in relation to the pricing of services provided by PowerNet which are excluded from its regulated income (which comprise around 5 per cent of its total revenues), under a Transmission Licence assigned to PowerNet to operate the business, these charges must be fair and reasonable.



Victorian electricity transmission grid.

.....

Sale process

3.8.154 While it was originally envisaged by the Government that the national electricity market would involve a single transmission grid owned by all participating States and Territories, in April 1997, the Government announced its intention to privatise PowerNet. This revised position was based on the view that eventually the transmission system would comprise multiple grid owners in direct competition with each other, and that the continued public ownership of PowerNet was constraining the ability of the business to diversify into other business areas, such as telecommunications.

3.8.155 In August 1997, following the issue of an Information Memorandum to those parties interested in the proposed sale of the company, the Government received 4 bids from industry-based consortia and 3 further bids from financial institutions. In the following month, the Department of Treasury and Finance was advised by its corporate advisers that there would be sufficient underwriting capacity in the financial markets to support up to 5 fully-financed bids. Consequently, the 4 industry-based consortia together with one of the financial institution bidders were short-listed to further participate in the sale process. All the short-listed parties were subsequently advised of the final bid requirements, which included:

- any bid involving a risk apportionment to the State beyond that described in draft sale agreements would be discounted materially in the evaluation of final bids;
- the purchase price of the business to be referenced to its audited balance sheet at 30 June 1997, without any further price adjustment mechanism;
- the bidders were expected to disclose any circumstances that were relevant to the cross-ownership restrictions contained in the *Electricity Industry Act 1993*, including any actual or proposed management arrangements between the bidder and any other Victorian electricity company;
- each bid would be evaluated by a team comprising representatives from the Energy Projects Division of the Department of Treasury and Finance and the Department's corporate, legal and accounting advisers; and
- all bids would be evaluated using consistent criteria, featuring both quantitative and qualitative aspects, relating to the certainty of completion of the sale arrangements and any proposed special conditions of sale, as well as the bid price.

3.8.156 Subsequently, in October 1997, the Government received 3 final binding bids, however, the following taxation matters were identified as causing some concern in relation to the certainty of the bids:

- In August 1997, the Federal Treasurer announced proposed changes to the taxation law which would impact on the depreciable value of the assets of privatised businesses. In relation to this matter, the bidders were advised that they would have to assume any risk associated with the potential application of any legislative changes; and



- The possible application of section 51AD of the *Income Tax Assessment Act 1936* which would apply if VPX, or its successor, remained exempt from taxation and was deemed to be an “end user” of PowerNet’s assets. However, this was seen as a remote risk by the State’s advisers, since PowerNet owned and was fully responsible for the network. The impact of the section may have been to effectively deny the buyer of all deductions for depreciation, interest, repairs and maintenance. Consistent with the seller’s obligations in the sale agreement, VPX became a taxable entity in October 1997.

3.8.157 Following the Government’s assessment of the bids, in the same month, the Government announced the sale of the net assets of PowerNet to the preferred bidder, Australian Transmission Corporation Pty Ltd, a wholly-owned subsidiary of GPU Inc., a United States-based utility company. The Government also disclosed that the successful purchaser held a 50 per cent interest in the electricity distribution company Solaris Power Ltd, which would be sold down to an interest to 20 per cent by April 1998 consistent with the cross-ownership rules under the *Electricity Industry Act 1993*. In January 1998, the purchaser fulfilled this requirement by selling its full interest in Solaris Power Ltd to the Australian Gas Light Company.

3.8.158 A private sector accounting firm was appointed by the Department of Treasury and Finance in February 1997 to perform the responsibilities of process auditor for the sale of PowerNet and the remaining electricity business sales. The firm concluded that the process was conducted in a manner that was fair and equitable to all bidders.

Sale results

3.8.159 Under the sale arrangements for PowerNet Victoria, the State received gross proceeds of \$2.7 billion, comprising amounts relating to:

- sale of the State's interest in the net assets of the businesses (\$1.8 billion);
- repayment of outstanding business debt owed to the Treasury Corporation of Victoria (\$754 million);
- present value of transmission licence fees payable by the purchaser of PowerNet (\$161 million); and
- stamp duty payable on the sale transactions (\$10 million).

3.8.160 Table 3.8S outlines the key components of the proceeds received from the sale of PowerNet Victoria.

TABLE 3.8S
COMPOSITION OF SALE PROCEEDS
(\$million)

<i>Details</i>	<i>PowerNet Victoria</i>
Proceeds in excess of book value	1 249
Proceeds equal to the State's interest in the book value of the business (a)	542
	1 791
Repayment of outstanding debt of the business (b)	754
Future licence fees (present value) (c)	161
Stamp duty on sale transaction	10
Total proceeds	2 716

- (a) Represents the value of net assets sold as disclosed in the audited financial statements of the business as at the date of sale completion.
- (b) Under the sale arrangements, the State retained responsibility for the repayment of the entity's loans and accrued interest payable to the Treasury Corporation of Victoria.
- (c) In accordance with the licence fee order, the purchaser of PowerNet agreed to pay future transmission licence fees totalling \$177.5 million in nominal dollar terms (\$161 million in present value terms) for the period July 1998 to December 2000, with no further fees expected to be payable beyond this date.

3.8.161 The above table shows that the State received \$1.8 billion for the sale of the net assets of PowerNet Victoria, which at the effective date of sale had a book value of \$542 million. In effect, this resulted in **the State obtaining proceeds of \$1.2 billion in excess of the book value of the business. The State incurred costs totalling \$9.7 million in relation to this sale.**

Adequacy of sale results

3.8.162 As has been the case in other electricity entity privatisations, to ensure that reasonable returns are achieved by the State from the sale of these major businesses, the Government obtains external valuations of the businesses prior to their sale.

3.8.163 In August 1997, the Department's advisers (an independent stockbroking firm) assessed that the sale of PowerNet would be well supported by investors due to its position as a monopoly supplier, its very strong cash flow and the potential for further cost savings. Furthermore, the advisers provided the following valuations, not including licence fees, to the Department in the event of a public float:

- an aggregate value of \$1.5 billion (based on an asset depreciation rate of 7 per cent per annum); and
- a valuation range of \$1.8 billion to \$1.9 billion (based on an asset depreciation rate of 4 per cent).



3.8.164 At the same time, the Department received indicative trade sale valuations for the business, not including licence fees, from a firm of corporate advisers. These valuations were as follows:

- \$2 billion, based on an analysis of the business' discounted cashflows; and
- \$1.9 billion to \$2.2 billion, based on the forecast earnings of PowerNet Victoria and the sale proceeds and earnings multiples achieved from the previous sale of the distribution businesses.

3.8.165 The total proceeds of \$2.7 billion received from the sale of PowerNet Victoria therefore compared favourably with the above valuations of the business.

Obligations of the purchaser

3.8.166 Under the sale arrangements, the purchaser of PowerNet agreed not to sell a substantial part of the business, except with the prior written consent of the Treasurer, for a 2 year period following the date of sale completion. However, if any member of the purchasing consortium demonstrates to the Treasurer that the book value of its investment in PowerNet is less than 50 per cent of that entity's book value of the total assets (excluding intangibles, cash and short-term marketable securities), then that member is entitled to dispose of up to 49.9 per cent of the assets of the consortium in an unrestricted manner.

3.8.167 In addition, as indicated previously, the purchaser of PowerNet has agreed to progressively pay Transmission Licence fees to the State with an aggregate nominal value of \$177.5 million (estimated net present value of \$161 million), for the period July 1997 to December 2000. The purchaser has also acknowledged that the State has not made any representation or warranty in relation to the manner or form in which the Federal Treasurer's announcement of August 1997, regarding the taxation treatment of the depreciation of assets acquired from tax exempt bodies, will be implemented or applied.

Obligations of the State to the purchaser

3.8.168 While substantial financial benefits have accrued to the State from the sale of PowerNet, the State has retained certain general obligations which are outlined below.

3.8.169 In October 1994, PowerNet and VPX entered into a Network Agreement pursuant to which PowerNet agreed to provide network services which would enable the operation of the Victorian transmission network by VPX. In October 1997, the purchaser and VPX entered into a Deed of Amendment to this agreement which included the following key provisions:

- In the event of a material change in certain specified circumstances from those prevailing at the date of sale, the parties must consider any variations to the Network Agreement to ensure that network services are delivered in a manner consistent with good electricity industry practice, subject to PowerNet receiving an appropriate reward for ownership of the assets and the provision of network services. The prescribed circumstances include:
 - a change in law, including the Tariff Order or the Transmission Licence, or in the manner in which these are administered;



- a material change in the structure of the electricity supply industry, other than the impact of the commencement of the national electricity market; and
- a material change in technology or the way in which electricity is most practicably transmitted, generated or consumed;
- The parties acknowledged that the network services delivered by the business as at October 1997, in accordance with the Network Agreement, are consistent on a risk-return basis with the revenues which the business is entitled to receive pursuant to the Tariff Order and the agreement; and
- The negotiation of any future variations to the quality or scope of network services will lead to adjustments to the level of revenues paid to the business. In determining any adjustments to revenue levels, reference must be made to the relationship between the basis on which services were delivered as at October 1997 and the revenues received under the Tariff Order and the Network Agreement at that time.

3.8.170 Furthermore, the State agreed to ensure that VPX or its successor was, at the sale completion date, a taxable body under the *Income Tax Assessment Act 1936*. However, this undertaking would be withdrawn in the event that VPX became a tax exempt body after sale completion as a result of a change in Commonwealth laws. Consistent with the sale agreement, VPX became a taxable body in October 1997.

3.8.171 The State further agreed not to vest the Victorian Network Switching Centre, the Network Agreement or the Transmission Service Access Agreements (between the distribution and generation businesses and VPX) to the Victorian Energy Networks Corporation (Vencorp), the National Electricity Market Management Company Limited (NEMMCO) or any other party, unless the transferee body is a taxable body. However, the above requirement could be waived in the event that either the purchaser or the State obtained a binding tax ruling from the Australian Taxation Office that VPX or the relevant transferee is not an “end user” within the meaning of section 51AD or division 16D of the *Income Tax Assessment Act 1936*.

3.8.172 Finally, the State agreed to consider in good faith any request by the purchaser for assistance in rectifying any deficiencies in existing land easements, in so far as structures erected on them may not have complied with appropriate planning requirements or received necessary planning approval in the past, through the administration of current laws or the passage of new laws.

Southern Hydro Ltd

3.8.173 Southern Hydro Ltd commenced operations in February 1995 following the disaggregation of Generation Victoria, which itself was formed following the disaggregation of the SECV in January 1994. The company, Southern Hydro Ltd, owned and operated 10 hydro-electric power stations, comprising 21 generators situated mainly in the north-eastern region of Victoria. The power stations have a total installed generation capacity of 479 megawatts and are divided into 3 major generation schemes, located at Eildon, Dartmouth and Kiewa, and 2 minor generation schemes, located at Rubicon and Cairn Curran.

3.8.174 The company's generation capability is substantially reliant upon the quantity of available water and the timing of water releases from dams, which in turn depend on:

- annual rainfall and snowfall;
- irrigation requirements downstream of the power stations at Eildon, Dartmouth and Cairn Curran, and decisions made by water authorities regarding the timing of water releases; and
- the level of water storages.

3.8.175 Southern Hydro Ltd has the sole right to store and release water at Kiewa via a bulk water entitlement issued to the company by the Department of Natural Resources and Environment. Water releases at Eildon, Cairn Curran and Dartmouth are primarily controlled by local water bodies. The Rubicon power station operations depend to a large extent on natural water flows, however, the company has a bulk water entitlement which gives it the right to divert natural river flows for generation purposes.

3.8.176 According to the Information Memorandum which was issued to prospective purchasers of the company's assets in August 1997, the business is well positioned to benefit from peaks in wholesale electricity prices due to its rapid start-up capability for the generation of electricity, relative to its competitors. In this regard, during the 1996-97 financial year, the average time weighted pool price received by the company represented a 43 per cent premium to the time weighted pool price in the wholesale market generally.

3.8.177 The Information Memorandum also highlighted the following significant matters:

- Given that Australia is a significant producer of greenhouse gases, pressure is likely to grow to take stronger policy action to reduce emissions. If voluntary measures do not provide enough reduction in emissions, the Australian Government may be required to introduce further measures, which could include emission controls or economic instruments such as tradeable permits or a carbon tax. Any such measures would increase the cost of generation for coal-based generators while not impacting on hydro-electricity operations, which would likely result in a significant improvement in the company's relative cost position;



- Although wholesale electricity prices have remained lower than anticipated, these price levels were likely to be temporary and would most likely recover within 6 to 18 months of the commencement of the national electricity market in May 1998;
- Vesting contracts with the electricity distribution businesses will provide stability for a high proportion of the company's earnings, with such contracts expected to cover approximately 45 per cent of the company's forecast sales in the year ending 30 June 1998. The contracts will decline to zero coverage from January 2001 when the retail franchise market will be fully deregulated; and
- The company's power stations and catchment assets at Kiewa and Rubicon are situated on Crown land. Consequently, as part of the privatisation arrangements, the purchasers will be expected to enter into a long-term lease arrangement for use of the Crown land for a period of 40 to 99 years.



Turbine hall of the Eildon Power Station.

Sale process

3.8.178 Following the issue of an Information Memorandum in September 1997 to prospective purchasers of Southern Hydro Ltd, the Government received 9 expressions of interest. Following consideration of these bids, the Government proceeded to short-list 5 of these bidders, however, 2 of the short-listed consortia later withdrew from the sale process.



3.8.179 In November 1997, the remaining 3 short-listed bidders were requested to lodge binding offers for the acquisition of the company, including the nomination of lease rentals to be payable in relation to the use of Crown land at the Kiewa and Rubicon schemes. Subsequently, the Government received 3 final bids which were assessed by an evaluation team comprising representatives from the Department of Treasury and Finance and contracted corporate, legal and accounting representatives.

3.8.180 Subsequently, in the same month, the Government announced the sale of the net assets of Southern Hydro Ltd to the preferred bidder, the Southern Hydro Ltd Partnership, whose cash offer was greater than the 2 other bids. This consortium comprised the following members:

- Infratil Australia Hydro Pty Ltd, which holds a 50.2 per cent interest, is a wholly-owned subsidiary of Infratil Australia Ltd - a Queensland-based investor in infrastructure and utility assets;
- Contact Hydro Australia Pty Ltd, which holds a 27.7 per cent interest, is a subsidiary of Contact Energy Ltd, a New Zealand Government-owned power company; and
- Kanina Willows Pty Ltd, which holds a 22.1 per cent interest, is a subsidiary of UniSuper Ltd which, in turn, holds a 2.75 per cent interest in the Loy Yang A power station.

3.8.181 In December 1997, the private sector firm previously appointed by the Government to act as process auditor for electricity business sales concluded that the sale process was conducted in a manner that was fair and equitable to all bidders.

Sale results

3.8.182 Under the sale arrangements for Southern Hydro Ltd, the State received gross proceeds of \$400 million, comprising amounts relating to:

- sale of the State's interest in the net assets of the business (\$167 million);
- repayment of outstanding business debt owed to the Treasury Corporation of Victoria (\$42 million);
- present value of prepaid and future lease rentals (\$189 million); and
- stamp duty payable on the sale transactions (\$2 million).

3.8.183 Table 3.8T outlines the key components of the proceeds received from the sale of Southern Hydro Ltd.

TABLE 3.8T
COMPOSITION OF SALE PROCEEDS
(\$million)

<i>Details</i>	<i>Southern Hydro Ltd</i>
Proceeds in excess of book value	115
Proceeds equal to the State's interest in the book value of the business (a)	52
	167
Repayment of outstanding debt of the business (b)	42
Prepaid and future lease rentals (present value (c))	189
Stamp duty on sale transaction	2
Total proceeds	400

- (a) Represents the value of net assets sold as disclosed in the draft financial statements of the business as at the date of sale completion.
- (b) Under the sale arrangements, the State retained responsibility for the repayment of the entity's loans and accrued interest payable to the Treasury Corporation of Victoria.
- (c) In accordance with the lease arrangements, the purchaser of Southern Hydro Ltd agreed to pay lease rentals mainly for the lease of Crown land at Kiewa and Rubicon. The lease payments comprised an amount of \$180 million which was prepaid at the date of sale completion and \$9 million representing the estimated present value of lease rentals payable beyond the prepaid lease period.

3.8.184 The above table shows that the State received \$167 million for the sale of the net assets of Southern Hydro Ltd, which at the effective date of sale had a book value of \$52 million. In effect, this resulted in **the State obtaining proceeds of \$115 million in excess of the book value of the business. The State incurred costs of \$3.8 million in relation to the sale.**

Adequacy of sale results

3.8.185 In August 1997, the Department received an evaluation from its corporate advisers of the merits of a public share float versus a trade sale for Southern Hydro Ltd. The advisers indicated that the State would have difficulty receiving in excess of \$300 million under a public float scenario due to:

- the volatility of the company's earnings;
- recent wholesale electricity prices being substantially below the long-term expectations of many parties;
- the business facing a declining vesting contract coverage from July 1998; and
- lower water availability in the 1998-99 financial year as a consequence of recent low rainfall.



3.8.186 Furthermore, the advisers suggested that a valuation premium would be achievable through a trade sale as it offered a number of advantages, including greater financial flexibility for a prospective purchaser.

3.8.187 The total proceeds of \$400 million received by the State in relation to the sale of Southern Hydro Ltd compared favourably with the valuations of the business, on the basis of a trade sale, provided by the Government's corporate advisers in August 1997, which are summarised as follows:

- a valuation range slightly above \$300 million, based on comparable acquisitions; and
- a valuation range of \$311 million to \$339 million, based on a discounted cash flow analysis.

3.8.188 In November 1997, the corporate advisers reiterated their views to the Department that a public share float of the company would be very difficult given the stock market correction in October 1997, continued low pool prices and persistent dry weather conditions.

Obligations of the purchaser

3.8.189 Under the sale agreement, the purchaser agreed not to sell a substantial part of the business, except with the prior written consent of the Treasurer, for a period of 3 years from the date of sale. However, the State agreed to the following exceptions to this obligation:

- if a member of the purchasing consortium demonstrates to the Treasurer that the book value of its investment in the Southern Hydro Ltd business is less than 50 per cent of that entity's book value of the total assets (other than intangibles, cash and short-term marketable securities), then that member is entitled to dispose of up to 49.9 per cent of the assets of the consortium in an unrestricted manner;
- a sell-down of up to 49 per cent of the purchaser's interest in the company is permissible to certain specified bodies within 4 months of sale completion date; and
- the members of the purchasing consortium are entitled to rearrange their relative percentage interest in the company.

3.8.190 Similar to the sale arrangements for PowerNet, the purchaser of the net assets of Southern Hydro Ltd acknowledged that the State provided no representation or warranty in relation to the manner or form in which the Federal Treasurer's announcement of August 1997, regarding the tax treatment of the depreciation of assets purchased from tax exempt bodies, will be implemented or applied.

Obligations of the State to the purchaser

3.8.191 While substantial financial benefits have accrued to the State from the sale of Southern Hydro Ltd, the State has retained certain general obligations which are outlined below.

3.8.192 While assuming no legal liability or obligation in relation to native title matters, the State acknowledged the interests of the community in the continued operation of the Southern Hydro business and, accordingly, in the event that a native title interest impeded or prevented the ownership or use of the business assets or the operation of the business by the purchasers, the State agreed to use its best endeavours to place the purchasers in the same position they would have been in had the native title interest not existed. The obligation of the State to use its best endeavours is subject to, and is to be exercised with regard to:

- the State's overall policy framework with respect to native title and Aboriginal affairs at the relevant time; and
- the State's powers and the administration of law, or the passage of new laws, and the proper exercise of these powers having due regard to the interests of the purchaser, other persons and the Victorian community.

3.8.193 In terms of expenses associated with the above obligations, the agreement provides that the State shall not be obliged to expend funds, other than for advisory and project management purposes in relation to this matter.

3.8.194 Under the sale arrangements, the State also retained the following general obligations which have subsequently been satisfied:

- an indemnity by the SECV against the payment of any stamp duty incurred by the purchaser in the event of a permitted sell-down of its ownership interest within 4 months of the date of sale completion; and
- a requirement by the State to transfer the bulk water entitlements to the purchaser in respect of the Kiewa and Rubicon schemes.

3.8.195 Finally, in relation to the Rubicon and Kiewa water catchment areas, the State and the purchasing consortium also entered into 2 agreements which set out the rights and obligations of the respective parties in relation to the management of these areas. The overriding requirement of these agreements is the protection of the catchment areas and their natural environment values, with due consideration required to be given to both the requirement to protect the quality and available yield of water resources within the catchment areas and the utilisation of these resources by the purchaser.

3.8.196 Where a conflict arises between the overriding requirements and the purchaser's use of its hydro-electric assets in the catchment areas, then that conflict must be resolved by the Minister for Conservation and Land Management in consultation with the purchaser, with the Minister required to the maximum extent reasonably possible to preserve the abovementioned water resource values to enable the purchaser to continue operating the hydro-electric assets in the same or substantially similar manner as at the date of signing this agreement.

3.8.197 If any damage is caused to the catchment areas by any action of the State, except in the case of fire, and has a material adverse effect on the quantity and quality of water resources within the catchment areas, then the State must rectify the damage so as to minimise the impact of the damage.

Comparison of sale results to previous business sales

3.8.198 The sale of PowerNet and Southern Hydro Ltd brings to \$21.7 billion the total proceeds to the State from the sale of electricity businesses (including the present value of franchise, licence and lease fees receivable) to the date of preparation of this Report.

3.8.199 In addition to the provision of comparisons of the results achieved by the State from the sale of electricity businesses to independent valuations, my previous Reports to the Parliament have also provided an analysis of the adequacy of the sale results on the basis of price to earnings multiples.

3.8.200 Table 3.8U presents the sale results achieved by the State in relation to the 2 electricity businesses, namely, PowerNet Victoria and Southern Hydro Ltd, on the basis of price to earnings multiples, and the results achieved from the earlier sales of the electricity distribution and generation businesses.

3.8.201 When comparing these ratios, recognition needs to be taken of the fact that PowerNet operates under different market conditions than all other electricity entities and that Southern Hydro Ltd provides hydro-electric as opposed to coal-based power generation and predominantly services intermediate and peak load power requirements as compared with the base load requirements serviced by the previously privatised generators. **In addition, under the arrangements established by the Government for the operation of the State's electricity supply industry, PowerNet will have the benefit of a regulated revenue base as the sole supplier of the existing high voltage transmission system in Victoria, whereas the electricity generation and distribution businesses (excluding the regulated monopoly distribution function) are exposed to an increasingly competitive electricity market.**

**TABLE 3.8U
SALE PROCEEDS AND EARNINGS MULTIPLES
ACHIEVED FROM THE SALE OF ELECTRICITY ENTITIES (a)**

<i>Details</i>	<i>Price to earnings multiples</i>			
	<i>PowerNet Victoria</i>	<i>Southern Hydro Ltd</i>	<i>Electricity generation businesses</i>	<i>Electricity distribution businesses</i>
1994-95	-	-	-	15.9
1995-96	-	18.9	12.5	15.0
1996-97	-	13.9	13.3	12.8
1997-98	13.4	14.7	11.1	12.0
1998-99	12.3	12.4	11.1	-
1999-00	11.2	12.6	-	-
Average	12.3	14.5	12.0	13.9
Sale proceeds (\$m) (b)	2 545	398	9 001	8 270

(a) The earnings multiples are based on projected earnings before depreciation, interest, tax and abnormal items (EBDIT), as per the Information Memorandum for each company (in nominal dollars).

(b) Represents proceeds for the sale of the net assets of the businesses and the repayment of debt. In relation to Southern Hydro Ltd, the sale proceeds also include the value of prepaid and future lease rentals.

3.8.202 Notwithstanding the difference in PowerNet's operating environment, Table 3.8U shows that the price to earnings multiples achieved by the State from

.....

the sale of this business were broadly comparable with the results achieved from the sale of the distribution and generation businesses. The major factor attributing to this outcome, as advised by the Department of Treasury and Finance, is that the operations of both PowerNet and the infrastructure element of the electricity distribution businesses are effectively monopoly activities subject to regulation, with the progressive introduction of competition to the retailing of electricity by the distribution businesses only impacting on a minor part of the profitability of these businesses. In relation to the consistency of outcomes between PowerNet and the generation businesses, it would appear that the purchasers have valued PowerNet's monopoly which is heavily regulated, on par with the generation businesses which are subject to competition, however, PowerNet may benefit from revenue expansion capability through improved utilisation of generation capacity.

3.8.203 The price-to-earnings multiples achieved for the sale of Southern Hydro Ltd were higher than those achieved by the previous sales of the generation businesses. The Department advised that the higher results reflected the higher purchaser expectations in relation to the future profitability of this business compared with the previous sales.

What will be the ongoing impact of electricity business sales on State finances?

3.8.204 The cash proceeds of \$2.9 billion received by the State from the 2 business sales were mainly applied towards the:

- reduction of budget sector debt (\$1.7 billion);
- retirement of debt with the Treasury Corporation of Victoria relating to the businesses sold (\$796 million);
- recoupment of the privatisation and reform costs through a contribution retained by the Consolidated Fund (\$60 million); and
- investments by the Department of Treasury and Finance, pending consideration by the Treasurer of alternative applications of these funds (\$346 million).

3.8.205 My previous Reports to the Parliament have provided an analysis of the future impact of the electricity privatisation program on State finances, in terms of the net interest savings to be achieved from the repayment of State debt from the sale proceeds, after taking into account revenue forgone in the form of dividends and State equivalent taxes.

3.8.206 As previously mentioned, the State has received in excess of \$21 billion from the sale of electricity businesses to date, the majority of which has been applied to the reduction of State debt which, in turn, has resulted in a significant reduction in interest costs. **On the basis of current Department of Treasury and Finance projections, it is estimated that the State will derive annual net savings of approximately \$760 million during the 1997-98 financial year from electricity privatisations that have occurred at the date of preparation of this Report.**

United Energy Limited - Franchise fee indemnity

3.8.207 My October 1996 *Report on the Statement of Financial Operations* commented on an indemnity provided by the State to the purchaser of United Energy Limited, an electricity distribution company, concerning the deductibility of franchise fees for taxation purposes. Under this indemnity, the State will be required to make a payment of \$85 million to the purchaser in the event that an unfavourable tax ruling is received from the Australian Taxation Office (ATO), and the ruling is not overturned within 3 years of the date of sale of the United Energy business.

3.8.208 In August 1995, the ATO issued a private tax ruling to United Energy which concluded that franchise fees payable by the company to the State were not tax deductible. Subsequently, in October 1995, the Government lodged an objection to the ATO ruling, however, a further private tax ruling was issued by the ATO in August 1996 which confirmed that the franchise fees were not deductible for taxation purposes.

3.8.209 The Government subsequently appealed the ATO decision in the Federal Court, but in August 1997 the Court dismissed the appeal and confirmed that the franchise fees were not deductible for tax purposes. The Government then **lodged an application seeking special leave to appeal to the High Court. However, in February 1998, the High Court refused the Government's application which resulted in the triggering of the indemnity clause in the sale agreement.**

3.8.210 Consequently, in February 1998, the SECV paid an amount of \$85 million to the purchaser of United Energy Ltd.

Introduction of winter power bonus

3.8.211 In February 1998, the Government announced plans for the provision to household and small business electricity customers in Victoria of a *Winter Power Bonus* in the form of a \$60 yearly reduction on winter electricity accounts over the next 3 years. The Government estimated that this initiative would deliver savings of around \$360 million to consumers over the 3 year period, through the passing-on to customers of the equivalent of franchise fees payable by the distribution businesses to the State where appropriate, or cash payments to those businesses from the Consolidated Fund. Accordingly, **the initiative will not impact on the profitability of the distribution businesses but will reduce the Government's overall return from these businesses by around \$360 million due to the reduction in franchise fees receivable.**

3.8.212 The Department of Treasury and Finance has advised that the *Winter Power Bonus* initiative will be facilitated by amendments to the relevant Tariff and Franchise Fee Orders under the *Electricity Industry (Amendment) Act 1993*. Detailed arrangements for the implementation of the initiative were subject to negotiation with the distribution businesses as at the date of preparation of this Report. The Department of Treasury and Finance advised that, in relation to United Energy Limited, the State had reached agreement with the business whereby \$20 million of the \$85 million paid by the State to the business under the previously mentioned indemnity arrangements will be repaid to the State, provided this initiative is introduced.

NO RESPONSE was provided to the issues raised.

COST OF TRICONTINENTAL FAILURE

Cost to the State from the failure of Tricontinental

3.8.213 My previous Reports to the Parliament have commented on the financial arrangements established by the Government during the 1990-91 financial year, as part of the sale of the State Bank of Victoria, to acquire the Tricontinental Group of companies. As at 31 December 1990, Tricontinental had a net deficiency of \$1.7 billion. Under a Deed of Undertaking between the State and Tricontinental, which was established subsequent to the sale of the State Bank, the State became obligated to provide all necessary financial support to ensure that Tricontinental would be able to meet its obligations as and when they fell due. That is, the State became obligated to meet the net deficiency of Tricontinental and any future movements in the level of that deficiency.

3.8.214 This Report provides an update of the aggregate cost to Victorian taxpayers of this financial failure, together with the status of the residual Tricontinental loan portfolio.

Aggregate cost to Victorian taxpayers

3.8.215 In my October 1991 *Report on the Government's Finance Statement* it was estimated that the aggregate cost of Tricontinental to Victorian taxpayers would be around \$2.4 billion. However, the current audit review identified that **the aggregate cost of Tricontinental to Victorian taxpayers as at 31 December 1997 had reduced to \$2.3 billion.** Table 3.8V outlines the key components of this cost.

TABLE 3.8V
AGGREGATE COST TO VICTORIAN TAXPAYERS OF
TRICONTINENTAL, AT 31 DECEMBER 1997
((\$million))

<i>Items</i>	<i>Amount</i>	
Debt and loans assumed by State (a)	1 966	
Operating subsidies provided by Consolidated Fund (b)	365	
Cost of servicing debt assumed (c)	181	
Royal Commission into the affairs of Tricontinental	17	2 529
Less -		
Tricontinental net assets as at 31 December 1997	90	
Recoupments from Tricontinental to the Consolidated Fund (d)	185	(275)
Total cost to Victorian taxpayers		2 254

(a) Comprises debt and loans with a value of \$576 million assumed prior to the sale of the State Bank, \$500 million assumed in June 1994 and a further \$890 million assumed in September 1994.

(b) Represents financial support provided to Tricontinental during the financial years 1991-92 to 1994-95.

(c) Represents the estimated financing costs incurred by the State on the debt assumed from Tricontinental, covering the period up to the date of repayment of this debt. As at the date of preparation of this Report, \$467 million of the debt previously assumed had not been repaid.

(d) Comprises amounts received by the Consolidated Fund from Tricontinental on account of loan recoveries and dividends.



3.8.216 The overall improvement of around \$120 million in the cost of Tricontinental to Victorian taxpayers, compared with the estimate as at 30 June 1991, mainly reflects the:

- achievement of higher than expected recoveries from the realisation of the loan portfolio, including the recovery of debts totalling \$173 million which were previously assessed as unrecoverable; and
- an out-of-court settlement of \$136 million during the 1993-94 financial year from the previous auditors of Tricontinental, **which were off-set by higher than anticipated interest costs incurred on the debt portfolio assumed by the State from Tricontinental, due in part to the portfolio being held for a longer than expected period.**

Current status and future outlook

3.8.217 As previously indicated in this Report, as at 31 December 1997, Tricontinental held net assets valued at \$90 million, comprising assets valued at \$93 million and liabilities valued at \$3 million. However, a number of litigation cases were being contested or defended by Tricontinental as at the date of preparation of this Report, which may ultimately impact on Tricontinental's financial position. Table 3.8W presents a summary of Tricontinental's financial position as at 31 December 1997.

TABLE 3.8W
TRICONTINENTAL'S FINANCIAL POSITION,
AT 31 DECEMBER 1997
((\$million))

<i>Items</i>	<i>Amount</i>	
Assets -		
Cash	50	
Loans and other receivables (net)	39	
Investments	2	
Property, plant and equipment	1	
Other	1	93
Liabilities -		
Creditors and borrowings	2	
Provisions	1	(3)
Net assets		90

3.8.218 The key residual activity of Tricontinental is the orderly realisation of the remaining loan and receivables portfolio which as at 31 December 1997, as illustrated above, had an estimated net realisable value of \$39 million. This figure comprised gross receivables of \$102 million, less a provision for bad and doubtful debts of \$63 million.



3.8.219 The Tricontinental Group has advised the Government that the remaining loan portfolio could take around 3 to 5 years to realise, if returns to the State are to be maximised. However, a number of factors may impact on the amounts to be ultimately recovered by the State, including:

- future economic circumstances;
- complexities associated with certain receivables;
- the outcome of a number of legal disputes in relation to outstanding loans and other receivables; and
- future investment decisions regarding the application of available cash funds.

NO RESPONSE was 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>
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MATTERS RESOLVED OR ACTION COMMENCED

DEPARTMENT OF TREASURY AND FINANCE

<p>Ministerial Portfolios, May 1997, pp. 288-91.</p>	<p>At the time of the introduction of the Corporate Card, the Department of Treasury and Finance did not develop a targeted level of cost savings to be achieved nor has it since sought to establish the actual level of savings achieved within the Victorian public sector to ensure that optimum outcomes have been obtained from the utilisation of the Card.</p> <p>An audit analysis indicated that the Corporate Card was not widely used, when compared with the level of purchasing activity undertaken within the public sector. Consequently, available cost savings were not being fully realised. The absence of central monitoring of Corporate Card utilisation adversely impacts on the ability of the Department of Treasury and Finance, as the responsible central agency, to measure and evaluate the success of the implementation of the Card across the whole-of-government, and formulate strategies to promote its use and maximise any available savings.</p>	<p>The Department has indicated that it now centrally monitors the Corporate Card facility. The monitoring covers, among other things, total card usage under the facility, card usage by the master billing account holders, the appropriateness of bank charges and selectively questions large cash equivalent usage with the participants. In addition the Department is leading the Victorian Government Best Practice Corporate Card Processing System Working Group, whose purpose is:</p> <ul style="list-style-type: none"> • to implement a best practice Corporate Card purchasing transactions process framework across the whole of government; and • to identify and provide a common Corporate Card System solution according to the best practice Corporate Card process framework while still meeting the specific needs of each government department. <p>The Working Group intends to develop and implement a common streamlined process for Corporate Card purchases that reduces the cost of purchasing transactions and increases the usage and user base of Corporate Cards across the Victorian Government Sector.</p>
<p>Ministerial Portfolios, May 1997, p. 290.</p>	<p>Almost 1 000 Corporate Cards had not been cancelled for up to 12 months after respective public sector agencies had been sold or abolished, unnecessarily exposing the State to financial risks.</p>	<p>The Department now ensures that any Corporate Cards that are on issue prior to the privatisation/sale/abolishment of an agency are withdrawn from circulation by the event date, cancelled and returned to the Bank by the account holder. Separate instructions are also provided to the Card Issuer advising of the impending event. The actual date of the event is confirmed as soon as possible thereafter to enable cancellation of the facility and to eliminate any possibility of exposure to the State from this facility when such a privatisation, sale or abolishment event occurs.</p>



**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>
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MATTERS RESOLVED OR ACTION COMMENCED - *continued*

DEPARTMENT OF TREASURY AND FINANCE - *continued*

<p>Ministerial Portfolios, May 1997, pp. 293-5.</p>	<p>There is a need at the Departments of Justice, and Premier and Cabinet to strengthen the authorisation and verification procedures to ensure the probity and accountability of all Corporate Card payments.</p>	<p>Refer comments included in this Report under Schedule A for the Departments of Justice and Premier and Cabinet.</p>
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VICTORIAN FUNDS MANAGEMENT CORPORATION

<p>Ministerial Portfolios, May 1996, p. 300.</p>	<p>The effective implementation of various initiatives aimed at improving the Corporation's performance will be vital to its ongoing viability and to the achievement of cost-efficiencies to the public sector from centralised funds management.</p>	<p>While the Corporation's client base and investment portfolio had not significantly increased since the date of the previous audit review, various initiatives had been introduced with the aim of improving the efficiency and effectiveness of its operations, and to establish a track record in funds management.</p>
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NO ACTION TAKEN

DEPARTMENT OF TREASURY AND FINANCE

<p>Ministerial Portfolios, May 1996, p. 335.</p>	<p>There is a need for clarification within the Government's supply guidelines of the classification of consultancy and contractor services, in order to improve the disclosure of consultancy payments to the Parliament.</p>	<p>The Victorian Government Purchasing Board reviewed the classification of consultancy and contractor services within the supply guidelines, however, the Board decided against amending the guidelines.</p>
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**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>
COMPLETED AUDITS				
Department of Treasury and Finance	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.46.	3 Sept. 1997	3 Sept. 1997
FINANCE				
Coal Mine Workers' Pensions Fund	30 June 1997	" "	3 Sept. 1997	3 Sept. 1997
Emergency Services Superannuation Board	30 June 1997	" "	24 Sept. 1997	24 Sept. 1997
Hospitals Superannuation Board	30 June 1997	" "	24 Sept. 1997	24 Sept. 1997
Local Authorities Superannuation Board	30 June 1997	" "	29 Aug. 1997	25 Sept. 1997
Parliamentary Contributory Superannuation Fund	30 June 1997	" "	8 Oct. 1997	9 Oct. 1997
Port of Geelong Authority Superannuation Fund (a)	30 June 1997	" "	15 Aug. 1997	15 Aug. 1997
Regulator-General, Office of the	30 June 1997	" "	3 Oct. 1997	3 Oct. 1997
State Superannuation Fund	30 June 1997	" "	17 Sept. 1997	17 Sept. 1997
Victorian Superannuation Board	30 June 1997	" "	17 Sept. 1997	17 Sept. 1997
Victorian Superannuation Fund	30 June 1997	" "	17 Sept. 1997	17 Sept. 1997
Victorian WorkCover Authority	30 June 1997	" "	29 Aug. 1997	29 Aug. 1997
Water Industry Superannuation Fund	30 June 1997	" "	10 Sept. 1997	16 Sept. 1997
Water Industry Superannuation Fund Pty Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994</i> , s.53A.	26 Aug. 1997	26 Aug. 1997

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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>
COMPLETED AUDITS - continued				
GAMING				
Tattersall Gaming Machine Division	30 June 1997	31 Oct. <i>Gaming Machine Control Act 1991, s.132.</i>	30 Oct. 1997	30 Oct. 1997
Tattersall Sweep Consultation	30 June 1997	<i>Tattersall Sweep Consultation Act 1958.</i>	30 Oct. 1997	30 Oct. 1997
Tattersall's Club Keno	30 June 1997	31 Oct. <i>Club Keno Act 1993, s.10.</i>	30 Oct. 1997	30 Oct. 1997
Victorian Casino and Gaming Authority	30 June 1997	31 Oct. <i>Financial Management Act 1994, s.46.</i>	21 Oct. 1997	21 Oct. 1997
TREASURER				
Aluminium Smelters of Victoria Pty Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994, s.53A</i>	29 Aug. 1997	29 Aug. 1997
Aluvic Metal Sales Pty Ltd	30 June 1997	" "	2 Oct. 1997	2 Oct. 1997
Australian Power Exchange Pty Ltd	30 June 1997	" "	1 Sept. 1997	8 Sept. 1997
Bannister Trial Pty Ltd (b)	Period 1 Nov. 1995 to 18 April 1997	18 Aug. <i>Financial Management Act 1994, s.53A.</i>	5 Sept. 1997	5 Sept. 1997
Chief Electrical Inspector, Office of the	30 June 1997	31 Oct. <i>Financial Management Act 1994, s.46.</i>	23 July 1997	17 Sept. 1997
Ecogen Energy Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994, s.53A.</i>	27 Aug. 1997	27 Aug. 1997

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>
COMPLETED AUDITS - continued				
TREASURER - continued				
Electricity Services Victoria (c)	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	2 Sept. 1997	5 Sept. 1997
Everton Dell Pty Ltd (d)	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.53A.	5 Sept. 1997	5 Sept. 1997
Gas and Fuel Corporation Superannuation Fund (e)	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	16 Sept. 1997	16 Sept. 1997
Gas Transmission Corporation	30 June 1997	" "	21 Aug. 1997	26 Aug. 1997
GASCOR	30 June 1997	" "	4 Sept. 1997	5 Sept. 1997
Generation Victoria	30 June 1997	" "	27 Aug. 1997	27 Aug. 1997
Holding Trust	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.53A.	26 Nov. 1997	26 Nov. 1997
Leanne Power Pty Ltd (f)	Period 13 March 1997 to 8 May 1997	8 Sept. <i>Financial Management Act 1994,</i> s.53A.	12 Nov. 1997	13 Nov. 1997
Loy Yang B Power Station Pty Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.53A.	5 Sept. 1997	5 Sept. 1997
Melbourne Port Corporation	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	11 Sept. 1997	11 Sept. 1997
National Electricity Pty Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.53A.	3 Sept. 1997	11 Sept. 1997
National Electricity Pty Ltd (g)	Period 1 July 1997 to 6 Nov. 1997	6 March. <i>Financial Management Act 1994,</i> s.53A.	18 Dec. 1997	19 Dec. 1997
National Power Exchange Pty Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.53A.	1 Sept. 1997	8 Sept. 1997

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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>
COMPLETED AUDITS - continued				
TREASURER - continued				
Opalwood Pty Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.53A.	26 Nov. 1997	26 Nov. 1997
Port of Geelong Authority	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	27 Aug. 1997	27 Aug. 1997
Port of Melbourne Authority	30 June 1997	" "	29 Aug. 1997	29 Aug. 1997
Port of Portland Authority	30 June 1997	" "	27 Aug. 1997	27 Aug. 1997
PowerNet Victoria	30 June 1997	" "	18 Sept. 1997	19 Sept. 1997
PowerNet Victoria (h)	Period 1 July 1997- to 6 Nov 1997	6 March <i>Financial Management Act 1994,</i> s.46.	18 Dec. 1997	19 Dec. 1998
Quiet Life Limited (i)	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.53A.	29 Aug. 1997	29 Aug. 1997
Rehabilitation Holdings Pty Ltd	30 June 1997	" "	31 July 1997	31 July 1997
Rehabilitation Holdings Pty Ltd (j)	Period 1 July 1997- 31 July 1997	" "	21 Oct. 1997	21 Oct. 1997
Rural Finance Corporation	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	12 Aug. 1997	12 Aug. 1997
Securities Finance Corporation Ltd	31 Dec. 1997	30 April. <i>Financial Management Act 1994,</i> s.53A.	12 Feb. 1998	12 Feb. 1998
Southern Hydro Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.53A.	29 Aug. 1997	3 Sept. 1997

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>
COMPLETED AUDITS - continued				
TREASURER - continued				
Southgate Control Limited	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.53A.	26 Nov. 1997	26 Nov. 1997
Southgate Hotel Management Pty Ltd	Period 1 July 1996 to 16 April 1997	" "	26 Nov. 1997	26 Nov. 1997
Southgate Trust	30 June 1997	" "	26 Nov. 1997	26 Nov. 1997
State Electricity Commission of Victoria	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	5 Sept. 1997	5 Sept. 1997
State Trustee Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.53A.	25 Sept. 1997	30 Oct. 1997
STL Financial Services Ltd	30 June 1997	" "	25 Sept. 1997	30 Oct. 1996
Great Eagle Hotels (Victoria Pty Ltd)	Period 1 July 1996 to 16 April 1997	" "	26 Nov. 1997	26 Nov. 1997
The Albury Gas Company Ltd	30 June 1997	" "	25 Aug. 1997	28 Aug. 1997
Transport Accident Commission	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	28 Aug. 1997	28 Aug. 1997
Treasury Corporation of Victoria	30 June 1997	" "	15 Sept. 1997	15 Sept. 1997
Tricontinental Australia Ltd	31 Dec. 1997	30 April <i>Financial Management Act 1994,</i> s.53A.	12 Feb. 1998	12 Feb. 1998
Tricontinental Corporations Ltd	31 Dec. 1997	" "	12 Feb. 1998	12 Feb. 1998
Tricontinental Holdings Ltd	31 Dec. 1997	" "	12 Feb. 1998	12 Feb. 1998
Twin Waters Resorts Pty Ltd	31 Dec. 1997	" "	12 Feb. 1998	12 Feb. 1998
Utilities Insurance Company Pty Ltd (k)	1 July 1995 to 31 March 1996	31 July <i>Financial Management Act 1994,</i> s.53A.	18 July 1997	31 July 1997

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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>
COMPLETED AUDITS - continued				
TREASURER - continued				
Vicfleet Pty Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.53A.	24 Oct. 1997	28 Oct. 1997
Victorian Channel Authority	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	27 Aug. 1997	27 Aug. 1997
Victorian Managed Insurance Authority	Period 1 October 1996 to 30 June 1997	" "	29 Aug. 1997	29 Aug. 1997
Victorian Rehabilitation Centre Pty Ltd	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.53A.	31 July 1997	31 July 1997
Victorian Rehabilitation Centre Pty Ltd (j)	Period 1 July 1997 to 31 July 1997	" "	21 Oct. 1997	21 Oct. 1997
Victorian Funds Management Corporation	30 June 1997	31 Oct. <i>Financial Management Act 1994,</i> s.46.	28 Aug. 1997	28 Aug. 1997
Victorian Power Exchange	30 June 1997	" "	9 Sept. 1997	9 Sept. 1997

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>
INCOMPLETE AUDITS				
GAMING				
Tabcorp Holdings Limited Club Keno Business Segment	15 Aug. 1994 to 30 June 1995	31 Oct. <i>Club Keno Act</i> 1993, s.10.	Awaiting signed set of financial statements.	
Tabcorp Manager Pty Ltd Gaming Business Segment	15 Aug. 1994 to 30 June 1995	31 Oct. <i>Gaming Machine Control Act 1991</i> , s.132.	Doubt exists as to whether financial statements meet requirements of the <i>Gaming Machine Control Act 1991</i> .	
Totalizator Agency Board	1 Aug. 1994 to 2 June 1995	31 Oct. <i>Financial Management Act 1994</i> , s.46.	Awaiting signed set of financial statements.	
TREASURER				
Southern Hydro Ltd (l)	Period 1 July 1997 to 18 Dec. 1997	18 April <i>Financial Management Act 1994</i> , s.53A.	Financial statements in the process of being finalised.	

- (a) Final Audit. Members' funds transferred to Victorian Superannuation Fund.
 (b) Final audit. Entity deregistered April 1997.
 (c) Final audit. Entity dissolved July 1997.
 (d) Final audit. Entity deregistered October 1997.
 (e) Final audit. Members' funds transferred to Victorian Electricity Industry Superannuation Fund on 1 July 1997.
 (f) The company, which was formed to facilitate the sale of the net assets of Loy Yang B Power Station Pty Ltd, was sold to a private sector entity on 8 May 1997.
 (g) Sold to private sector entity as at 6 November 1997.
 (h) Audit requested by the Treasurer of Victoria as at the date of sale of the entity's net assets to the private sector.
 (i) Formerly Loy Yang Power Ltd. Name changed on 13 May 1997.
 (j) Sold to private sector entity as at 31 July 1997.
 (k) Sold to private sector entity as at 31 March 1996.
 (l) Sold to private sector entity as at 18 December 1997.

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