VICTORIA

Auditor-General
of Victoria

REPORT ON MINISTERIAL PORTFOLIOS

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President
Legislative Council
Parliament House
MELBOURNE

The Hon. A. Andrianopoulos MLA
Speaker
Legislative Assembly
Parliament House
MELBOURNE

Sir

I am pleased to forward this report to you for presentation to each House of Parliament, pursuant to section 15 of the *Audit Act* 1994.

This report sets out the results of audits conducted on public sector agencies pertaining mainly to the financial years ending 30 June 2000 and 31 December 2000, and the results of special reviews undertaken up to the date of preparation of this report.

Yours faithfully

J.W. CAMERON
Auditor-General

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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, EMPLOYMENT AND TRAINING	**Page 19**

Bio21 project

- The State entered into a contract in October 2000 with The University of Melbourne, the Walter and Eliza Hall Institute of Medical Research and the Royal Melbourne Hospital to undertake and assist in the commercial development of bio-medical research. Total funding of up to $159.5 million was available to this project, known as Bio21.

Paras 3.1.29 to 3.1.32

- Given that the majority of the ownership and the risks of the Bio21 project will rest with public sector agencies, consideration needs to be given to the level of accountability for Bio21 Australia Limited (the company established to implement the project) to Parliament and, ultimately, to Victorian taxpayers. As Parliament's auditor, it will be important that the Auditor-General is involved in this accountability process.

Paras 3.1.37 to 3.1.39

Melbourne University Private Limited

- Melbourne University Private Limited (MUPL) was established in January 1998 as a public company limited by shares. Although the original intention was to seek other investors, The University of Melbourne is currently the only investor.

Paras 3.1.52 to 3.1.54

- MUPL has incurred significant losses since its establishment. For the year ended 31 December 2000, MUPL reported an operating loss of $2.2 million.

Paras 3.1.69 to 3.1.72

EDUCATION, EMPLOYMENT AND TRAINING - *continued* Page 19

Financial viability of TAFE institutes

- The Chisholm Institute of TAFE did not pay its suppliers in accordance with government guidelines and experienced cash flow problems that required advance funding of $2 million from the Office of Post Compulsory Education, Training and Employment in December 2000 to enable the payment of both suppliers and staff.

Paras 3.1.92 to 3.1.95

School Global Budget

- The method used to calculate School Global Budgets (SGB) changed for the 2001 school year which was designed to achieve greater transparency and equity in the funding of schools.

Paras 3.1.193 to 3.1.194

- The Office of Schools has identified 590 schools (36 per cent) requiring transition funding, that is, actual salary costs are forecast to be greater than the funding allocation, based on the formula under the new SGB model. DEET has provided transition funding of $28 million for the 2001 school year.

Paras 3.1.160 to 3.1.186

- Even though the leadership profiles (principal, assistant principal and leading teachers) of secondary schools are higher than for primary schools and, accordingly, the actual cost per teacher in secondary schools is greater than in primary schools, the SGB funding formula is based on a standard salary cost for all teachers (other than principals) irrespective of whether they are primary or secondary.

Paras 3.1.160 to 3.1.186

HUMAN SERVICES — Page 79

Financial viability of hospitals

- There are 12 hospitals which, based on the hospitals subject to our analysis, are expected to be operating under financial difficulties as at 30 June 2001.

  Paras 3.2.16 to 3.2.27

- Despite the injection of supplementary funds over the past year or so, the financial condition of the public hospital system remains weak and vulnerable. Suitable financial structures need to be in place to reward innovation and cost-effectiveness if this ongoing issue is to be placed on a sounder footing in the future.

  Para. 3.2.28

Rural hospital information technology alliances

- The establishment of the rural alliances to provide information technology (IT) facilities to rural hospitals represents a new model of operating initiated by the Department of Human Services. This model has successfully delivered benefits in the form of up-to-date IT technologies to all participating hospitals.

  Paras 3.2.68 to 3.2.69

Post-acute care planning

- In the latter part of the last decade, the Department of Human Services, particularly through its Acute Health Division, has introduced a range of innovative programs and initiatives to address the demand for services in the sub-acute and post-acute sectors. Despite these innovations, limitations in available data precluded us from making a definitive judgement on the adequacy of the Department's actions.

  Paras 3.2.200 to 3.2.210

- There is increasing demand for post-acute care services due to decreasing length of stay and bed availability in acute hospitals and rehabilitation services, weaknesses in discharge effectiveness, and decreases in community care-type services provided by hospitals.

  Paras 3.2.120 to 3.2.153

INFRASTRUCTURE Page 161

Local government infrastructure

- Deficiencies in the recognition and valuation of infrastructure assets controlled by local government entities may adversely impact on the effectiveness of their management and may expose ratepayers to unexpected renewal and replacement costs.

Paras 3.3.12 and 3.3.20 to 3.3.25

Local government performance reporting

- Despite the substantial challenges of implementing performance reporting, the local government sector leads the Victorian public sector in this area. As other elements of the public sector seek to improve their performance reporting practices, the lessons learnt by the local government sector will provide a helpful guide to those that follow the path of comprehensive performance reporting.

Paras 3.3.35 to 3.3.67

- Public accountability now requires more than just audited financial outcomes and other general information on operations in annual reports. Externally reported performance-based information is an essential obligation of all public sector entities, including local government, to achieve an adequate level of accountability to the community.

Paras 3.3.64 to 3.3.67

Property valuations used for rating purposes

- During 2000, all rateable properties were required to be valued for municipal rating and other State taxing purposes. Contract and time management, together with a shortage of appropriately skilled valuers, emerged as some of the key issues identified during the 2000 valuation process.

Paras 3.3.68 to 3.3.91

- The adoption and use by municipal councils of the year 2000 property valuations for rating purposes without the Valuer-General's certification as to the truth and correctness of the valuations and the Minister's declaration that the valuations were suitable for adoption and use, pursuant to the *Valuation of Land Act* 1960, was imprudent.

Paras 3.3.93 to 3.3.99 and 3.3.117 to 3.3.122

- It is estimated that some 93 000 rate notices (4 per cent) issued by municipal councils resulted in a query by ratepayers. Approximately 44 000 rate notices have been subject to a supplementary valuation to correct deficiencies in the 2000 valuation process. In addition, some 18 900 rate notices were subject to a formal objection.

Paras 3.3.103 to 3.3.105

JUSTICE **Page 205**

Metropolitan Women's Correctional Centre

- In November 2000, the Government reached an agreement with the contractor to transfer the ownership and management of the Metropolitan Women's Correctional Centre at Deer Park to the public sector as the defaults under the contract were persistent and continuing in nature, and the operator could not ensure the safety and wellbeing of prisoners, staff and visitors.

Paras 3.4.47 to 3.4.55

- The settlement amount was $20.2 million, consisting of $17.8 million to purchase the Centre's buildings, infrastructure and chattels, and $2.4 million to finance the costs associated with terminating the loan facility.

Paras 3.4.47 to 3.4.55

- In response to the Government's drive for significant cost savings from outsourcing, the Department in selecting the original service provider for the Centre, placed considerable emphasis on the financial evaluation criteria used to ensure cost savings and less emphasis on the capacity of the contractor to effectively manage and operate the facility. This emphasis on cost savings was one of the factors contributing to the problems encountered at the Centre.

Paras 3.4.61 to 3.4.70

Estate Agents Guarantee Fund

- Approximately $8.4 million is anticipated to be expended from the Estate Agents Guarantee Fund during the year. This is significantly less than the $28.4 million in revenue expected to be generated by the Fund, resulting in a budgeted surplus of almost $20 million for the 2000-01 financial year.

Paras 3.4.110 to 3.4.118

- The net assets held in the Fund as at 30 June 2000 totalled $99.9 million. In these circumstances, the Parliament could consider amendments to the Act in order to broaden the criteria for grant payments.

Paras 3.4.110 to 3.4.118

NATURAL RESOURCES AND ENVIRONMENT Page 243

Automation of the Land Titles Register

- The current titles automation project at the Land Registry was initially scheduled for completion in March 2000. However, this target was subsequently revised to April 2002.

Paras 3.5.39 to 3.5.44

- The project is expected to cost $91.6 million, an increase of $29.4 million or 47 per cent from the original cost estimate.

Paras 3.5.45 to 3.5.51

Wind-up of the Victorian Dairy Industry Authority

- The Victorian Dairy Industry Authority (VDIA) ceased operating in October 2000, at which time its net assets were distributed to Dairy Food Safety Victoria and a private company known as the Geoffrey Gardiner Dairy Foundation. The VDIA transferred net assets amounting to $62.6 million to this private company.

Paras 3.5.81 to 3.5.94

- Although the Foundation is required to table audited annual financial reports in the Parliament, no independent review mechanism has been established to ensure that the funds transferred to the company are spent in accordance with the intentions of Parliament as outlined in the *Dairy Act* 2000.

Paras 3.5.87 to 3.5.94

- In April 2000, the VDIA sold its interest in a joint venture arrangement involving the manufacture and marketing of Big M milk products in China. The VDIA received $50 000 from the sale which was $342 000 less than the value of the VDIA's share of the net assets of the joint venture. The overall cost to the VDIA as a result of its involvement in the joint venture was in excess of $2 million.

Paras 3.5.100 to 3.5.106

- In September 2000, the Big M brand was sold to National Foods and the REV, Skinny Milk and Farmhouse brands were sold to Parmalat Foods. The sale of the brands generated $57.2 million for the VDIA, with costs associated with the sale process amounting to $686 000.

Paras 3.5.95 to 3.5.99

NATURAL RESOURCES AND ENVIRONMENT *- continued* Page 243

Buy-out of bay and inlet commercial fishing access licences

- The Department of Natural Resources and Environment initiated a licence buy-out scheme which resulted in the removal of more than half of the commercial fishing licences for Victorian bays and inlets for an average purchase price of $74 000. The voluntary buy-back scheme, which cost $8 million, will be ultimately funded by the $20 recreational licence for anglers.

  Paras 3.5.130 to 3.5.142

- The primary objective of the buy-out was to obtain the voluntary surrender of the maximum number of licences without affecting commercially caught fish supplies. The buy-out is expected to have negligible impact on the commercial fish catch in bays and inlets, with the exception of Shallow and Anderson's Inlets, and has not directly addressed recreational fishers' concerns with net fishing.

  Paras 3.5.159 to 3.5.165

- The method chosen for the buy-out has created significant differences in the benefits received by fishers in different locations.

  Paras 3.5.166 to 3.5.170

- The Fisheries Co-Management Council's 1997 Review indicated that the sustainable future of bay and inlet fisheries were more seriously threatened by habitat and environmental degradation than by current recreational or commercial fishing activities. ***Paras 3.5.171 to 3.5.174***

Alpine resorts land stability

- The Government, through the Department of Natural Resources and Environment, initiated a comprehensive review of land stability at all 6 of Victoria's alpine resorts during 1997-98. Of the 660 sites assessed, 76 were rated as either a high or very high hazard. ***Paras 3.5.179 to 3.5.198***

- High and very high hazard sites requiring urgent attention were managed at acceptable levels by the June 2000 snow season following the undertaking of remedial work, and it is anticipated that the remaining remedial work will be completed by mid-2002.

  Paras 3.5.199 to 3.5.203

- The importance of, and need for, ongoing monitoring of not only hazardous but also potentially hazardous sites is illustrated by the collapse, in January 2001, of a significant section of the fill supporting the resort access road at Mt Baw Baw.

  Paras 3.5.204 to 3.5.207

- It was quite clear that the Thredbo disaster was the catalyst for the action taken to identify the significant hazards at the Victorian alpine resorts and the subsequent action taken to mitigate those risks.

  Paras 3.5.233 to 3.5.236

STATE AND REGIONAL DEVELOPMENT Page 323

Federation Square development

- The original cost estimate for the development of the Federation Square, set in March 1996, was $110 million. Recently revised estimates bring total costs to complete the project to around $369 million. At the date of preparation of this Report, a funding shortfall of approximately $31 million remains.

Paras 3.7.30 to 3.7.40

Melbourne Docklands development

- The Docklands Authority is still to finalise arrangements for development of 34 hectares of the Docklands precinct.

Paras 3.7.58 to 3.7.64

- In February 2001, Transurban, a private sector consortium for the financing, construction and operation of the Melbourne City Link, lodged a $35.8 million claim against the Government seeking compensation for loss of revenue associated with the construction of Wurundjeri Way, and the widening of the Westgate Freeway. Transurban considers that these developments will have a material adverse effect on traffic volume on the City Link.

Para. 3.7.81

Regional Infrastructure Development Fund

- At March 2001, the Department of State and Regional Development had approved 18 applications with funding to be provided totalling $37.7 million from the Regional Infrastructure Development Fund. In relation to the projects approved, only 3 projects related to non-government entities.

Paras 3.7.145 to 3.7.149

- More work needs to be done by the Department in terms of improving its prioritisation of projects, providing timely and complete information to applicants on the outcome of the assessment process, and establishing a performance measurement framework to assess the effectiveness of this initiative.

Paras 3.7.134 to 3.7.144 and 3.7.166

TREASURY AND FINANCE — Page 379

Financial standing of the Victorian WorkCover Authority

- During the 6-month period to 31 December 2000, the Victorian WorkCover Authority incurred an operating loss of $651 million, bringing the accumulated losses to almost $1.1 billion.

Paras 3.8.14 to 3.8.15

- The increase in the operating loss for the 6 months to 31 December 2000 has arisen due mainly to significant increases in the level of claims, the substantial reduction in investment revenue earned, and changes in economic assumptions used in the valuation of the outstanding claims liability.

Paras 3.8.16 to 3.8.19

- The Authority's consulting actuaries do not expect the WorkCover Fund to return to a fully-funded position before 30 June 2006, 3 years later than intended when the amending legislation was enacted in May 2000.

Paras 3.8.20 to 3.8.21

- The common law component of the outstanding claims liability had increased by around 138 per cent from $630 million to over $1.5 billion since 30 June 1998, with the majority of the increase taking place during the 2000 calendar year.

Paras 3.8.27 to 3.8.28

Motor vehicle fleet management by Department of Treasury and Finance

- In May 2000 the Department of Treasury and Finance assumed responsibility for providing fleet management services to those agencies previously contracted to LeasePlan. The Department had not determined the ongoing costs associated with providing fleet management services and, therefore, was not in a position to determine whether it should continue to provide such services in the future.

Paras 3.8.52 to 3.8.62

TREASURY AND FINANCE - *continued* Page 379

State Revenue Office information technology systems

- Over the past 3 years, the State Revenue Office (SRO) has embarked on a comprehensive information technology development project involving the key revenue systems of the State of Victoria. The project is currently in the critical phases of testing and final implementation. The progress made in these final phases and the extent of any significant issues encountered at this stage will ultimately determine the success of the SRO in implementing effective revenue collection systems.

  Paras 3.8.65 to 3.8.98

- The SRO, under a current policy, does not allow credit card payment options by taxpayers. In light of the current trends toward e-commerce and the increasing usage by consumers paying by credit card, the appropriateness of the current policy may require review.

  Paras 3.8.94 to 3.8.95

BROAD SCOPE ISSUES Page 417

Performance reporting in the budget sector

- Considerable progress has been made by the Government in implementing a new performance management and reporting framework for the budget sector. The framework is not yet sufficiently developed for audit opinions to be issued regarding the relevance, appropriateness and fair presentation of performance information.

  Paras 4.1.14 to 4.1.19

- The output measures incorporated in the Government's Budget Papers may not be the most appropriate indicators of departmental performance.

  Para. 4.1.34

Part 2

Parliament of Victoria

Part 2.1

Parliament of Victoria

KEY FINDING

- The audit of the financial statements of the Parliament of Victoria was satisfactorily concluded.

Paras 2.1.1 to 2.1.5

SUMMARY OF AUDIT RESULTS

2.1.1 The Parliament, as the law-making body of the State, provides the base from which the Government is formed. It is composed of the Crown (represented by the Governor), the Legislative Council and the Legislative Assembly, which collectively form the legislature. The scrutiny and deliberative roles of the Parliament are complemented by a number of committees, the role of which is to inquire, investigate and report upon proposals or matters referred to them by either House or by the Governor-in-Council, or in certain circumstances, upon a self-initiated reference.

2.1.2 The administrative support services of the Parliament and the associated Committees are provided by 5 parliamentary departments, namely, the Legislative Council, the Legislative Assembly, Parliamentary Debates (Hansard), the Parliamentary Library and Parliamentary Services. The primary function of these departments is to service the 2 Houses and associated committees, as well as to provide administrative support for Members and electorate offices.

Finalisation of financial statements

2.1.3 While no reporting requirements are established in legislation in relation to the administrative operations of the Parliament, under a standing arrangement with the presiding officers of both Houses, my Office undertakes an annual audit of the financial statements of the Parliament (which comprises the 5 parliamenrary departments), which are prepared consistent with the requirements of the *Financial Management Act* 1994.

2.1.4 Under recent amendments to the *Constitution Act* 1975, the Victorian Auditor-General's Office now forms part of the Parliament. The financial reporting requirements of the Office are set out in section 7B of the *Audit Act* 1994, which provides that, as soon as practicable after the end of each financial year, the Auditor-General must prepare financial statements which comply with section 49 of the *Financial Management Act* 1994 and provide them to the independent auditor appointed by the Parliament for auditing. The Auditor-General must then, as soon as practicable, cause an annual report which includes a report of operations and the audited financial statements, to be transmitted to each House of the Parliament.

2.1.5 During the 1999-2000 financial audit cycle, confirming audit opinions were issued on the financial statements prepared by the Parliament of Victoria and the Victorian Auditor-General's Office. Schedule A to this Part of the Report outlines the timing of the finalisation of the financial statements and the issue of the audit opinions.

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS

Entity	*Financial statements signed by entity*	*Audit report signed*	*Clear opinion issued*
COMPLETED AUDITS			
FINANCIAL YEAR ENDED 30 JUNE 2000			
Parliament of Victoria	2 Oct. 2000	18 Oct. 2000	✓
Victorian Auditor-General's Office *(a)*	16 Aug. 2000	16 Aug. 2000	✓

(a) The Victorian Auditor-General's Office was audited by a firm of private auditors appointed by the Parliament.

Part 3

Audit of Ministerial Portfolios

Part 3.1

Education, Employment and Training

KEY FINDINGS

Status of the Bio21 project

- The State entered into a contract in October 2000 with The University of Melbourne, the Walter and Eliza Hall Institute of Medical Research and the Royal Melbourne Hospital to undertake and assist in the commercial development of bio-medical research. Total funding of up to $159.5 million was available to this project, known as Bio21.

  Paras 3.1.29 to 3.1.32

- Given that the majority of the ownership and the risks of the Bio21 project will rest with public sector agencies, consideration needs to be given to the level of accountability for Bio21 Australia Limited (the company established to implement the project) to Parliament and, ultimately, to Victorian taxpayers. As Parliament's auditor, it will be important that the Auditor-General is involved in this accountability process.

  Paras 3.1.37 to 3.1.39

Melbourne University Private Limited

- Melbourne University Private Limited (MUPL) was established in January 1998 as a public company limited by shares. Although the original intention was to seek other investors, The University of Melbourne is currently the only investor.

  Paras 3.1.52 to 3.1.54

KEY FINDINGS - *continued*

Melbourne University Private Limited - *continued*

- In July 2000, MUPL entered into a 5-year agreement with The University of Melbourne to lease 7 000 square metres of floor space over 4 levels, within one of the buildings of the University Square complex. Since entering into the leasing agreement, a number of factors including lower than expected growth have reduced MUPL's floor space requirements. MUPL is currently re-negotiating the lease agreement with a view to occupying only around 30 per cent of the original leased space.

  Paras 3.1.55 to 3.1.58

- MUPL has incurred significant losses since its establishment. For the year ended 31 December 2000, MUPL reported an operating loss of $2.2 million.

  Paras 3.1.69 to 3.1.72

- In October 2000, The University of Melbourne decided to consider a proposal to merge the activities of MUPL and Melbourne Enterprises International Limited (MEI) and, in May 2001, it agreed that the proposed merger should proceed.

  Paras 3.1.77 to 3.1.84

- In order to improve the outcomes from the proposed merger, it is important that The University of Melbourne ensure that detailed business plans currently being developed for the merged operations of MUPL and MEI incorporate a detailed risk analysis and are comprehensively reviewed by The University of Melbourne.

  Paras 3.1.77 to 3.1.84

Financial viability of TAFE institutes

- Five public sector TAFE providers were considered to be operating under financial difficulties as at 31 December 2000. ***Para. 3.1.91***

- The Chisholm Institute of TAFE did not pay its suppliers in accordance with government guidelines and experienced cash flow problems that required advance funding of $2 million from the Office of Post Compulsory Education, Training and Employment in December 2000 to enable the payment of both suppliers and staff.

  Paras 3.1.92 to 3.1.95

- In the context of corporate governance of a public institution, it is of concern that the Council of the Chisholm Institute of TAFE did not ensure that adequate strategic financial planning was undertaken, and that sufficiently robust monitoring and accountability processes were put in place. ***Paras 3.1.103 to 3.1.111***

KEY FINDINGS *- continued*

School Global Budget

- The method used to calculate School Global Budgets (SGB) changed for the 2001 school year which was designed to achieve greater transparency and equity in the funding of schools.

  Paras 3.1.193 to 3.1.194

- The Office of Schools has identified 590 schools (36 per cent) requiring transition funding, that is, actual salary costs are forecast to be greater than the funding allocation, based on the formula under the new SGB model. DEET has provided transition funding of $28 million for the 2001 school year.

  Paras 3.1.160 to 3.1.186

- Even though the leadership profiles (principal, assistant principal and leading teachers) of secondary schools are higher than for primary schools and, accordingly, the actual cost per teacher in secondary schools is greater than in primary schools, the SGB funding formula is based on a standard salary cost for all teachers (other than principals) irrespective of whether they are primary or secondary.

  Paras 3.1.160 to 3.1.186

- For schools to operate in future within the resources provided under the SGB funding model, principals of secondary schools in particular will need to significantly alter their staffing profiles.

  Paras 3.1.193 to 3.1.194

- Ultimately, the school funding model should be directed to linking resources to the educational needs of students. The level of resources provided and the staffing profiles of schools should move over time to more adequately reflect the learning needs of students in different stages of schooling across both primary and secondary schools.

  Paras 3.1.193 to 3.1.194

SUMMARY OF AUDIT RESULTS

3.1.1 The Department of Education, Employment and Training was created in its present form through the amalgamation of the former Department of Education and the respective areas responsible for Employment and Youth Affairs within the Departments of State and Regional Development, and Human Services. The Department of Education, Employment and Training delivers education and training services from preparatory through to post-compulsory education. The Department provides services within 3 broad portfolio areas of school education, tertiary education and training.

3.1.2 Significant aspects of the Department's operations include the management of:

- Schools – the delivery of school education for students in the compulsory years (Prep to Year 10) of schooling and students participating in the Victorian Certificate of Education (VCE). Departmental assistance is provided to schools to assist with the implementation of government education and related training policies;
- Post-compulsory education and training – organisational arrangements for the State training system, including identifying training needs, allocating resources, establishing industry training practices, negotiating performance agreements with Technical and Further Education (TAFE) institutes and industry training boards to facilitate the allocation of resources to be utilised in the provision of training, and undertaking system capital planning;
- Higher education – co-ordination, planning and monitoring of higher education within Victoria and legislative processes for accreditation and approval of higher education programs by private providers, and endorsement of programs for overseas students;
- Employment – initiatives to improve employment opportunities for targeted groups of unemployed Victorians, research and collation of labour market information to assist with business planning, assessment of overseas qualifications and provision of vocational information to migrants to Victoria; and
- Youth – policy advice to the Minister for Youth Affairs and to government, and a leadership and an advocacy role in co-ordinating youth service delivery.

3.1.3 Three Ministers, namely, the Minister for Education, the Minister for Post Compulsory Education, Training and Employment, and the Minister for Youth Affairs have responsibility for operations within the Education sector. These Ministers have collective responsibility for the Department of Education, Employment and Training.

3.1.4 Details of the specific ministerial responsibilities for public bodies within the Education sector are provided in Table 3.1A. These public bodies, together with the Department of Education, Employment and Training, were subject to audit by the Auditor-General during the 1999-2000 financial year.

TABLE 3.1A
MINISTERIAL RESPONSIBILITIES FOR
PUBLIC BODIES WITHIN THE EDUCATION, EMPLOYMENT AND TRAINING SECTOR

Ministerial portfolio	*Entities subject to audit*
Education	Board of Studies
	Telematics Course Development Fund Trust
Post Compulsory Education, Training and Employment	Adult, Community and Further Education Board Council of Adult Education
	Driver Education Centre of Australia Ltd
	International Fibre Centre Ltd
	International Training Australia Pty Ltd
	Post-compulsory education institutions:
	universities (8) and associated companies, trusts and foundations (69)
	institutes of technical and further education (14) and associated companies (6).
	State Training Board
	Victorian Tertiary Admission Centre
Youth Affairs	-

3.1.5 The annual reporting and audit requirements for entities within the portfolio are set out in the *Financial Management Act* 1994 and the *Audit Act* 1994. In particular, under section 45 of the Financial Management Act, each department and public body must submit its annual financial statements to the Auditor-General within 8 weeks of the end of the financial year. Under the Audit Act, the Auditor-General is then required to audit the financial statements within 4 weeks of their receipt. Finally, within 4 months of the end of the financial year or the next sitting day after the end of the fourth month, the relevant Minister is required to table in each House of the Parliament the annual report of each entity, which includes a report of operations and the audited financial statements.

Nature of audit opinions issued

3.1.6 During the 1999-2000 financial audit cycle, 90 confirming audit opinions were issued on financial statements prepared by portfolio entities, with 11 financial statements subject to audit qualification. Schedule B to this Part of the Report outlines the audit opinions issued in respect of portfolio entities during the audit cycle.

3.1.7 In the Education portfolio, the 2 major reasons for the issue of qualified audit opinions related to the recognition of revenue and unfunded superannuation contributions.

3.1.8 *Revenue recognition* - The qualifications made in respect of inappropriate recognition of revenue occurred mainly in relation to the non compliance of the particular entities with Australian Accounting Standard AAS 15 – *Revenue,* which requires that any income received by or due to an entity must be treated as income in the accounts of the recipient in the year of receipt, when the grants are regarded as non- reciprocal in nature. In the case of 7 education entities where the grants were of a material size and non-reciprocal in nature and were recorded as current liabilities rather than recognised as revenue in the year of receipt, a qualified audit opinion was issued.

3.1.9 *Unfunded superannuation contributions* - In the case of all 8 universities the audit opinion issued on their financial statements were qualified on the grounds that they had inappropriately recognised a receivable from the Commonwealth Government for the universities' unfunded superannuation liabilities. As the universities do not exercise control over the future Commonwealth Government funding associated with unfunded superannuation liabilities, a right to these funds should not have been recognised as an asset in the universities' balance sheets.

Timeliness of financial reporting

3.1.10 As previously mentioned, the legislative framework requires the audited financial statements of public sector agencies to be completed within 12 weeks after the end of the relevant financial year. Table 3.1B illustrates the performance of portfolio agencies in meeting this statutory requirement during the 1999-2000 reporting cycle.

TABLE 3.1B
TIMELINESS OF FINALISATION OF AUDITED FINANCIAL STATEMENTS, EDUCATION, EMPLOYMENT AND TRAINING PORTFOLIO *(a)*

	Entities	
Number of weeks after end of financial period	*Number*	*Per cent (cumulative)*
Less than 8 weeks	1	1
8 to 10 weeks	3	4
10 to 12 weeks	12	15
12 to 14 weeks	39	53
14 to 16 weeks	10	62
Over 16 weeks *(b)*	42	100

(a) This table does not include financial statements of entities for the 1998–99 financial year that were signed during the current audit cycle.

(b) Includes 6 entities where the audited financial statements are yet to be finalised.

3.1.11 The table demonstrates that there is scope for improvement in the timeliness of completion of audited financial statements, with 15 per cent of entities meeting the 12 week legislated completion timeframe. The audited financial statements of the majority of the remaining entities were available within 4 weeks of the legislated completion timeline (i.e. within 16 weeks of year-end).

3.1.12 Timeliness of reporting is an essential characteristic of quality information and the effectiveness of the accountability process. Accordingly, it is important that avenues are identified and pursued to improve the timeliness of the financial reporting process.

Restructure within the portfolio

3.1.13 A restructure of post-compulsory education was commenced in 2000. Legislation was introduced to create a single qualifications body, – the Victorian Qualifications Authority, that will be responsible for accrediting all public qualifications except higher education. In addition, the Learning and Skills Commission will be set up to replace the State Training Board and the Victorian Board of Studies will become The Victorian Curriculum and Assessment Authority.

3.1.14 The restructure also includes the establishment of *Learning and Employment Skills Networks*. The networks are intended to assist schools to work more effectively with other education and training organisations, industry and local government in supporting young people to take up education and training opportunities.

Losses, thefts and irregularites

3.1.15 Table 3.1C summarises particulars of losses, thefts and irregularities, including property damage, which occurred in 2000 and were reported to our Office by entities within the Education, Employment and Training sector.

TABLE 3.1C
LOSSES, THEFTS AND OTHER IRREGULARITIES
($'000)

Item	*Amount*
Department of Education, Employment and Training -	
Equipment and property damage caused by fire	3 200
Theft, burglary and vandalism	1 970
Technical and Further Education Institutes -	
Thefts	300
Universities -	
Thefts	1 200

3.1.16 The table identifies that substantial financial losses were incurred, which resulted from numerous instances of theft and burglary, particularly relating to computers and other electronic equipment stolen from a significant number of schools and universities.

3.1.17 In addition, the Department of Education, Employment and Training reported a number of fires at schools. In the majority of cases, the suspected cause was arson and police were notified. The major instances of fire and associated damages were:

- Brighton Secondary College ($1.2 million);
- Coatesville Primary School ($750 000); and
- Healesville Primary School ($600 000).

STATUS OF Bio21

3.1.18 Biomedical research is said to be at the forefront of scientific investigation following advances in knowledge about genetics and in the application of this knowledge to health care. As a result, a major challenge facing the scientific research community is to capture the financial and other benefits that may flow from that research effort.

3.1.19 The Department of State and Regional Development has recognised the importance of biomedical developments as part of its science, technology and innovation programs. The objectives of these programs relevant to biomedical research include building world-class research infrastructure, developing the State's skills base, fostering a culture of innovation, and positioning Victoria as a national and world-class leader of science.

3.1.20 The University of Melbourne has also recognised the importance of biomedical advances. In early 1999, the University established a working party to consider how it might best capitalise on emerging opportunities. The working party identified the urgent need for the University to develop biotechnology strategic plans in response to the ongoing genomics and related technological revolution.

Proposal by the University

3.1.21 In March 1999, the University of Melbourne approached the Government for assistance in relation to a proposal referred to as Bio21. The project involved the creation of a world-class precinct in Australia to specialise in health-related biotechnology. The Bio21 proposal called for approval by the Government, by 30 June 2000, of matching funding of $30 million to satisfy a condition imposed by a private foundation for a donation of $30 million to be made to the University.

3.1.22 The project proposed a partnership with the Walter and Eliza Hall Institute, a renowned medical research agency, and Melbourne Health, and a collaboration with affiliated universities, institutes, industry and governments. The partnership offered unique opportunities to develop synergies between the University's life science and technology groups and relevant hospital and biomedical institute groups.

3.1.23 A key element of the University's proposal was the creation of the Bio21 Molecular Science and Biotechnology Institute to be located within a purpose-built building in the western precinct of the University's Parkville campus. Total costs to construct this facility were estimated at around $100 million.

3.1.24 The Institute was to have direct links to a number of research groups and a Bio21 commercial centre. The Institute was also to accommodate the research groups of the University's Departments of Chemistry and Biochemistry and Molecular Biology, and provide space to the wider University community and to external research organisations on a commercial basis.

Initial planning for the project

3.1.25 The Minister for State and Regional Development agreed to consider the University's proposal in the context of the Government's Biotechnology Strategic Plan, which was under development at the time, and on the basis that any government commitment would be dependent on the preparation of a satisfactory business case.

3.1.26 In March 2000, consultants were jointly engaged by the University and the Department of State and Regional Development to prepare a strategic business plan to outline the parameters for the successful implementation of the project.

3.1.27 The consultants reported in April 2000 that while Bio21 was a highly speculative venture, the project potentially offered substantial financial and other benefits such as:

- assisting to overcome certain challenges faced by the Australian biotechnology industry including:
  - access to finance;
  - a relatively small research sector compared with other countries;
  - a comparatively small domestic market and the distance from other key international markets; and
  - the management of intellectual property;
- providing world-class research facilities for projects with commercial potential; and
- offering significant economic benefits to the State comprising:
  - creation of around 5 to 10 new businesses each year resulting in an estimated investment in Victoria of $30 million per annum;
  - increased employment through directly creating around 100 new jobs per annum and indirectly generating further new employment;
  - attraction of spin-off companies and related industries; and
  - generation of significant exports by Bio21 businesses, and attracting and retaining the world's best scientists and innovation managers.

3.1.28 Despite the potential benefits, the consultants also concluded that the risks associated with the initial stages of such a venture would be high as the projected commercial cash flows would be uncertain and income may not arise until some years in the future. Given this, the support of the Government, together with the private donation, was considered critical in the first 5 years of the project. However, the consultants did not envisage a need for ongoing financial support from the Government as the market capitalisation of biotechnology companies would be likely to continue to improve and the initial current funding would provide sufficient "seeding" capital to commence the development and to continue research projects in the biotechnology area.

Funding of the project

3.1.29 Following consideration of the consultants' report, in May 2000, the Government's Economic Development Committee recommended to Cabinet that the Government provide support of $50 million in land and cash to the Bio21 project. This amount represented $30 million to satisfy the condition of the private donor for matching funding and an additional $20 million to facilitate the implementation of the project. In addition, if within 3 years, management of the Bio21 project could prove a need for utilising the existing site of the Royal Dental Hospital in Parkville, the Government may also grant that site to the University (currently valued at $16 million).

3.1.30 The Government formally approved the $50 million contribution to Bio21 in June 2000 subject to:

- achievement of certain milestones, including the commencement of the construction of the Bio21 Molecular Science and Biotechnology Institute's complex by 30 June 2001 and its completion within 36 months; and
- funding commitments to the project of $80 million by the University (which includes $30 million provided by a private foundation) and $4 million by the Walter and Eliza Hall Institute.

3.1.31 In July 2000, the Commonwealth Government also approved a $9.5 million grant to the University tied directly to the building of the new Biotechnology Institute.

3.1.32 Based on the above arrangements, **total funding of up to $159.5 million was available to the project** for the applications summarised in Table 3.1D.

TABLE 3.1D
FUNDING FOR THE Bio21 PROJECT
($million)

Source of funding	*$m*	*Application of funding*
State Government	15	Contribution towards construction of building to house the Bio21 Molecular Science and Biotechnology Institute.
	16	Draw-down facility for Bio21 projects to be funded from the Department of State and Regional Development's science, technology and innovation budget between July 2001 and June 2004.
	15	Value of land transferred to the University relating to the Veterinary Science Precinct.
	4	Development of a Proteomics Facility at the Royal Melbourne Hospital.
	16	Site value of Royal Dental Hospital in Parkville (subject to proof of need for the site within 3 years).
University of Melbourne		
• Contribution from proceeds of sale of Melbourne IT	45	$80 million represents University's share of construction of new facilities and other costs of the Bio21 project.
• Allocation from University funds	5	
• Private donation	30	
Commonwealth Government	9.5	Construction of new Bio21 Molecular Science and Biotechnology Institute.
Walter and Eliza Hall Institute of Medical Research	4	Contribution towards the development of a Proteomics facility.
Total project funding	**159.5**	

Agreement between the State and Bio21 partners

3.1.33 **The State entered into a Heads of Agreement in June 2000, with the University of Melbourne, the Walter and Eliza Hall Institute of Medical Research and the Royal Melbourne Hospital, to undertake and assist in the commercial development of bio-medical research.** The parties subsequently entered into a formal contract in October 2000. The key terms of the contract are as follows:

- A concept design of the proposed facilities, incorporating the results of certain feasibility studies, are required to be prepared and must be assessed by the State as satisfactory;

- A corporate structure is to be established for the project comprising:
  - Bio21 Corporate, initially to be equally owned by the University, Walter and Eliza Hall Institute of Medical Research and Melbourne Health (registered in February 2001 as Bio21 Australia Limited, a company limited by guarantee) to attract new and permanent membership of the company and to promote and facilitate collaborative research;
  - Bio21 Commercial, a subsidiary of Bio21 Australia Limited, to be responsible for the development and commercialisation of intellectual property created from the research activities of the project and to assist local companies in obtaining access to financial expertise and international markets;
  - constitutions and corporate governance arrangements for both corporate bodies to be established that meet the requirements of the State, including guidelines for managing the different intellectual property policies of each partner in Bio21 in a manner which will facilitate the commercialisation of research outcomes of the project; and
  - the boards of management of the 2 entities to comprise a mix of scientific, business and industry representatives appointed following consultation with the State;
- All agreements for the construction of the University's building to house the Institute of Biomolecular Science and Technology require the approval of the Minister for Planning; and
- A 5 year business plan is to be developed by Bio21 Australia Limited to demonstrate that Bio21 will be able to attract and retain leading universities and research institutions and be financially viable over the long-term.

3.1.34 As part of the agreement, Bio21 Australia Limited and the Bio21 Commercial partners have undertaken to:

- use the State Government funds provided to it under the agreement solely to implement the Bio21 project;
- prepare and provide to the State an annual report which compares and measures performance of the Bio21 project against the business plan; and
- jointly and severally, indemnify the State against any claim arising from the implementation of the Bio21 project.

3.1.35 In order to maximise the economic benefits from the project and to the State, Bio21 Commercial is to establish strong links with local and international industry, select and develop commercialisation projects, which are likely to achieve such benefits and secure sufficient funding for commercialisation projects from the initial stages of their development up to their readiness for professional investment.

3.1.36 **The management framework provided for the Bio21 project under the agreements should, if effectively implemented, provide an appropriate basis for the ongoing monitoring of the project from both a University and State Government perspective.**

Public accountability for Bio21

3.1.37 The constitution of Bio21 Australia Limited provides for the Board of the company to ensure that the annual financial statements, and the Director's and Auditor's reports are prepared in accordance with the Corporations Law. Under these requirements, the auditor of Bio21 Australia Limited will be appointed by the Board as provided under the Corporations Law.

3.1.38 Both the University of Melbourne and Melbourne Health, 2 of the 3 equal members of Bio21 Australia Limited, are currently subject to audit by the Auditor-General under the requirements of the *Audit Act* 1994, and are required to table an annual financial report in the Victorian Parliament.

3.1.39 **Given that the majority of the ownership and the risks of the Bio21 project will rest with public sector agencies, consideration needs to be given to the level of accountability for Bio21 Australia Limited to the Parliament and, ultimately, to Victorian taxpayers. As Parliament's auditor, it will be important that the Auditor-General is involved in this accountability process.**

Current status of Bio21

3.1.40 The project will comprise 2 stages:

- *Stage 1*, involving construction of 2 new buildings at the University of Melbourne in the western precinct corner of Flemington Road and Park Drive (previously the Veterinary Science Precinct). The construction project is estimated to cost \$105 million and is scheduled to commence by 30 June 2001 with completion expected within 3 years. One of these buildings will house the Bio21 Institute, the second building will be available to the private sector to start up "incubator" businesses. Stage 1 will also include an extension to the Walter and Eliza Hall Institute of Medical Research located in the Royal Melbourne Hospital building in Parkville and development of a Clinical Trial Centre at the Hospital; and
- *Stage 2*, involving construction of additional facilities on the existing site of the Royal Dental Hospital if Bio21 participants can prove a need for this development.

3.1.41 In November 2000, the Victorian Parliament passed legislation, namely, the *University of Melbourne (Land Act)* 2000, providing the University with the right to develop the land in its Veterinary Science Precinct. This legislation repealed a previous restricted Crown Grant, which had limited the use of the precinct to veterinary teaching and a veterinary hospital. The University and the Minister for Agriculture previously managed the site jointly. Under the new legislation, the land has been provided solely to the University for the purposes of education, research and development in the fields of science and biotechnology.

3.1.42 As referred to previously, the University is required to contribute $80 million to the project. The University has decided that this contribution will be made up of $45 million from the proceeds of the float of Melbourne IT Limited, the private donation of $30 million made to the University (of which $6m has been received) and $5 million from the University's reserve investment funds. In addition to this required contribution, in July 2000 the Commonwealth Government provided $9.5 million to the University tied directly to the building of the new Biotechnology Institute.

3.1.43 At the date of preparing this Report, a community consultation program had commenced concerning construction of Bio21 facilities and an architect and cost planner had been appointed to the project. In addition, site preparation has commenced as a prelude to the commencement of construction prior to 30 June 2001.

Operational issues confronting Bio21

Management of intellectual property

3.1.44 The April 2000 consultancy report identified that it was critical to the success of the Bio21 project that appropriate intellectual property policies are designed and implemented to facilitate commercialisation.

3.1.45 Ownership of intellectual property is a difficult issue confronting a number of industries. A discussion paper on the *Ownership of intellectual property in higher educational institutions*, issued by the Australian Vice-Chancellors' Committee in 1995, outlined a wide range of objectives to be considered in developing a related policy including:

- promoting the fundamental objectives and purpose of an institution in teaching, research and further knowledge of its own sake;
- protecting the integrity and welfare of an institution;
- obtaining appropriate return for the use of facilities, resources and services provided by an institution outside the mainstream activities of teaching and research;
- encouraging and developing institutional growth, progress and success through ventures with industry and commerce in mainstream and peripheral activities for full commercial return;
- providing fair and reasonable remuneration for staff and students in return for profitable and sound performance;

- providing incentives for staff and students in developing and applying intellectual activity in the fields of industry, commerce, science, literature and the arts;
- attracting and retaining the highest quality staff; and
- increasing accountability for management and use of public funds.

3.1.46 The discussion paper goes on to list factors, which would support an institution's claim to ownership of intellectual property, including that the property was created:

- in the course of employment;
- through substantial use of institutional resources and/or services;
- through use of pre-existing intellectual property owned by an institution; and
- use of institutional funding or funding obtained by an institution.

3.1.47 At this stage, the Bio21 participants have not developed a uniform policy in relation to intellectual property rights but instead are relying on the individual policies of each participant. In this respect, the University recently adopted a new policy concerning intellectual property rights. Under this new policy, the University is entitled to receive 5 per cent of the proceeds resulting from the successful commercialisation of research falling between the range of $50 000 and $1 million, and 15 per cent where proceeds exceed $1 million. However, the share of proceeds retained by the University under this policy is less than the share retained by other Australian universities, with their share of proceeds ranging between 25 and 50 per cent, under their intellectual property policies.

3.1.48 The participants of Bio21 project have agreed that each party is to appoint an individual with the responsibility and authority to negotiate commercial and intellectual property matters with Bio21 Australia Limited. Each party is to support the implementation of intellectual property guidelines and policies for Bio21 Australia Limited in a manner, which will facilitate the commercialisation of research outcomes of the Bio21 project.

Funding and distributions by Bio21 Australia Limited

3.1.49 Ongoing funding of Bio21 Australia Limited is estimated to cost up to $2 million per annum to be funded by the participants of the Bio21 project on an equal basis. A funding agreement between Bio21 Australia Limited and the agencies participating in the project provides that all funds received from the participating agencies are to be recorded by Bio21 Australia Limited as a loan. Any loans and related interest (at the long-term government bond rate plus 2 per cent) are required to be repaid by Bio21 Australia Limited before any other distributions to owners from the earnings of the company.

3.1.50 The method of allocation of distributions from Bio21 Australia Limited is to be determined by the participating interest (33.3 per cent for each participant). While the structure proposed would limit distributions to specified members (initially the founding participants), declaration of dividends or distributions is to be made by the board of Bio21 Australia Limited. In the case of Bio21 Commercial, any dividend would be payable to its shareholders (initially owned by Bio21 Australia Limited).

Overall conclusion

3.1.51 The potential commercial opportunities arising from biotechnology in general and the Bio21 project in particular, as highlighted in the independent consultants' report referred to previously, are widely recognised. However, a number of commercial risks and operational issues critical to the ultimate success of the Bio21 project are still in the early stages of resolution. These issues include implementing management structures within the corporate entities, the need to ensure that construction of new facilities is managed within cost targets, developing effective intellectual rights ownership policies and resolving key financial issues such as the distribution of surpluses and the ongoing funding of the corporate structure. For the potential benefits of the project to be realised, it will, therefore, be essential that the University and other participants carefully manage the ongoing planning, implementation of the project and the associated risks.

***RESPONSE** by the Acting Vice-Chancellor, The University of Melbourne*

Your Report notes that the Bio21 project involves parties other than the University of Melbourne. There were 3 parties to the Bio21 funding agreement with the State of Victoria: the University of Melbourne, the Walter and Eliza Hall Institute and the Royal Melbourne Hospital (Melbourne Health), and, at the present time, these are the 3 "Founding Members" of Bio21 Australia Limited. Under the funding agreement, Bio21 Australia Limited and the 3 partes undertake to:

> *"target and encourage the participation … in the Bio21 project of other universities and research institutions in the areas of biology, medicine, science and bioengineering research which will add value to the Bio21 project and with a view to expansion of its activities beyond the Parkville medical precinct".*

The University of Melbourne is actively pursuing this.

Under the heading "Public accountability for the Bio21 project", the Report states that "… consideration needs to be given to the level of accountability for Bio21 Australia Limited to the Parliament and ultimately to Victorian taxpayers. As Parliament's auditor, it will be important that the Auditor-General is involved in this accountability process".

The University will account to the Parliament of Victoria for its part in the Bio21 project through its Annual Report as required under the Financial Management Act 1994. It is our understanding that the other parties involved in the Bio21 project will similarly report to their "stakeholders" regarding their involvement in the project.

As part of the funding agreement with the State, the founding parties were required to form the company now known as Bio21 Australia Limited. This company has been formed under Corporations Law and, as such, the Board of the company will appoint an external auditor as required by that law.

The University recognises that, for as long as Bio21 Australia Limited is the recipient of University funds, the Auditor-General has the right, under the Audit Act 1994, to access financial documents on Bio21 Australia Limited.

IMPACT OF THE CREATION OF MELBOURNE UNIVERSITY PRIVATE ON THE UNIVERSITY OF MELBOURNE

3.1.52 Melbourne University Private Limited (MUPL) was established in January 1998 as a public company limited by shares. Although the original intention was to seek other investors, The University of Melbourne is currently the only investor, having acquired 10 million $1 shares issued from MUPL's total nominal capital of 100 million shares.

3.1.53 The University of Melbourne considered that the establishment of a private university could reduce its reliance on government funding by providing commercial opportunities, allow access to external equity and generate licence fees and royalties payable to The University of Melbourne.

3.1.54 The University of Melbourne envisaged that development of a private university would be a further element in enhancing its position as one of the "great universities of the world". It was felt that the synergy between the public and the private university, operating under the "Melbourne" brand, would add quality and dynamism to the delivery of educational services. Located within the proposed new University Square complex in Parkville, just north of the Melbourne Central Business District, MUPL would be ideally placed to have access to intellectual resources, educational infrastructure and student amenities, and was seen as integral to the creation of a major "knowledge precinct".

Lease agreement for University Square development

3.1.55 In January 2000, The University of Melbourne commenced development of University Square, a new university precinct south of the main campus in Grattan Street, Parkville. The University's engineering, science and law faculties were to occupy most of the new campus. The new university precinct, which comprises 3 main academic buildings with a total floor space of 50 000 square metres, is projected to cost $250 million and be completed by December 2001. Funding for the project is being provided through a $150 million bank loan, with the balance provided from The University of Melbourne's reserve investment funds.

3.1.56 **On 14 July 2000, MUPL entered into a 5-year agreement with The University of Melbourne to lease 7 000 square metres of floor space over 4 levels, within one of the buildings of the University Square complex, at an annual cost of $1.4 million.** Under the leasing arrangements, The University of Melbourne agreed to a loan facility of $14 million to MUPL to fund the cost of the associated fit-out works. At the date of preparation of this Report, MUPL had expended $2.1 million on design fees and fit-out costs associated with the leased space.

3.1.57 **However, since entering into the leasing agreement a number of factors have reduced MUPL's floor space requirements, namely, MUPL's lower than expected growth, and the preference by many clients to have tailor-made courses delivered at their own premises. Based on these factors, MUPL is re-negotiating the lease agreement with a view to occupying only around 30 per cent of the original leased space** at an annual cost of $200 000, around half the rate of the original lease.

3.1.58 MUPL's reduced floor space requirements may result in a potential loss of rental income of around $1 million per annum to The University of Melbourne until another occupant can be found to occupy this space. In addition, the "upmarket" fit-out arrangements, designed for executive level programs, will cost around 50 per cent more per square metre to that proposed for the balance of the building space in the University Square development. As 3 levels of the proposed MUPL occupancy will now revert to The University of Melbourne, $3 million in "upmarket" fit-out costs could be incurred which are no longer required. At the date of preparation of this Report The University of Melbourne was investigating ways to mitigate these additional costs.

Operating activities

3.1.59 MUPL's constitution provides it with broad powers to conduct business as a provider of educational, administrative, research and consulting services. In line with the company's aims and corporate mandate, its stated mission is to "… *provide the highest quality education and training, including degree programs, research and consulting services, specifically designed to meet the needs of our national and international clients"*.

3.1.60 The original business proposal for MUPL indicated that the programs offered would be driven by client demand. It was planned that applied courses would be offered mainly to staff of government agencies and private sector corporations, rather than to individual fee-paying students. It was anticipated that employers would pay the fees for courses and programs delivered to their staff. In addition, it was planned to offer an extensive range of advanced educational, research and consultancy services.

3.1.61 At present, MUPL operates a Professional Services Division, which has provided a strategic leadership course for middle management in the Federal Department of Defence and provides other academic courses and consultancy services. MUPL have also established 2 specialist academic schools comprising:

- The Melbourne School of Telecommunications, Multimedia and Information Technology which currently delivers a Bachelor of Software Engineering to employees of a technology company and provides quarterly in-house training for all Australian staff at a major international technology firm; and

- The Melbourne School of Energy and the Environment to service what was thought to be a rapidly growing demand for advanced education and training related to energy production, distribution and regulation, and for environmental remediation, management and control. Since July 1999, a number of professional staff have been employed to design and develop programs, courses and curriculum relevant to that industry sector. Although the School has recently undertaken certain minor training programs, its first major course is not scheduled to commence until October 2001.

Accountability and control over Melbourne University Private

Corporate governance arrangements

3.1.62 In order to protect its investment in the private university, the University of Melbourne has prescribed certain requirements under MUPL's Memorandum and Articles of Association which enable The University of Melbourne to control and oversight the activities of the private university and to protect its position in the event that private investors become members of MUPL. The Memorandum and Articles of Association cannot be altered unless authorised by the Council of The University of Melbourne.

3.1.63 The University has also ensured that it will continue to retain corporate control of MUPL as long as it continues to hold the majority of the shares. Any other investors must hold at least 10 per cent of the shares before they are entitled to appoint a member to the MUPL Board. At present, as sole shareholder in MUPL, the University Council has appointed the directors and nominated the chairperson of its Board.

Licencing Agreement

3.1.64 The Licence Agreement between The University of Melbourne and MUPL requires the private university to pay The University of Melbourne an annual licence fee of up to $1 million and royalties of up to 20 per cent of net earnings subject to the achievement of specific conditions and level of earnings. At this stage, no licence fees or royalties have been paid to The University of Melbourne, as MUPL has not been profitable and accordingly has not reached the required level of earnings.

3.1.65 The Licencing Agreement also contains a number of key provisions to protect and/or benefit The University of Melbourne, including:

- in return for the payment of licence fees and royalties, MUPL has the right to use the name "Melbourne University" but is subject to certain sanctions if the "Melbourne University" name is brought into disrepute;
- the right for the University to inspect the books of account of MUPL, in order to verify the amounts payable; and
- a requirement that the Academic Board of The University of Melbourne must approve the curriculum, a course or an academic award of MUPL.

Financial reporting obligations

3.1.66 MUPL maintains a comprehensive financial management system that is used to produce detailed reports of its financial performance, which are scrutinised by its Board of Directors.

3.1.67 Under the licencing agreement, MUPL is not required to provide The University of Melbourne with periodic reports on its financial operations throughout the year, but is required to provide a copy of its audited financial statements within 3 months after the end of each financial year. These financial statements are audited by the Auditor-General under the authority of the *Audit Act* 1994 and a copy is forwarded to the Minister for Post Compulsory Education and Employment.

3.1.68 In November 2000, The University of Melbourne established a University Subsidiaries Committee to oversight the financial and operational activities of its various subsidiaries including MUPL. **The establishment of the Committee should strengthen the monitoring of MUPL's activities and financial performance.**

Financial performance

3.1.69 Table 3.1E discloses that MUPL has incurred significant losses since its establishment. The University of Melbourne expected that MUPL would generate strong cash flows and profitability within its first 5 years of operation. However, given an operating loss of $2.2 million for the year ended 31 December 2000 and a projected loss of $4.5 million for the year ended 31 December 2001 (prior to the decision to lease less space and the decision to merge MUPL with MEI), this expectation was unlikely to be achieved. Without a significant turnaround in its operating performance, additional capital injections would be required as existing cash reserves amounted to only $4.1 million at 31 December 2000.

TABLE 3.1E
FINANCIAL PERFORMANCE OF MUPL
FROM JANUARY 1998 TO DECEMBER 2000 AND
PROJECTED FINANCIAL PERFORMANCE TO DECEMBER 2001
($'000)

	1998	*1999*	*2000*	*2001 (a)*
Revenue	421	1 122	1 506	3 179
Expenses	1 509	2 473	3 735	7 718
Operating loss	(1 088)	(1 351)	(2 229)	(4 541)
Net assets	8 911	7 560	5 331	*(b)*

(a) Based on revised budget forecasts for the year ended 31 December 2001, prior to the decision to lease less space and the decision to merge MUPL with MEI.

(b) Net assets at 31 December 2001 will be dependent on level of capital injections by The University of Melbourne during the year.

3.1.70 A key aspect adversely affecting MUPL's financial performance was the shortfall in demand for the courses and services on offer in comparison with what was envisaged under the original business plan. For example, the Professional Services Division has only undertaken a limited number of projects and although the Communications School is starting to have some success in conducting a number of courses, total award enrolments are less than anticipated.

3.1.71 Another issue confronting MUPL is that the unique and specialised nature of many of the planned courses results in substantial costs associated with developing course material and curriculum. MUPL's ambitious business plans, which involved the development of many courses simultaneously, have resulted in large development costs being incurred. These factors are exacerbated by the long lead times involved before a course can be marketed to clients in order to generate revenue streams and recoup the course development costs. For example, although the Environmental School's first major training program was due to commence in October 2001, it had expended $900 000 on business and course development costs during the last 21 months.

3.1.72 **The MUPL revised business plan of January 2001, reveals that it aimed to secure an annual revenue target of $35 million, have a positive cash flow and achieve a positive operating result by 31 December 2004. However, given MUPL's performance and the fact that its operating losses continued to grow despite generating increasing levels of revenue, there was doubt whether MUPL could achieve the forecasts outlined in the business plan.**

Financial impact on The University of Melbourne

3.1.73 Under existing arrangements, the financial standing of MUPL had substantial financial ramifications for The University of Melbourne. Specific ramifications included:

- potential loss of the University's initial capital if MUPL did not improve its operating performance and the need for further capital injections;
- loss of potential revenue to the University in the form of licence fees and royalties from MUPL; and
- loss of significant revenue streams and other benefits to various faculties of The University of Melbourne, through a decrease in the level of educational services purchased by MUPL from these faculties to support its delivery of training programs.

Overlap in services offered by Melbourne University Private Limited

3.1.74 In establishing MUPL considerable care was taken to ensure that the courses offered would not be in competition with The University of Melbourne. Our review of the courses that have been provided to date, the courses that were planned to be provided and the consulting activities undertaken, did not disclose areas where MUPL was in direct competition with The University of Melbourne. However, our review found that there were similarities and overlap with activities undertaken by other entities associated with The University of Melbourne, such as:

- consultancies undertaken and non-award courses planned by MUPL, which were within the current scope of activities that could be undertaken by Melbourne Enterprises International Limited, a wholly-owned subsidiary; and
- certain courses offered by the Melbourne Business School, a 45 per cent owned associated company.

3.1.75 A consultant's report commissioned by The University of Melbourne has also identified that, with the recent introduction of full fee-paying students in the public university environment, there was increased potential for duplication, with many of the activities being undertaken by MUPL better suited for delivery by The University of Melbourne and the Melbourne Business School. Such overlaps in activity could result in the following detrimental effects on the performance of MUPL and other subsidiaries associated with The University of Melbourne:

- potential for increased competition and costs for staff and suppliers of professional services;
- lower student enrolments for certain courses leading to higher per unit costs; and
- lower profitability and, therefore, less potential for gaining returns on capital invested.

3.1.76 **In order to reduce the risks associated with the establishment and ongoing operation of MUPL and other subsidiaries of the University, The University of Melbourne should ensure that areas of overlap and duplication are eliminated as a matter of priority.**

Proposed restructure and merger of Melbourne University Private Limited

3.1.77 In October 2000, The University of Melbourne decided to consider a proposal to merge the activities of MUPL and Melbourne Enterprises International Limited (MEI). The basis for the proposed merger was to *"… augment the range and flexibility of educational service delivery by MUPL"* and to avoid *"… the growing danger of debilitating competition between MEI and MUPL"*.

3.1.78 On 1 January 1997, the business operations of Melbourne Research Enterprises Ltd were merged with the International Division of the Hawthorn Institute of Education Ltd. The latter company was renamed MEI. An aim of MEI is to support and promote the commercial and international interests of The University of Melbourne. Currently, its major activities involve the provision of English language skills to foreign students both in Melbourne and at overseas locations. For the year ending 31 December 2000, MEI had net assets of $32.6 million and, from a turnover of $38.9 million, had generated a net profit of $100 000 after donating $500 000 to The University of Melbourne.

3.1.79 During October 2000, The University of Melbourne formed a Re-structuring Steering Committee to consider the capital requirements and the issues confronting the proposed merger. Upon its establishment, the Committee sought responses from the management of MUPL and MEI across a broad range of issues so that a new business model for the merged entity could be developed. Both MUPL and MEI’s operations and activities were analysed by management and a number of documents were progressively provided to the Committee during the last months of 2000. These documents identified the following key benefits of the proposed merger:

- create a single private arm with common governance arrangements and greater clarity of roles;
- co-ordinated strategic direction for commercial activities;
- increased business development and revenue generating opportunities from exploiting MEI’s international network; and
- eliminate duplication of resources in many areas such as administration and support.

3.1.80 A draft business model was subsequently developed for the proposed merged entity. The Re-structuring Steering Committee appointed external consultants in March 2001, with the overall objectives to determine whether the proposed merger should proceed, consider the draft business model and potential alternatives, and assess the viability of the most appropriate model.

3.1.81 The consultant’s report, issued in April 2001, recommended the rationalisation and restructure of MUPL’s activities, and supported the proposed merger. The consultant developed a revised business model, with an emphasis placed on MUPL pursuing a more narrowly focused business based on demand rather than supply. The revised model considers that separate academic schools were inappropriate and highlights the need for enhanced sales and research capabilities. Although the proposed merger is likely to cost $1.6 million, annual savings of $1.3 million from improved operating efficiencies were identified.

3.1.82 On 7 May 2001, the Council of The University of Melbourne resolved that MUPL and MEI should merge. The University advised that this decision was based on a business model prepared by the consultant, which concluded that the merged entity has the potential to create significant value for the public university.

3.1.83 The consultant also concluded that, if the outcome of a due diligence review confirms the targets in MEI's business plan and that there are no large acquisitions or other unplanned changes to the business, the merged entity should be self-financing and fulfil the University's specific financial return requirements. The consultant indicated that there would be a short-term drain on the capital base of the business when a refocused MUPL was added to the business portfolio. However, the consultant also indicated that given the small scale of the refocused MUPL relative to the whole business, the merged entity should still provide appropriate financial returns and should not require additional capital.

3.1.84 In order to improve the outcomes from the proposed merger, it is important that The University of Melbourne ensure that detailed business plans currently being developed for the merged operations of MUPL and MEI incorporate a detailed risk analysis and are comprehensively reviewed by The University of Melbourne.

***RESPONSE** provided by the Vice-Chancellor, The University of Melbourne*

Lease agreement for University Square Development

While MUPL's reduced floor space requirements may result in loss of rental income to the University of Melbourne, the rent that would have been paid will now remain in MUPL. Accordingly, the net effect on shareholder value is nil. Furthermore, the fact that 3 floors of what is known as "Building A" in the University Square development will now revert to the University of Melbourne provides it with an opportunity to address some of its own pressing demands for space. Moreover, several synergistic, external research organisations that would benefit from close proximity to the University of Melbourne are seeking space in the relevant building on a commercial basis.

Financial performance

The Report states that a key aspect adversely affecting MUPL's financial performance was the shortfall in demand for the courses and services on offer in comparison to what was envisaged under the original business plan. The following changes in the operating environment of higher education and training have affected the original business plans for MUPL:

- *the introduction of income contingent loan arrangements to support coursework postgraduate study in public universities has sharply reduced the commercial viability of such courses in MUPL;*
- *demand for customised award courses to serve particular industry needs has turned out to require much less "on-campus" instruction than initially anticipated, with client preference being essentially for flexible delivery either on line or at remote sites at, or close to, the clients' work; and*
- *demand for certified executive training is now understood to operate most effectively through ad hoc arrangements using the facilities of the client or one-off rental space; it requires little dedicated infrastructure.*

The last 2 points also explain the reduced space needs of MUPL.

***RESPONSE** provided by the Chairman, Melbourne University Private Ltd*

Lease agreement for University Square development

The Report states that "a number of factors have reduced MUPL's floor space requirements" and include "MUPL's lower than expected growth" as one of those factors. This was not a major contributing factor. The initial business plans for MUPL were prudently based on the take-up of space on a variable basis, related to client demand. The renegotiation of the lease is due to our continuing policy of minimising risk, in addition to the other factor you identify. In any event, as a fall back, MUPL always planned to sub-lease surplus space.

The Report further states that the annual cost will now be $200 000. Note that the cost of the associated fit-out works that were the subject of the loan from the University (as noted in the Report and including the $2.1 million) will no longer be borne by MUPL.

The $1 million rental saving in MUPL will now be turned to more productive and revenue-generating activities rather than infrastructure costs, thereby increasing shareholder value.

Accountability and control over Melbourne University Private

Under financial reporting obligations we note that MUPL is also audited by MGI Meyrick Webster and that in all years, up to and including the year ended 31 December 2000, it has received unqualified audit opinions.

Financial performance

You state that "MUPL has incurred significant losses since its establishment". This is in line with expectations in the initial submission to the State Government for Ministerial approval to operate as a university

You further state that "The University of Melbourne expected that MUPL would generate strong cash flows and profitability within its first 5 years of operation". We disagree that this was the University's expectation. The submission to the Government for Ministerial approval to operate as a university stated that "Latest estimates suggest that on the most conservative of figures, that Melbourne University Private will generate positive cash flows from Year 9".

You refer to a projected loss of $4.5 million for the year ended 31 December 2001 (prior to the decision to lease less space and the decision to merge with MEI). MUPL's estimate is that, should it continue without merging, the loss for 2001 would be about $2.5 million. In any event, the merger has now been approved.

You state that the School of Energy and Environment has expended $900 000 on business and course development costs in the last 21 months. The majority of this expenditure has been on the establishment and development of the School's business, including identification of key areas of business needs and market demand, capability building, profile and network development, establishment of partnership and alliances, feasibility studies and programme development.

RESPONSE *provided by the Chairman, Melbourne University Private Ltd - continued*

You state that "… the MUPL revised business plan of January 2001, reveals that it aimed to secure an annual revenue target of $35 million, have a positive cash flow and achieve a positive operating result by 31 December 2004". We advise that:

- *The MUPL Board has not formally adopted the draft MUPL 2001 Business Plan as it was superseded by the restructuring process;*
- *The draft MUPL 2001 Business Plan was based on the following key assumptions:*
  - *the company would pursue major long-term developments (subject to resource availability); and*
  - *the obligations in the current lease for building A would remain.*

  Neither of these assumptions is now valid; and
- *The draft MUPL Business Plan was subject to access to additional capital to achieve the objectives.*

FINANCIAL VIABILITY OF PUBLIC TECHNICAL AND FURTHER EDUCATION PROVIDERS

3.1.85 Our June 2000 *Report on Ministerial Portfolios* commented on the financial position of public TAFE providers at 31 December 1999. That analysis identified that 6 of the 22 public TAFE providers were considered to be operating under financial difficulty.

3.1.86 As the capacity of all public TAFE providers to deliver high quality educational and training services is influenced by their ability to maintain a sound financial position, we again reviewed the financial position of public TAFE providers for the year ended 31 December 2000.

3.1.87 It is generally accepted that a key indicator of an organisation's financial viability is its capacity to meet current liabilities from available current assets as and when they fall due. Accordingly, one of the measurements to determine viability is the working capital position, which compares liabilities falling due for payment in the next 12 months, such as creditors and employee entitlements, against assets that typically provide the funds to extinguish those liabilities.

3.1.88 Other indicators are:

- operating result for the year, prior to grants received for capital purposes and transactions of an extraordinary nature; and
- net cash flows generated from operating activities during the year.

Position at December 2000

3.1.89 Our examination of the overall financial performance of public TAFE providers for the financial year ended 31 December 2000 disclosed:

- a deficit (prior to grants received for capital purposes and transactions of an extraordinary nature) of $26.5 million for the year to 31 December 2000 compared with a deficit of $25.3 million for the year to 31 December 1999;
- net cash inflows from operating activities of $40.7 million for the year to 31 December 2000 compared with net cash inflows of $32.1 million for the year to 31 December 1999; and
- a positive working capital position of $91.1 million as at 31 December 2000 compared with a positive working capital position of $66.4 million as at 31 December 1999.

3.1.90 Only 4 of the 6 public TAFE providers identified in the previous review as showing signs of financial difficulty were considered to be in financial difficulty as at 31 December 2000, namely Chisholm Institute of TAFE, Driver Education Centre, Council of Adult Education and Central Gippsland Institute of TAFE. However, the Wodonga Institute of TAFE is also now showing signs of financial difficulty.

Providers operating under financial difficulties

3.1.91 Table 3.1F provides details of the 5 public TAFE providers which, based on the results of our analysis, were considered to be operating under financial difficulties as at 31 December 2000.

TABLE 3.1F
PUBLIC TAFE PROVIDERS DISPLAYING SIGNS OF FINANCIAL DIFFICULTY, AS AT 31 DECEMBER 2000 *(a)*
($'000)

	Positive (negative) working capital position		*Operating surplus (deficit) prior to capital grants and extraordinary items*		*Net cash inflows (outflows) from operating activities*	
TAFE provider	*1999*	***2000***	*1999*	***2000***	*1999*	***2000***
Chisholm *(b)*	(8 514)	**(8 221)**	(9 495)	**(8 053)**	1 480	**(2 021)**
Driver Education Centre	(427)	**(460)**	(380)	**(381)**	136	**385**
Wodonga	72	**(22)**	(1 807)	**(2 155)**	652	**424**
Council of Adult Education	(1 023)	**(15)**	685	***(c)* 1 736**	1 678	**1 100**
Central Gippsland	(1 811)	**714**	(1 379)	**(2 133)**	866	**212**

(a) Based on audited financial reports.
(b) Qualified audit report issued on the accounts for the year ended 31 December 2000 - above table adjusted to correctly account for issue subject to audit qualification.
(c) Improved performance as a result of $1.5 million special government grant.

Chisholm Institute of TAFE

3.1.92 Chisholm is the largest TAFE Institute with over 57 000 students and 9 major campuses servicing the eastern and south-eastern suburbs of Melbourne, as well as regional Victoria.

3.1.93 **Of major concern is the poor financial position of Chisholm Institute of TAFE which, after adjusting for the effect of the audit qualification issued on its financial statements, had a negative working capital position of $8.2 million, an operating deficit prior to capital grants and extraordinary items of $8.1 million, and a net cash outflow from operating activities of $2 million.**

3.1.94 **The audit review of the Institute identified that it did not pay its suppliers in accordance with government guidelines and experienced cash flow problems that required advance funding of $2 million from the Office of Post Compulsory Education Training and Employment (PETE) in December 2000 to enable the payment of both suppliers and staff. However, the Institute treated this amount as a loan rather than revenue as required by Australian Accounting Standard AAS 15 "Revenue" resulting in grant revenue being understated by $2 million, the operating result for the year being overstated by $2 million and current liabilities being overstated by $2 million.**

3.1.95 **PETE has also again provided a letter of support to the Institute to ensure that cash flow will be available in 2001 to enable the Institute to meet its debts as they fall due.**

Chisholm - managing business plans and targets

3.1.96 Our June 2000 *Report on Ministerial Portfolios* made a number of recommendations in view of the continuing financial difficulties experienced by a number of public TAFE providers. The Report recommended that institutes:

- undertake strategic financial planning to address working capital and financial management issues; and
- continually re-examine business strategies so that future programs and operations are financially viable.

3.1.97 In addition, a number of detailed recommendations were also made regarding the reporting and cost management of fee-for-service activities.

3.1.98 **Given the extent of financial difficulties facing the Institute, it is, therefore, disappointing that Chisholm Institute of TAFE did not fully implement these recommendations.**

3.1.99 A comparison of the actual results of the Institute compared with its budget for 2000 indicates that a shortfall of $6.1 million occurred in its commercial revenue, out of a total revenue shortfall of $6.6 million compared with its budget.

3.1.100 In addition, total operating costs exceeded budget by $771 000. While salary and on-costs exceeded budget by $3.2 million, non-salary costs were below budget by $2.5 million.

3.1.101 In accordance with a revised Ministerial Direction dated 30 November 2000, Institutes are required to provide the Office of Post Compulsory Education, Training and Employment (PETE) with a fee-for-service report each year, outlining actual results for the previous financial year and a budget for the current year. The audit review of the fee-for-service report provided by the Institute for the 2000 financial year indicates that the report does not disclose the correct revenue figures as reported in the audited financial statements and that the Institute reported a surplus of some $4.1 million after indirect overheads from fee-for-service activity during the year, compared with an actual deficit before capital contributions of $10.1 million.

3.1.102 **Audit is concerned that the data contained in reports forwarded by public TAFE providers to PETE to facilitate monitoring of provider activities associated with fee-for-service may not be accurate and, therefore, recommends that PETE undertake a thorough review of all such reports received from public TAFE providers.**

Monitoring the performance of the Institute

3.1.103 Due to problems associated with the 1999 financial year, the Minister for Post Compulsory Education, Training and Employment advised the Institute on 5 June 2000 that it would be subjected to a monthly monitoring process by PETE, for the remainder of the 2000 financial year. The Institute was required to provide an Operating Statement and Balance Sheet to PETE within 10 working days of the following month. The statements were expected to be in a format similar to the quarterly report, with detailed explanations for all variances.

3.1.104 In addition, the Institute was also required to provide year-to-date details of fee-for-service activities. However, audit found no evidence of information having been provided or subsequently sought from the Institute in respect to its fee-for-service activities.

3.1.105 Table 3.1G below provides an indication of the progressive results reported by the Institute to PETE.

TABLE 3.1G
SUMMARY OF YEAR-TO-DATE (YTD) RESULTS REPORTED DURING THE 2000 FINANCIAL YEAR BY CHISHOLM INSTITUTE OF TAFE
($'000)

	YTD at June 2000	*YTD at September 2000*	*YTD at October 2000*	*YTD at November 2000*	***2000 financial year (a)***	***1999 financial year***
Operating revenue	54 541	78 902	86 294	94 642	103 115	95 547
Less operating expenses	51 785	78 499	86 632	95 635	106 444	97 684
Operating result before capital contributions and depreciation	**2 756**	**403**	**(338)**	**(993)**	**(3 329)**	**(2 137)**
Less depreciation	3 822	5 733	6 370	7 007	*(b)* 4 724	7 358
Operating result before capital contributions	**(1 066)**	**(5 330)**	**(6 708)**	**(8 000)**	**(8 053)**	**(9 495)**
Plus capital contributions	1 400	5 225	5 225	5 594	6 914	2 807
Net operating result	**334**	**(105)**	**(1 483)**	**(2 406)**	**(1 139)**	**(6 688)**

(a) Figures adjusted to correctly account for issue subject to audit qualification – advance funding of $2 million should have been accounted for as revenue instead of a loan.

(b) Depreciation charges were reduced in the year end financial statements due to a reassessment of the useful lives of the Institute's assets.

3.1.106 At the time of providing its September year-to-date results to PETE, the Institute forecast an Operating Deficit before Capital Contributions and Depreciation of up to $1.4 million at year-end.

3.1.107 At that time, the Institute identified that cash flow support may be required in December in order to pay staff salaries. On 20 November 2000 the Institute sought an advance of up to $4 million from PETE to enable staff to be paid on time in December and for cheques already drawn in favour of suppliers to be released. PETE provided advance funding of $2 million to the Institute on 20 December 2000 .

3.1.108 At the time of providing its November year-to-date results to PETE, the Institute reported a year-to-date Operating Deficit before Capital Contributions and Depreciation of $993 000. However, the accounts for the year ended 31 December 2000 adjusted for the effect of the audit qualification, disclosed an Operating Deficit before Capital Contributions and Depreciation of $3.3 million, some $2.3 million higher than the result reported as at November, and $1.9 million higher than that forecast in September.

3.1.109 **Despite the monthly monitoring process overseen by PETE, it would appear that neither the process nor the Institute management accurately projected the financial position of the Institute. For its part, PETE appears to have accepted the financial information provided by Institute management.**

3.1.110 **In the context of corporate governance of a public institution, it is of concern that the Council of the Institute did not ensure that adequate strategic financial planning was undertaken and that sufficiently robust monitoring and accountability processes were put in place.**

3.1.111 **We recommend that the Office of Post Compulsory Education, Training and Employment undertakes a review of the monthly monitoring process used for public TAFE providers deemed to be operating under financial difficulty.**

Staffing the Institute

3.1.112 In 1999 and 2000, the Institute received funding of $3.5 million to meet 98 voluntary redundancy packages. From a review of staffing statistics provided to PETE by the Institute, audit was unable to confirm that the Institute achieved ongoing annual savings through reduced staffing levels.

3.1.113 In October 2000, an enterprise bargaining agreement for teaching staff of the Institute was signed giving effect to salary increases of 13.6 per cent between the date of signing of the agreement and 1 September 2002. Although the Institute will receive supplementary funding for staff employed on State-funded programs, the Institute has calculated that it will be required to recover some $2.75 million over the next 2½ years in respect to non-recurrent activity, through a variety of means.

3.1.114 Therefore, not only will the Institute remain dependent on the generation of substantial commercial revenue, but it will also be required to seek major efficiency improvements. The implementation guidelines for enterprise bargaining provided to Institutes by PETE indicate that in relation to employees for whom supplementation funding is not available, auditable evidence of how the additional costs are to be met is to be provided by Institutes.

3.1.115 **We recommend that the Office of Post Compulsory Education, Training and Employment undertakes a thorough review of the outcomes of enterprise bargaining, particularly over the management of unfunded salary increases, in order to ensure that stated efficiency improvements are achieved and that such costs do not adversely impact on the overall provision of education and training by Institutes.**

Positioning of the Chief Financial Officer in the organisational structure

3.1.116 Audit is aware that the Chief Financial Officer is not part of the senior management team of the Institute. There is a recognisable danger when this situation exists that key financial decisions may be made without adequate professional input and expertise.

3.1.117 **We recommend that the Office of Post Compulsory Education, Training and Employment and public TAFE providers consider and review the organisational arrangements necessary to ensure that the correct mix of skills and abilities is available at the right level within public TAFE providers to ensure the proper operation and representation of the finance function.**

Institute budget

3.1.118 At 31 December 2000 the Institute reported:

- An increase in contingent liabilities from $1.6 million to $3.9 million for the non-delivery of contracted student contact hours. This will create additional pressure in the 2001 financial year to deliver additional student contact hours without additional funding or fund the repayment of this amount if required by PETE; and
- An increase in future operating lease commitments from $5.1 million to $10.5 million (105 per cent increase), creating additional pressure in future years on the management of fixed costs and cash flows.

3.1.119 **These obligations, together with the current financial position of the Institute, will require robust financial budgets to be developed and stringent monitoring of financial outcomes.**

3.1.120 As at 8 March 2001, the Institute had not finalised and adopted an annual budget for the 2001 financial year, including an entity-wide monthly cash forecast to indicate the expected cash position of the Institute.

3.1.121 Subsequently, the Institute produced an annual budget based on a deficit (which is contrary to applicable Ministerial Directions) of $8 million for the 2001 financial year, which was unacceptable to PETE and a revised budget has been requested.

3.1.122 **It is imperative that detailed and timely budgets are prepared in accordance with Ministerial Directions as part of the responsible financial management of the Institute.**

3.1.123 **In our June 2000 *Report on Ministerial Portfolios* we expressed serious concerns about the financial performance and position of the Chisholm Institute of TAFE. Given the losses incurred by the Institute in the second half of the financial year, it is disappointing that our concerns were not acted upon more fully at that time.**

3.1.124 **On 21 February 2001, the Government ordered an extensive review into the operations of Chisholm Institute of TAFE, due to concerns about the Institute's worsening financial position and the possible impact on the provision of education and training in the South Eastern suburbs. The results of that review were not available at the time this Report was finalised.**

Driver Education Centre

3.1.125 The financial position of the Centre at 31 December 2000 showed little improvement over the financial position reported for the 1999 financial year. During the 2000 financial year, a Ministerial Review of driver education in Victoria was undertaken, including a review of the future role and responsibility of the Centre. At the date of this Report, decisions have not been announced on the recommendations made by the review.

Council of Adult Education

3.1.126 The financial position of the Council at 31 December 2000 improved compared with the previous financial year mainly due to the receipt of a special Government grant of $1.5 million. Following a review by Government of Adult and Further Education in Victoria, the operations of the Council have been subsumed by the new Centre for Adult Education as from 1 March 2001.

Central Gippsland Institute of TAFE

3.1.127 During 2000, the Department of Employment, Education and Training purchased the Chadstone Campus, which was originally acquired in 1994 for $3.2 million, from the Institute for $4 million conditional on the Institute repaying a bank loan of $1.5 million, an advance of $914 000 to PETE, and retaining the balance to ensure that an appropriate working capital ratio was maintained.

3.1.128 Although the Institute now has a positive working capital position, its operating deficit prior to capital grants and extraordinary items deteriorated from $1.4 million in 1999 to $2.1 million in 2000. In addition, the net cash inflow generated by its operating activities declined from $866 000 in 1999 to $212 000 in 2000.

3.1.129 The Institute has identified the major reasons for the reported deterioration as:

- the expenditure on minor equipment acquisitions or on maintenance of $187 000 funded from Capital Contributions;
- a decrease in fee for service revenue of $954 000, mainly related to decreased training provided to major utility businesses and the direct impact of the Olympic Games on the Sydney operations of the Institute; and
- the impact of an Enterprise Bargaining Agreement for teaching staff signed in October 2000 and of supplementation funding of $91 000 not received in the 2000 financial year.

International Fibre Centre

3.1.130 The operating results of the International Fibre Centre deteriorated during the year due to a conscious decision by the Victorian Government to reduce the funding allocation, pending the results of a review being completed on the future direction of the Centre.

3.1.131 On the 10 April 2001, the Commonwealth and Victorian Governments and the CSIRO jointly announced the establishment of 2 new centres of excellence in Technical Textiles and Advanced Wool Products in Geelong, the provision of some $4.7 million to establish the centres, and the provision of ongoing funding. The centres will operate as part of the CSIRO to jointly develop and transfer knowledge and skills required for future textile and fibre technologies.

3.1.132 The bulk of the equipment from the Geelong Campus of the International Fibre Centre will transfer to the CSIRO, while a small amount of the equipment will transfer to the Brunswick Campus of the International Fibre Centre. The Brunswick Campus will become the focus for vocational education and training delivery for the fibre and textiles industries.

Actions of government in relation to TAFE providers

3.1.133 During the 2000-2001 financial year, the Government implemented a number of initiatives to assist public TAFE providers, including:

- provision of a further $9.7 million to assist those public TAFE providers with large numbers of students eligible for fee exemption;
- provision of $6 million by way of one-off maintenance grants;
- provision of $5 million by way of plant and equipment grants; and
- allocation of further special government grants totalling $3 million for voluntary redundancy packages.

3.1.134 Public TAFE providers are also being funded for the cost of enterprise bargaining agreements and award safety net increases applicable to State-funded programs. As mentioned earlier, public TAFE providers are expected to meet applicable costs for staff employed on non-recurrent activity through a variety of efficiency improvements over the period of the agreements.

3.1.135 However, offsetting the additional funds provided in 2000 were reductions comprising:

- $5 million relating to the 1.5 per cent annual productivity deduction; and
- $1.7 million relating to embedded tax savings following the introduction of the GST.

Fee-for-service activities

3.1.136 Audit acknowledges the work undertaken by PETE to implement the recommendations we made relating to reporting on fee-for-service activities in our June 2000 *Report on Ministerial Portfolios*. This led to the implementation of revised reporting arrangements being approved by the Minister on 30 November 2000.

3.1.137 **Audit review of a sample of fee-for-service reports received by PETE under the new reporting arrangements indicates the need for:**

- **greater internal checking by Institutes of the reports prior to submission;**
- **assurance from Institutes that the budget for the current year aligns with business plan and strategic financial planning targets; and**
- **stronger role to be taken by PETE in monitoring the outcomes of fee-for-service activity.**

3.1.138 However, we reiterate our concern that public TAFE providers need to ensure that:

- the returns generated by individual commercial activities justify the level of investment;
- overheads are correctly allocated to all activities; and
- comprehensive risk management strategies are in place which address key risks associated with this significant area of business activity.

3.1.139 The Commonwealth Department of Education, Training and Youth Affairs recognised the importance of universities having robust arrangements in place to fully and accurately measure the costs associated with their various activities. Several significant studies regarding costing within Australian higher education institutions were funded in 1998 and a number of Victorian universities have now taken the next step of implementing *activity based costing.*

3.1.140 **The implementation of activity-based costing by universities could provide a source of valuable learning for public TAFE providers in improving the structure and accountability of their fee-for-service programs.**

Accountability framework and financial performance monitoring of public TAFE providers

3.1.141 The Government has been continually moving towards achieving greater financial accountability for departments and public authorities within the Victorian public sector. The accountability of public sector entities to the Government and, ultimately, to the Parliament is dependent on a clear understanding by all parties of their roles and the processes used to plan and allocate funds as well as monitor and report on the outcomes of government-funded activities.

3.1.142 As a consequence, the Office of Post Compulsory Education, Training and Employment has a clear mandate and obligation to the Government to undertake robust and effective monitoring of all public TAFE providers, including their financial performance and the delivery of agreed outcomes.

3.1.143 The audit review identified that at present there are a number of opportunities for making improvements to the monitoring process and in the present quarterly financial reporting arrangements between public TAFE providers and PETE. These include the need for:

- a greater focus by PETE in analysing the projected year end results as well as the year-to-date results;
- clear identification of both the original and revised budgets in the reports; and
- public TAFE providers to provide explanations of any material differences between the quarterly report results and the actual results for the year, as well as any material differences from the results of the previous year.

3.1.144 **We recommend that the Office of Post Compulsory Education, Training and Employment undertake a detailed review of quarterly reporting requirements in order to ensure that it has the most efficient and effective mechanisms available to provide information to the Corporate Board of the Department of Education, Employment and Training, the Learning and Skills Commission and the Minister for Post Compulsory Education on the performance of public TAFE providers.**

***RESPONSE** provided by the Secretary, Department of Education, Employment and Training*

The Department of Education, Employment and Training notes the report on the financial viability of public technical and further education providers. In particular the Department notes the Auditor-General's assessment that while the deficit for all public TAFE providers has increased marginally, the results in terms of net cash inflows from operating activities and the working capital position of institutes indicate a substantial improvement over the previous year. In particular, the Department agrees that the significant improvement in the working capital position of Institutes from $66.4 million as at 31 December 1999 to $91.1 million at 31 December 2000, demonstrates a significant improvement in a key indicator of the system's financial viability.

In terms of the operating results for the year ended 31 December 2000, the Department does not believe that it is reasonable to include depreciation in any analysis of the financial health of the system since institutes are not funded for depreciation. If the depreciation expense is excluded, the sector showed a surplus of $33.6 million in 2000.

The Department notes that that the Auditor-General is of the view that 3 TAFE institutes, the Driver Education Centre of Australia, the Centre of Adult Education and the International Fibre Centre were considered to be operating under financial difficulties as at 31 December 2000.

The Report recognises the action already taken by the Government in relation to the International Fibre Centre and the Centre of Adult Education and that the Minister for Post Compulsory Education, Training and Employment is considering the recommendations of a Ministerial Review of Driver Education in Victoria which was commissioned in August 2000 to address concerns about the financial viability of the Driver Education Centre of Australia.

RESPONSE *provided by the Secretary, Department of Education, Employment and Training - continued*

The Department worked closely with the Council and Management of Chisholm Institute during 2000 to monitor the financial position of the Institute. PETE relied on the financial projections of the Institute as a self-governing body, until it became clear that the Institute was unable to trade its way out of financial difficulties and that its projections would not be achieved. During the first half of 2000, the Institute consistently advised the Department that it was confident that its 2000 budget projections would be achieved. The results during that time supported this view. Once it became clear that the financial position of the Institute was not continuing to improve, the Department determined that an external review was required and that it should proceed in a way that did not further add to the worsening financial position of the Institute. While formal announcement of the review did not occur until February 2001, the decision to conduct a review was in fact made in November 2000. However, the timing of the announcement was delayed so that student enrolments would not be adversely affected..

The financial position of Wodonga Institute of TAFE deteriorated marginally in 2000. The Department will continue to work with the Institute during 2001.

Central Gippsland Institute was adversely affected by the decline in fee-for-service revenue in 2000, however, its balance sheet position has improved. As with Wodonga Institute, the Department will continue to monitor the position of the Institute during 2001.

During 2000, the Department developed, with the assistance of TAFE institutes and the Victorian Auditor-General's Office, a report of the financial outcome of fee-for-service activities. These reports were provided to the Department recently. The Department agrees that some of the data forwarded by TAFEs associated with fee-for-service activities may not be completely accurate. This issue will be further pursued with institutes to ensure that the reports are accurate.

Audit proposes a review of the outcomes of enterprise bargaining. From the outset of the process, institutes were advised that the efficiency improvements negotiated through the enterprise bargaining process must be auditable and it was always intended that this issue would be revisited.

The comments on the role of the Chief Financial Officer in public TAFE providers are supported.

The Department agrees with audit that accurate quarterly reporting of the financial position of TAFE institutes is essential. Furthermore the experience with Chisholm Institute during 2000 highlights the need for TAFE institute councils to be provided with accurate financial information and projections, and to exercise a strong degree of control and oversight in the management of institute affairs.

The monthly monitoring of those institutes which have been assessed with particular financial difficulties will continue, and, where appropriate, remedial action will be taken in conjunction with institute councils and the Minister for Post Compulsory Education, Training and Employment.

SCHOOL GLOBAL BUDGET

3.1.145 A major feature of government schools in Victoria is the delegation of responsibility to schools for approximately 90 per cent of their operating costs, including staffing costs. This is achieved through the use of a School Global Budget (SGB), which is designed to enable schools to allocate resources in ways that best support the effective delivery of their educational programs.

3.1.146 The SGB was first introduced into Victorian schools in 1994. The key drivers of funding allocations through this system of budgeting are numbers and characteristics of students and student-to-teacher ratios.

3.1.147 The introduction of SGB was guided by 6 principles provided to underpin the design, implementation, review and refinement of funding to schools. Those principles were pre-eminence of educational considerations, fairness, transparency, subsidiarity, accountability and strategic implementation.

3.1.148 Through the SGB, the Department of Education, Employment and Training (DEET) provided budget allocations of approximately $2.96 billion in the 2001 financial year to all Victorian government schools. Funding associated with the SGB is provided through Annual Parliamentary Appropriation to DEET and represented around 53 per cent of DEET's overall annual Parliamentary appropriations in 2000-01. The Office of Schools within DEET is responsible for administering the SGB.

3.1.149 The processes followed by DEET for allocating the SGB to schools is a 3-step process as follows:

- an **indicative** SGB for each school is prepared by the Office of Schools during the preceding year using enrolment projections advised by schools;
- a **confirmed** SGB, issued at the end of Term 1 of the school year following the collation and confirmation of enrolment census information; and
- a **revised** SGB, which may be issued for specific updates or changes, for example following a census audit or as a result of entitlement changes relating to student mobility.

3.1.150 For the past 5 years, the determination of the budget for schools and the allocation of the bulk of funding through the SGB has been based on a funding model using the concept of *"averages-in/averages-out"*. *"Averages-in"* refers to the determination of the budget based on system-wide average costs for teachers in particular categories. The notional salary budget for each school was determined based on the allocation of the system-wide average costs for each category of teacher against the profile of teachers in each school. *"Averages-out"* refers to the use of these system-wide averages for charging salaries paid against these budgets.

3.1.151 Resulting from recommendations contained in 2 reviews undertaken in 2000, namely, The Ministerial Working Party - Public Education:The Next Generation (PENG 2000) and The Ministerial Review of Post Compulsory Education and Training Pathways in Victoria (Kirby Review, August 2000), together with the need to incorporate the Victorian Government Schools Agreement 2001 into the SGB, an alternative method of determining the budget allocation for each school and the allocation of amounts expended against the budget was introduced by the Government effective from the 2001 school year.

3.1.152 The changes to the SGB funding model represent a significant change to the school funding allocation process and have generated considerable debate and confusion in school communities. Concerns have been expressed by a significant number of school principals and other stakeholders, including the Victorian Associations of Primary and Secondary School Principals and the Australian Education Union regarding the true costs and benefits of the changes to the funding model and, particularly, the impact of the recently negotiated Victorian Government Schools Agreement 2001.

Confirmed SGB for 2001

3.1.153 **The Confirmed SGB for 2001 (the Confirmed Budget), that was released in April 2001, totalled $2.96 billion (the 2000 Confirmed Budget was $2.784 billion). This represents an increase of $176 million over the previous year's Confirmed Budget which was mainly attributed to:**

- $23 million for primary schools to reduce prep, year 1 and year 2 class sizes;
- $15 million to secondary schools for the implementation of the *Managed Individual Pathways* priority program;
- $49 million to support the new teacher career structure effective from January 2001 and the associated pay increases from April 2001, as a result of the implementation of the Agreement;
- $15 million representing funds for assistant principal and leading teacher accreditation and performance incentive payments (previously funded from other sources);
- $15 million to implement recommendations from the *Middle Years Research and Development Project*;
- $10 million additional funding for students with disabilities and impairments;
- $26 million for enrolment increases;
- $15.6 million for additional salary on-costs;
- $6 million for changes to cleaning, teaching support and casual relief teacher rates; and
- $1.4 million for student welfare and support.

3.1.154 Table 3.1H shows the total number of Victorian government schools, students, teaching staff and funding received, by type of school. These statistics formed the basis for the calculation of the 2001 Confirmed Budget.

TABLE 3.1H
GOVERNMENT SCHOOLS STATISTICS AND FUNDING, 2001

	Primary	*Secondary*	*Other (a)*	*Total*
Number of schools(*b*)	1 235	264	126	1 625
Number of students(c)	305 239	204 086	28 654	537 979
Teaching staff (d)	17 108	15 301	1 993	34 402
Confirmed Budget ($m)	1 440	1 230	290	2 960

(a) Represents Primary-Secondary, Special and Language Schools.
(b) At February 2001.
(c) Confirmed full-time equivalent student enrolment.
(d) Entitlement full-time equivalent staffing.
Source: Office of Schools.

3.1.155 The Confirmed Budget comprises 6 major funding components listed in Table 3.1I below:

TABLE 3.1I
CONFIRMED BUDGET FUNDING COMPONENTS, 2001

SGB components	*Allocation*	*Allocation*
	($m)	*(%)*
Core	2 490	84.1
Priority Programs	189	6.4
Disabilities and Impairments	179	6.0
Special Learning Needs	37	1.3
Rurality and Isolation	33	1.1
English as a Second Language	32	1.1
Total SGB	**2 960**	**100.0**

Source: Office of Schools.

3.1.156 As table above indicates, Core funding represents the main funding component, comprising 84.1 per cent of the total Confirmed Budget.

3.1.157 Core consists of the following sub-components:

- **leadership and teaching** – teachers' salaries and allowances;
- **teaching support** - for non-teaching staff salaries and school operational expenses;
- **premises** - contract cleaning, ground maintenance, utilities and associated maintenance works; and
- **salary on-costs** - including payroll tax, superannuation charges and WorkCover premiums.

3.1.158 The leadership and teaching sub-component account for $1.76 billion or 71 per cent of the Core component. Teacher salaries are also included in the other 5 funding components of the SGB. Consequently, teacher salaries represent the major funding element within the overall SGB.

3.1.159 The salaries input to the SGB while allocated to schools, is not physically provided to the schools as teacher salaries are paid by DEET. However, schools have flexibility in regard to the number and categories of teachers employed and any related salary savings are available to schools to be utilised as the schools determine.

Key changes to the funding model

3.1.160 The major change to the SGB funding model introduced in January 2001 relates to the salaries component of the SGB. The salaries component of the SGB is now based on a concept of "*funding-in/actuals-out*". *Funding-in* refers to the determination of the budget based on a Statewide average (standard) salary cost for all entitlement positions (excluding principals who are funded at their actual employment cost). *Actuals-out* refers to the actual salary costs incurred which are charged against these budgets.

3.1.161 This contrasts with the previous "*averages-in/averages-out*" model outlined in earlier paragraphs. The key changes in the funding model are presented in Table 3.1J.

TABLE 3.1J
KEY CHANGES IN THE SALARIES COMPONENT OF THE SGB FUNDING MODEL

2000 SGB	*2001 SGB*
Basis of determining budget allocation	
Funding allocation provided for in the budget is based on average/notional cost for each teacher classification, including the principal, as follows: • Level 1 teachers - $47 000; • Leading teachers 2 - $53 583; • Leading teachers 3 - $55 733; • Assistant principals – ranging from $60 000 to $74 400; and • Principals – ranging from $60 000 to $82 600.	Funding allocation provided for in the budget, based on estimated standard salary cost for **all** teachers (excluding principals) of $53 080. Funding allocation for principals based on their actual salary.
Performance incentives and special payments were provided for separately.	Performance incentives and special payments are now provided for in the standard salary cost of $53 080.
Funding was provided to allow for 30 per cent*(a)* of the total number of entitlement positions to be filled at the leading teacher level, assistant principal or principal level.	Leading teacher and assistant principal positions are now included in the standard salary cost of $53 080.
Charging against budget	
Notional average costs incurred based on Statewide averages for each classification charged against the budget as follows: • Level 1 teachers - $47 000; • Leading teachers 2 - $55 583; • Leading teachers 3 - $55 733; • Assistant principals*(b)* – ranging from $60 000 to $74 400; and • Principals* – ranging from $60 000 to $82 600.	Actual costs*(b)* incurred charged against budget as follows: • Beginning teachers – ranging from $37 500 to $43 200; • Experienced teachers – ranging from $44 400 to $51 100; • Experienced teachers with responsibility – ranging from $52 500 to $54 000; • Leading teachers – ranging from $55 600 to $58 800; • Assistant principals – ranging from $69 300 to $86 100; and • Principals – ranging from $69 300 to $99 700.

(a) According to DEET, nearly one-third of the leadership positions were not substantively filled and funding for almost one in 5 leadership positions in 2000 was used for purposes other than leadership positions.
(b) Depending on classification.
(c) Based on the new career structure and associated salary rates as at 1 January 2001.

3.1.162 As shown in the above table, **the 2001 SGB was based on an estimated standard cost of an entitlement position (teacher and assistant principal) of $53 080 with actual salary costs incurred charged against the budget.**

3.1.163 The total available funding for the salaries component of the SGB is made up of:

- an amount equivalent to the teacher salary component in the 2000 Confirmed Budget;
- new government funding to support the implementation of the new teacher career structure and the associated 3 per cent salary increase included in the Agreement; and
- internally redirected funding, previously outside of the SGB, consisting of accreditation funding for leading teachers and assistant principals, salary allowances and performance incentive payments.

3.1.164 In a memorandum dated 15 November 2000 issued by DEET to all school principals and school council presidents, DEET advised schools that the new SGB model would apply for the years 2001 to 2003, and would include transition funding in order to ensure no schools would be disadvantaged by the changes.

3.1.165 DEET modelling indicated that the move to the new SGB model would mean that for most schools their salaries component of the SGB would be enhanced. It also identified that transition support would be required for "a small group of schools". The Office of Schools guaranteed to make up the difference between the actual salary cost of teachers in these schools and the standard salary rate of funding allocated.

3.1.166 Details of the estimated impact for schools in need of transition support under the new SGB model and for schools where their advantage was "capped" at $75 000 were placed in an addendum to the indicative 2001 school global budgets.

3.1.167 Table 3.1K below shows the number of schools (by type) and the effect of the new model on their funding position in relation to salaries.

TABLE 3.1K
SCHOOLS FUNDING POSITION, BY TYPE
(number)

	Primary schools	*Secondary schools*	*Other schools (a)*	*Total*
Schools where advantage is capped at $75 000	67	6	3	76
Schools advantaged up to $75 000	842	53	64	959
Schools requiring transitional funding	326	205	59	590
Total	**1 235**	**264**	**126**	**1 625**

(a) Represents Primary-Secondary, Camps, Language and Special schools.
Source: Office of Schools.

3.1.168 The majority of schools (64 per cent) have been advantaged by the new model whereby the actual cost of their staff will be less than the funded rate in the 2001 SGB.

3.1.169 DEET records show that as of April 2001, there were 959 schools (59 per cent) projected to incur salary expenditures less than their budgeted allocation by up to $75 000, In accordance with DEET policy, the schools will be allowed to retain these funds.

3.1.170 DEET records also show that as at April 2001, there are 76 schools (5 per cent) projected to incur expenditures less than their budget allocation, by between $75 100 and $328 000. In accordance with DEET policy, these schools will be allowed to retain funds capped at $75 000. School principals may use these funds at their discretion for student outcomes consistent with government educational priorities.

3.1.171 **The Office of Schools has identified 590 schools (36 per cent) requiring transitional funding, that is, actual salary costs are forecast to be greater than the funding allocation, based on the formula under the new model, with 26 per cent of primary schools and 78 per cent of secondary schools projected to incur salary expenditures in excess of their allocation under the formula**.

3.1.172 DEET estimates the transitional funding required for primary schools will be in the range $79 to $66 000 and secondary schools in the range $1 700 to $247 000. A greater number of secondary schools will require transitional funding because they employ a significantly higher proportion of more experienced and leading teachers.

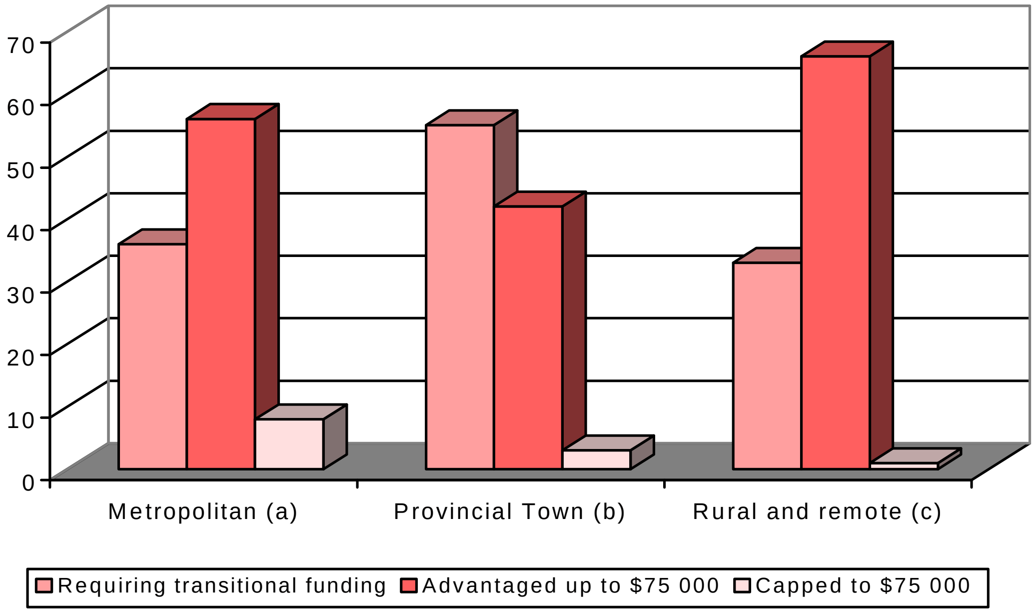
3.1.173 The salaries component provided in the SGB is based on all teachers, both primary and secondary being paid under the same salary structure. Primary schools are staffed according to a teacher to student ratio of 1 to 21. The principal of the primary school is included in this ratio. Secondary schools are staffed on a base entitlement of 4 staff (which includes the principal) in addition to a teacher to student ratio of 1 to16.

3.1.174 Even though the leadership profiles (principal, assistant principal and leading teachers) of secondary schools are higher than for primary schools and, accordingly, the actual cost per teacher in secondary schools is greater than in primary schools, the SGB funding formula is based on a standard salary cost for all teachers (other than principals) irrespective of whether they are primary or secondary.

3.1.175 During the transitional period, DEET expects schools to adjust their staffing profile away from 30 per cent of the total number of entitlement positions to be filled at the leading teacher level, assistant principal or principal level towards a profile that reflects the focus of the Agreement and the appointment of teachers to the new Experienced Teacher With Responsibility category.

3.1.176 Chart 3.1L compares the salaries funding position for schools in metropolitan Melbourne, provincial towns and rural and remote Victoria, following the introduction of the changes to the SGB funding model.

CHART 3.1L
SCHOOL'S SALARIES FUNDING COMPONENT POSITION
METROPOLITAN, PROVINCIAL TOWNS, RURAL AND REMOTE VICTORIA, 2001
(per cent)



(a) Metropolitan includes schools inside the Melbourne statistical division as defined by the Australian Bureau of Statistics.

(b) Provincial towns includes any city or town outside the Melbourne metropolitan area with a population of greater than 20 000.

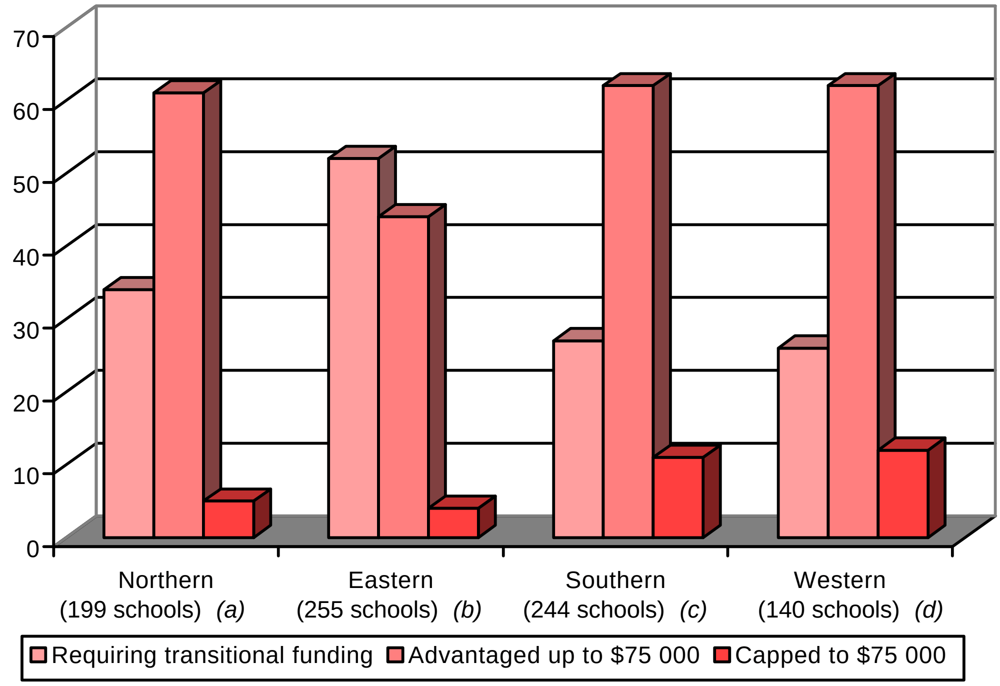
(c) Rural areas include any area outside the Melbourne metropolitan area, with a population of less than 20 000 that does not meet the criteria for remote area. Remote areas includes schools more than 150 kms from Melbourne and more than 25 kms from a provincial city, located in a district with less than 5 000 population.

Source: Office of Schools.

3.1.177 The new model attempts to provide a more equitable distribution of funding across all schools. **As illustrated in the above chart there are a higher percentage of schools in provincial towns requiring transition funding under the new funding arrangement with 72 schools out of a total of 131 schools in provincial towns (55 per cent) requiring transitional funding.** The transitional funding required for these schools ranges from $1 300 to $224 000. This is attributed to schools in provincial towns employing a greater number of experienced and leading teachers.

3.1.178 Chart 3.1M discloses the number of schools within each metropolitan region and their projected funding position in relation to the salaries component of the SGB, following the application of the changes to the funding model. The majority of schools in metropolitan regions are advantaged by the changed funding arrangements.

CHART 3.1M
METROPOLITAN SCHOOLS SALARIES FUNDING COMPONENT POSITION
(per cent)



(a) Northern region is represented by the local government boundaries of Moreland, Darebin, Banyule, Yarra, Hume, Whittlesea and Nillumbik.

(b) Eastern region is represented by the local government boundaries of Boroondara, Manningham, Whitehorse, Monash, Maroondah, Knox and Yarra Ranges.

(c) Southern region is represented by the local government boundaries of Port Phillip, Stonnington, Glen Eira, Bayside, Kingston, Greater Dandenong, Cardinia, Casey, Frankston and Mornington Peninsula.

(d) Western region is represented by the local government boundaries of Hobson Bay, Brimbank, Maribyrnong, Moonee Valley, Melbourne, Wyndham and Melton.

Source: Office of Schools.

3.1.179 As the chart illustrates, schools located in the Eastern region of Melbourne were identified as having the greatest percentage of schools projected to incur expenditures in excess of their budget allocations and require transition funding. At April 2001, there were 255 schools in the Eastern region, of which 133 (or 52 per cent) require transitional funding. This reflects that these schools employ a higher proportion of more experienced and leading teachers than schools in other metropolitan regions.

Transition funding

3.1.180 As stated in earlier paragraphs, school principals were advised by the Office of Schools that no school will be disadvantaged as a result of the change to a new funding model. **DEET has provided transition funding of $28 million for the 2001 school year.** In agreement with the Department of Treasury and Finance, transitional funding was sourced from within DEET's overall budget allocation

3.1.181 In determining the actual amount of transitional funding to be provided for each school, the Office of Schools has developed a methodology that has been used to determine the need for, and to calculate the level of transition support required. The methodology, which was agreed by DEET with the Victorian Associations of Primary and Secondary School Principals and the Australian Education Union, consists of an analytical tool which calculates the level of transition funding on the following step-by-step basis:

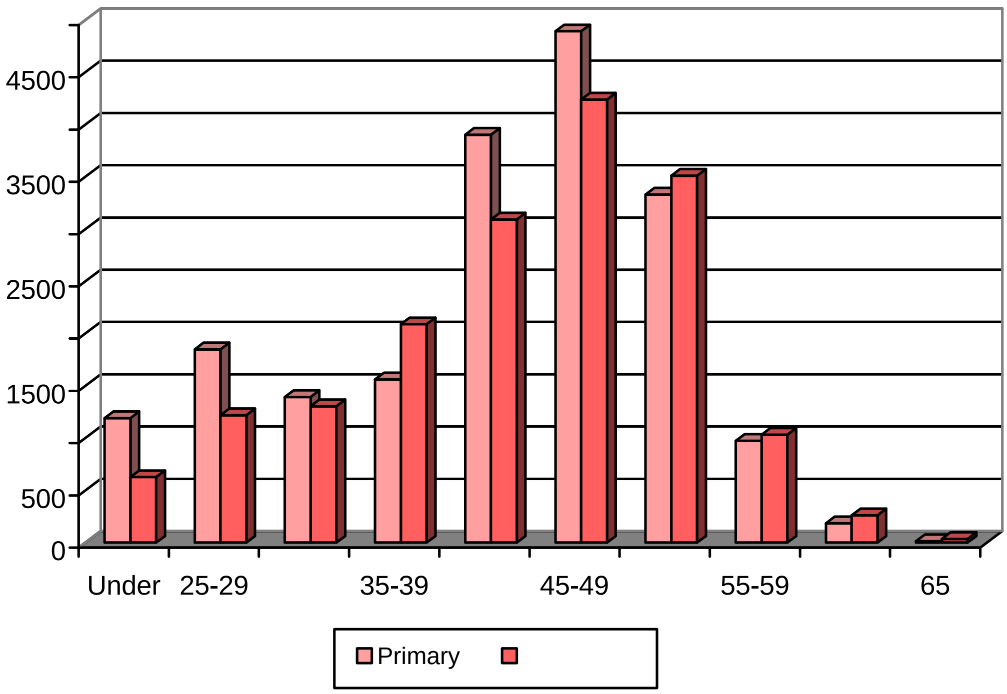
- Step 1 - Provision of additional funding determined by the differential between the total salary cost using the new teacher salary rates as at January 2001 (based on 2000 staffing entitlement levels) and the standard salary rate of $53 080 used for the SGB;
- Step 2 - Provision of additional amounts of $600 for each entitlement teacher position and $1 490 for 30 per cent of eligible staff who could occupy Experienced Teacher With Responsibility (ETWR) positions;
- Step 3 - Amounts deducted for teacher attrition based on an actuarial assessment prepared by external consultants engaged by DEET; and
- Step 4 - Amounts for leadership positions are funded at the base cost of the relevant classification. Where a school has more than the State average (24 per cent) of these positions substantively filled they are funded at their actual cost.

3.1.182 Currently, around 16 700 teachers are eligible to apply for promotion to ETWR positions. In accordance with the Agreement, each of these positions carries a salary increment of $1 490. **DEET indicated that sufficient resources have been provided in each school's budget to fund ETWR positions if filled.**

3.1.183 Given the age profile in secondary schools and based on an actuarial assessment of attrition, DEET expects that secondary schools will derive benefits from teacher attrition at a faster rate than primary schools.

3.1.184 Chart 3.1N presents the age profile of primary and secondary teachers.

CHART 3.1N
AGE PROFILE OF TEACHERS, FEBRUARY 2001
(actual teacher numbers)



Source: Office

age band and 2 800 teachers in the 55 to 65 plus years age band, out of a total of 39 900 teachers.

3.1.186 **DEET is relying on attrition as one means amo transition funding to schools. However, where attrition does not occur or takes longer than expected, this may result in the continuation of transition funding.**

Implementation process for the new SGB

GB was released to schools later than was intended. Normally, the indicative budget is promulgated in early September. -

November 2000. DEET indicated the need to delay the SGB resulted from endeavours to

the implementation of the Victorian Government Schools Agreement 2001, which was certified by the Australian Industrial Relations Commi December 2000.

3.1.188 The timing of the Indicative SGB combined with the introduction of the new funding model and the Agreement has caused considerable confusion and anxiety for ar. In addition, many principals expressed concern at the lack of consultation regarding the changes to the funding

arrangements. This situation led to negative publicity concerning the school funding process.

3.1.189 On such an important issue as public education, there needs to be greater communication and consultation with all stakeholders and greater transparency in the overall SGB process if the public is to have confidence in the administration of significant public funds. **The demonstrated lack of communication highlighted a need for DEET to introduce formal arrangements designed to educate school principals and school administrators in the dynamics of the SGB process**.

3.1.190 DEET has advised us that it has since taken action and has developed a State-wide program of communication and training in relation to the SGB process.

Review of the SGB funding model in 2001

3.1.191 In response to the many concerns raised by various stakeholders regarding the 2001 SGB funding model, in late November 2000, the Minister for Education requested DEET to undertake a review of the new SGB funding model. In December 2000, DEET announced the establishment of a review and monitoring process to be undertaken by a consultative committee with a representative from all key stakeholders, including Parents and School Council organisations, the Victorian Associations of Primary and Secondary School Principals and the Australian Education Union.

3.1.192 The aim of the review is to:

- identify the effectiveness of the SGB in 2001 in delivering more equitable funding to schools;
- examine international models of school funding which link resources to student need; and
- confirm the model for the SGB in 2002.

Conclusion

3.1.193 **The changes to the SGB have introduced greater transparency and equity into the funding of schools. However, the differences in the staff profiles of primary and secondary schools, has resulted in the need to provide transition funding as part of the SGB funding model. Accordingly, for schools to operate in future within the resources provided under the SGB funding model, principals of secondary schools in particular will need to significantly alter their staffing profiles.**

3.1.194 **Ultimately, the school funding model should be directed to linking resources to the educational needs of students. The level of resources provided and the staffing profiles of schools should move over time to more adequately reflect the learning needs of students in different stages of schooling across both primary and secondary schools.**

RESPONSE

The School Global Budget 2001 was introduced to enhance local control and redress
ffective subsidy paid by some schools to other schools through the use of the "averages in, averages-
issue raised by principals and their representatives during the PENG review. The final report (Public Education: The Next Gen
have a funding advantage over another school where such an advantage is not related to the specific needs of students.

Key changes to the funding model

- *A new funding- d on a standard salary credit of $53 080 for all entitlement positions (excluding principals);*
- *budget; and*

  A guarantee that transition support would be provided so that no school disadvantaged by the changes.

Transition funding is part of a school's total budget allocation and has been from the
incurring salary expenditure in excess of their budget allocation is not accurate.

Regarding Paragraph 3.1.174 -
by the school's EFT staffing. While the funding rate ($53 and secondary schools is the same, the method of calculating the EFT varies between the two

For example, the teacher entitlement in effect provides the following core teaching salary
ite of 500 students.

– 1 teacher for 21 students	*Secondary 1 teacher for 16 students + 4 base entitlement (including Principal)*
500 ¸ 21 = 23.81 total – Principal *= 22.81 teaching x $53 080* ***= Total core teaching $1 210 755***	*500 ¸ 16 + 4 = 35.25 total – Principal* *= 34.25 teaching x $53 080* ***= Total core teaching $1 817 990***

***RESPONSE** provided by Secretary, Department of Education, Employment and Training – continued*

Key changes to the funding model – continued

This has resulted in many secondary schools having higher EFT staffing entitlements, higher leadership profiles and higher funding relative to most primary schools.

Secondary colleges, on average, also have higher staff salary profiles due to a combination of more experienced teachers and higher leadership profiles. This has resulted in a greater proportion of secondary colleges receiving transition funding. However, this also means that they will gain benefits from teacher attrition at a faster rate than primary schools.

Transition funding

The overall median amount for schools is $28 106. This amount provides a clearer picture of the impact of the new SGB. The amount is relatively small for most schools.

Although 36 per cent of schools received transition funding in 2001, financial modeling based on current school data and feedback from schools and principal organisations has revealed that there will be a significant downward trend in 2002 in the number of schools receiving transition funding.

Attrition is only one means of reducing the amount of transition funding to schools. Other factors expected to have a significant effect on transition are:

- *New employments resulting from new funded programs (e.g. Middle Years); and*
- *Enrolment growth in some instances.*

Regarding Step 3 paragraph 3.1.182, attrition was reviewed during first term as part of the agreed process. In cases where attrition did not occur, DEET provided a rebate of the amount deducted.

Review of the SGB Model in 2001

The proposed review of the SGB funding model is not only in response to stakeholder concerns. DEET has had an in-principle agreement for some time (in response to the PENG recommendation on School Funding) to initiate a program of research to establish clearer links between the educational needs of students, the programs necessary to meet those needs and the resources required to deliver programs.

Conclusion

There is no requirement for schools to alter their staffing profiles except to reflect the new promotion position in the Victorian Government Schools Agreement 2001. DEET will continue to provide transition funding to any school where the actual salary costs of the EFT entitlement are greater than the funded rate.

DEET, through the SGB Review is looking at how closely current school funding is directed at educational needs and if necessary whether this linkage can be further improved.

SCHEDULE A
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS

Report	*Subject*	*Status at date of preparation of this Report*

MATTERS RESOLVED OR ACTION COMMENCED

DEPARTMENT OF EDUCATION EMPLOYMENT AND TRAINING

Privatisation of Melbourne IT Ltd

Ministerial Portfolios, June 2000 pp.22-51	The University of Melbourne benefited substantially from the public sale of shares in Melbourne IT Ltd. Nevertheless, there were lessons for government and public sector entities that can be learnt from the float, including the need for independent valuations and avoidance of conflict of interest.	All State and Territory Education Departments and the Commonwealth Department of Education, Training and Youth Affairs have agreed on a national review of the regulatory environment within which universities operate including the formation, governance and operation of companies formed by universities. The findings of this review are expected in July 2001 and they will be used to place the Victorian policy development on university subsidiary companies into the national context.The Department, in conjunction with the Department of Treasury and Finance (DTF), is developing a possible model for a “Constitution of a Company” for the use by university councils and their subsidiaries. Audit was advised that prior to finalising this matter there will be a need for extensive consultation with universities.

Financial viability of TAFE providers

Ministerial Portfolios, June 2000 pp. 52-60	As at 31 December 2000, there were 6 public TAFE providers showing signs of financial difficulty**.**	Further comment on the viability of public TAFE providers is provided in this Part of the Report.

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

Report	*Subject*	*Status at date of preparation of this Report*

MATTERS RESOLVED OR ACTION COMMENCED - *continued*

DEPARTMENT OF EDUCATION EMPLOYMENT AND TRAINING - *continued*

Property maintenance at TAFE Institutes

Ministerial Portfolios, June 2000, pp. 61-6.	The Department of Education, Employment and Training in February 2000 estimated that building maintenance funding requirements for all public TAFE providers were in the order of $12.6 million per annum. Given the quantum of maintenance backlog across the sector there is a need to focus on this issue to ensure that the TAFE facilities are maintained in a safe condition and are fit for their intended purpose.	The Department has allocated $6 million by way of maintenance funding for the 2000 - 2001 financial year. The Department is currently developing an asset management information system for TAFE institutes that will enhance the ability of the Department to make strategic decisions in relation to maintenance works and the development of new facilities. The information system is expected to be operational later this year.

NO ACTION TAKEN

VICTORIAN UNIVERSITIES

Ministerial Portfolios, May 1999, pp.44-6.	Qualified audit opinions were issued on the financial reports of all Victorian universities for the year ended 31 December 1998 due to the inappropriate recognition, in their balance sheets, of an asset representing the funding they expect to receive from the Commonwealth Government by way of future annual grants which in part will be applied towards their unfunded superannuation liabilities.	Position unchanged. The financial reports of all universities for the year ended 31 December 2000 were again qualified on this issue. This issue was considered by the Parliament’s Public Accounts and Estimates Committee during 2000-01 who agreed with the position taken by our Office.

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS			
FINANCIAL YEAR ENDED 30 JUNE 2000			
EDUCATION			
Board of Studies	26 July 2000	11 August 2000	✓
Department of Education	29 Sept. 2000	19 Oct. 2000	✓
Adult, Community and Further Education Board	24 Nov. 2000	25 Nov. 2000	✓
State Training Board	19 Sept 2000	29 Sept 2000	✓
Victorian Tertiary Admission Centre	28 Nov. 2000	30 Nov. 2000	✓
FINANCIAL YEAR ENDED 31 DECEMBER 2000			
POST COMPULSORY EDUCATION INSTITUTIONS			
Universities and associated companies			
Australian Alpine Institute Pty Ltd	12 April 2001	17 April 2001	✓
Australian International Health Institute Ltd	16 March 2001	29 March 2001	✓
Australian Music Examination Board (Vic.) Ltd	7 Feb. 2001	29 March 2001	✓
Australian National Academy of Music Ltd	22 March 2001	29 March 2001	✓
Betec Ltd	9 March 2001	21 March 2001	✓
Centre for Innovation and Enterprise Pty Ltd	23 Feb. 2001	28 March 2001	✓
Citytech Pty Ltd	26 March 2001	18 April 2001	✓
Centre for Innovation and Enterprise Trust	23 Feb. 2001	28 March 2001	✓
Copyrat Pty Ltd	1 Feb. 2001	23 May 2001	✓
Deakin University	27 March 2001	9 April 2001	Qualified opinion
(**Reason for Qualification:** *Inappropriate recognition of a receivable related to unfunded superannuation liabilities)*			
Dovaport Pty Ltd *(a)*	30 April 2001	30 April 2001	✓
Hexima Ltd	28 March 2001	3 April 2001	✓
Inskill Ltd	18 April 2001	23 May 2001	✓
International Education Network Pty Ltd *(b)*	13 March 2001	21 March 2001	✓
Institute for Innovation and Enterprise Ltd	23 Feb. 2001	28 March 2001	✓
Land and Food Services Ltd	2 April 2001	5 April 2001	✓
La Trobe International Pty Ltd	5 April 2001	12 April 2001	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS - *continued*			
FINANCIAL YEAR ENDED 31 DECEMBER 2000 - *continued*			
POST COMPULSORY EDUCATION INSTITUTIONS - *continued*			
Universities and associated companies - *continued*			
La Trobe Marketing Pty Ltd	12 April 2001	12 April 2001	✓
La Trobe University	26 April 2001	30 April 2001	Qualified opinion
*(**Reason for Qualification**: Inappropriate recognition of a receivable related to unfunded superannuation liabilities)*			
La Trobe University Housing Ltd	23 April 2001	26 April 2001	✓
Maccine Pty Ltd *(a)*	21 Feb. 2001	27 April 2001	✓
Meanjin Company Ltd	26 March 2001	6 April 2001	✓
Melbourne Enterprises International Ltd	29 March 2001	5 April 2001	✓
Melbourne Enterprises International (NZ) Ltd *(a)*	15 Feb. 2001	4 April 2001	✓
Melbourne Enterprises International (Taiwan) Ltd *(a)*	29 Jan. 2001	4 April 2001	✓
Melbourne Information Management Pty Ltd *(c)*	28 March 2001	3 April 2001	✓
Melbourne Research Enterprises Ltd	3 April 2001	5 April 2001	✓
MUP Services Pty Ltd	19 March 2001	5 April 2001	✓
Melbourne University Private Ltd	16 March 2001	6 April 2001	✓
Meltech Services Ltd	18 April 2001	4 May 2001	✓
Monash Digital Media Pty Ltd (a)	22 Feb. 2001	18 May 2001	✓
Monash International Pty Ltd	9 April 2001	9 April 2001	✓
Monash IVF Pathology Services Trust	6 Feb. 2001	22 May 2001	✓
Monash IVF Pty Ltd	6 Feb. 2001	15 May 2001	✓
Monash English Language Centre Pty Ltd	8 Feb. 2001	1 May 2001	✓
Monash Reproductive Pathology and Genetics Pty Ltd	6 Feb. 2001	15 May 2001	✓
Monash Southern Africa Pty Ltd *(a)*	22 Feb. 2001	15 May 2001	✓
Monash Unicomm Pty Ltd	20 Feb. 2001	18 May 2001	✓
Monash University	5 March 2001	1 May 2001	Qualified opinion
*(**Reason for Qualification**: Inappropriate recognition of a receivable related to unfunded superannuation liabilities)*			

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS – *continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS – *continued*			
FINANCIAL YEAR ENDED 31 DECEMBER 2000 – *continued*			
POST COMPULSORY EDUCATION INSTITUTIONS – *continued*			
Universities and associated companies – *continued*			
Monash Ultrasound Pty Ltd	9 Feb. 2001	8 May 2001	✓
Monash Ultrasound Trust	6 Feb. 2001	14 May 2001	✓
Monash University Foundation Pty Ltd	22 Feb. 2001	1 May 2001	✓
Monash University Foundation Year Ltd	9 Feb. 2001	27 April 2001	✓
Monash University Foundation Trust	22 Feb. 2001	18 May 2001	✓
Montech Pty Ltd	22 Feb. 2001	18 May 2001	✓
Montech Medical Development Pty Ltd	22 Feb. 2001	8 May 2001	✓
Mt Bulla Education Facilities *(a)*	30 April 2001	30 April 2001	✓
National Institute of Circus Arts Ltd	21 Feb. 2001	28 March 2001	✓
Neurometric Systems Pty Ltd	21 Feb. 2001	28 March 2001	✓
Prostate Diagnostics Pty Ltd *(a)*	21 Feb. 2001	23 March 2001	✓
RMIT University	30 March 2001	6 April 2001	Qualified opinion
(***Reason for Qualification:*** *Inappropriate recognition of a receivable related to unfunded superannuation liabilities and inappropriate disclosure of non-reciprocal grants.)*			
RMIT Foundation	26 March 2001	18 April 2001	✓
RMIT Innovation Ltd	6 April 2001	26 April 2001	✓
RMIT International Pty Ltd	6 April 2001	20 April 2001	✓
RMIT (Malaysia) SDN BHD	26 March 2001	26 April 2001	✓
RMIT Resources Limited	9 April 2001	26 April 2001	✓
RMIT Training Pty Ltd	5 April 2001	18 April 2001	✓
RMIT Union	26 April 2001	26 April 2001	✓
School of Forestry Creswick Ltd	2 April 2001	3 April 2001	✓
School of Mines and Industries Ballarat Ltd	9 May 20001	23 May 2001	✓
Sir John Monash Business Centre Pty Ltd	22 Feb. 2001	7 May 2001	✓
Spatial Vision Innovations Pty Ltd *(a)*	13 April 2001	13 April 2001	✓
Swinburne Graduate School of Integrative Medicine Pty Ltd	28 Feb. 2001	28 March 2001	✓
Swinburne Ltd	21 Feb. 2001	28 March 2001	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS - *continued*			
FINANCIAL YEAR ENDED 31 DECEMBER 2000 - *continued*			
POST COMPULSORY EDUCATION INSTITUTIONS - *continued*			
Universities and associated companies - *continued*			
Swinburne University of Technology	29 March 2001	5 April 2001	Qualified opinion
(Reason for Qualification: *Inappropriate recognition of a receivable related to unfunded superannuation liabilities and inappropriate disclosure of non-reciprocal grants.)*			
University of Ballarat	28 March 2001	4 April 2001	Qualified opinion
(Reason for Qualification: *Inappropriate recognition of a receivable related to unfunded superannuation liabilities and inappropriate disclosure of non-reciprocal grants.)*			
University of Melbourne	3 April 2001	6 April 2001	Qualified opinion
*(**Reason for Qualification:** Inappropriate recognition of a receivable related to unfunded superannuation liabilities and inappropriate recognition of non-reciprocal grants.)*			
Victoria University Enterprises Proprietary Limited	23 March 2001	3 April 2001	✓
Victoria University of Technology	22 March 2001	6 April 2001	Qualified opinion
*(**Reason for Qualification:** Inappropriate recognition of a receivable related to unfunded superannuation liabilities and inappropriate disclosure of non-reciprocal grants)*			
Victoria University of Technology (Singapore) Pty Ltd	22 March 2001	23 April 2001	✓
Victoria University of Technology Foundation Ltd	20 March 2001	3 April 2001	✓
Victorian College of the Arts	9 March 2001	6 April 2001	Qualified opinion
(Reason for Qualification: *Inappropriate recognition of a receivable related to unfunded superannuation liabilities and inappropriate disclosure of non-reciprocal grants.)*			
INSTITUTES OF TECHNICAL AND FURTHER EDUCATION AND ASSOCIATED COMPANIES, AND OTHER PROVIDERS			
Angliss Consulting Pty Ltd	21 March 2001	26 March 2001	✓
Angliss Multimedia Pty Ltd *(d)*	21 March 2001	26 March 2001	✓
Angliss Solutions Pty Ltd	21 March 2001	26 March 2001	✓
Bendigo Regional	23 Feb. 2001	9 March 2001	✓
Box Hill	15 March 2001	19 March 2001	✓
Box Hill Enterprises Ltd	15 March 2001	19 March 2001	✓
Central Gippsland	13 March 2001	22 March 2001	✓
Chisholm	20 March 2001	30 March 2001	Qualified opinion
(Reason for Qualification: *Inappropriate recognition of a receivable.)*			

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS - *continued*			
FINANCIAL YEAR ENDED 31 DECEMBER 2000 - *continued*			
INSTITUTES OF TECHNICAL AND FURTHER EDUCATION AND ASSOCIATED COMPANIES, AND OTHER PROVIDERS - *continued*			
Council of Adult Education	30 March 2001	2 April 2001	✓
Driver Education Centre of Australia Ltd	13 March 2001	22 March 2001	✓
East Gippsland	13 March 2001	23 March 2001	✓
Gordon	23 April 2001	23 April 2001	✓
Goulburn Ovens	23 Feb. 2001	27 March 2001	✓
Holmesglen	2 March 2001	14 March 2001	✓
Holmesglen International Training Services Pty Ltd	2 March 2001	14 March 2001	✓
International Fibre Centre Ltd	18 May 2001	22 May 2001	✓
International Training Australia Pty Ltd	28 March 2001	30 March 2001	✓
John Batman Training and Consulting Pty Ltd	2 March 2001	14 march 2001	✓
Kangan Batman	28 March 2001	30 March 2001	✓
Northern Melbourne	2 Feb. 2001	21 Feb. 2001	✓
South West	14 March 2001	26 March 2001	✓
Sunraysia	16 March 2001	22 March 2001	✓
William Angliss	26 March 2001	27 March 2001	✓
Wodonga	9 March 2001	15 March 2001	✓
INCOMPLETE AUDITS			
EDUCATION			
Telematics Course Development Fund Trust	*Audited financial statements yet to be finalised*		
POST COMPULSORY EDUCATION INSTITUTIONS			
AMPASC Pty Ltd	*Audited financial statements yet to be finalised*		
Deakin Software Services Pty Ltd	*Audited financial statements yet to be finalised*		
Monash University South Africa *(a)*	*Audited financial statements yet to be finalised*		
Monash Mt Eliza Graduate School of Business	*Audited financial statements yet to be finalised*		
Unilink Ltd	*Audited financial statements yet to be finalised*		

(a) New audit responsibility.
(b) Formerly known as Pexmont.
(c) Formerly known as ASAP Information Services Pty Ltd.
(d) Formerly known as WAI Online Pty Ltd.

Part 3.2

Human Services

KEY FINDINGS

Financial viability of hospitals

- There are 12 hospitals which, based on the hospitals subject to our analysis, are expected to be operating under financial difficulties as at 30 June 2001.

  Paras 3.2.16 to 3.2.27

- Despite the injection of supplementary funds over the past year or so, the financial condition of the public hospital system remains weak and vulnerable. Suitable financial structures need to be in place to reward innovation and cost-effectiveness if this ongoing issue is to be placed on a sounder footing in the future.

  Para. 3.2.28

Rural hospital information technology alliances

- The establishment of the rural alliances to provide information technology (IT) facilities to rural hospitals represents a new model of operating initiated by the Department of Human Services. This model has successfully delivered benefits in the form of up-to-date IT technologies to all participating hospitals.

  Paras 3.2.68 to 3.2.69

- While substantial benefits have been realised by participating hospitals under the alliances, the Y2K issue and the delay in the flow of funds have impacted the progress of implementation of the Information, Information Technology and Telecommunications Strategy for Public Hospitals.

  Paras 3.2.29 to 3.2.67

- The results achieved under the alliances model to date should encourage the Department to utilise this approach in other operational areas in rural hospitals.

  Paras 3.2.70 to 3.2.72

KEY FINDINGS - *continued*

Post-acute care planning

- In the latter part of the last decade, the Department of Human Services, particularly through its Acute Health Division, has introduced a range of innovative programs and initiatives to address the demand for services in the sub-acute and post-acute sectors. Despite these innovations, limitations in available data precluded us from making a definitive judgement on the adequacy of the Department's actions.

  Paras 3.2.200 to 3.2.210

- There is increasing demand for post-acute care services due to decreasing length of stay and bed availability in acute hospitals and rehabilitation services, weaknesses in discharge effectiveness, and decreases in community care-type services provided by hospitals. This has resulted in the swift take-up of Post-Acute Care Program places.

  Paras 3.2.120 to 3.2.153

- As well as the State, the Commonwealth Government is a major funding source. Post-acute care is provided through private, public and community-based organisations. To limit systems complexity and duplication of services, the State, the Commonwealth and service providers need good communication and co-ordination.

  Paras 3.2.187 to 3.2.199

- Flexible policy and funding models can encourage a focus on patient outcomes, reduce the complexity of the service system, set clear service standards and monitor achievements against those standards. There are examples of such models, but they have been small and have yet to demonstrate their broad applicability.

  Paras 3.2.177 to 186

- Despite a recent focus on strategic planning, poor data has hampered planning, monitoring and an understanding of how individuals access post-acute care services. Some encouragement of innovation and improved service delivery for sub-acute and post-acute services occurred in the latter part of the last decade.

  Paras 3.2.160 to 176

- The Department has not adequately monitored the effectiveness of the service delivery models for the provision of post-acute care. Program monitoring and evaluation has been variable, with delays in developing performance indicators, non-collection and/or non-reporting of some important indicators and limitations on the availability and quality of data.

  Paras 3.2.211 to 3.2.239

SUMMARY OF AUDIT RESULTS

3.2.1 The Human Services portfolio comprises the Department of Human Services, 96 health bodies, 14 cemetery trusts and a number of registration boards for a range of health professionals. The Department's principal responsibilities are:

- provision of high quality and efficient health care services through the public hospital system, community health centres and ambulance services;
- provision of residential and rehabilitation care for older and disabled persons as well as support and assistance to enable them to continue to live at home as long as possible;
- provision of secure, affordable and appropriate housing to low income Victorians, crisis accommodation and support for homeless people;
- provision of a wide range of health, welfare and community services for Victorian families, including the provision of services to vulnerable families and individuals;
- promoting health and preventing illness, disability and distress through education, regulation, early intervention and other services; and
- provision of government concessions to low income groups to improve the affordability of key essential items.

3.2.2 Most services are provided by agencies under funding and service agreements with the Department. These agencies include public hospitals, metropolitan health services, nursing homes operated by public sector agencies, municipal councils, community health centres, ambulance services and a range of non-government organisations providing mainly welfare services. The Department also provides some services directly including public rental housing, intellectual disability accommodation, child protection and juvenile justice services.

3.2.3 Within the portfolio the Auditor-General is also responsible for the financial audit of 14 cemetery trusts. These trusts are statutory authorities constituted under the provisions of the *Cemeteries Act* 1958 and are responsible for the management of cemeteries and memorial gardens, and the provision of burial and cremation facilities.

3.2.4 The Minister for Health, the Minister for Community Services, the Minister for Aged Care and the Minister for Housing have responsibility for public sector agencies within the Human Services Sector as outlined in Table 3.2A. These Ministers also have collective responsibility for the Department of Human Services.

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

Ministerial portfolio	*Entities subject to audit*
Aged Care	-
Community Services	-
Health	Advanced Dental Technicians Qualifications Board *(a)*
	Alexandra and District Ambulance Service
	Ambulance Officers' Training Centre *(b)*
	Ambulance Service Victoria - Metropolitan Region
	Anti-Cancer Council of Victoria
	Chiropractors Registration Board of Victoria
	Dental Board of Victoria *(a)*
	Dental Technicians Licensing Committee *(a)*
	Infertility Treatment Authority
	Medical Practitioners Board of Victoria
	Mental Health Review Board
	Nurses Board of Victoria
	Optometrists Registration Board of Victoria
	Osteopaths Registration Board of Victoria
	Pharmacy Board of Victoria
	Podiatrists Registration 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 (14)
	Public hospitals (86) *(c)*
	Rural Ambulance Victoria
	Victorian Health Promotion Foundation
	Victorian Institute of Forensic Mental Health
Housing	-

(a) From 1 July 2000, entity ceased operations and were combined to form the Dental Practice Board of Victoria.

(b) Entity ceased operations on 30 November 1999.

(c) From 1 July 2000, the 7 existing metropolitan health care networks were replaced with 12 smaller metropolitan health services.

3.2.5 The annual reporting and audit requirements for entities within the portfolio are set out in the *Financial Management Act* 1994 and the *Audit Act* 1994. In particular, under section 45 of the Financial Management Act, each department and public body must submit its annual financial statements to the Auditor-General within 8 weeks of the end of the financial year. Under the Audit Act, the Auditor-General is then required to audit the financial statements within 4 weeks of their receipt. Finally, within 4 months of the end of the financial year or the next sitting day after the end of the fourth month, the relevant Minister is required to table in each House of the Parliament the annual report of each entity, including the audited financial statements.

Nature of audit opinions issued

3.2.6 During the 1999-2000 financial audit cycle, 100 clear audit opinions were issued on the sector's financial statements, with 20 financial statements subject to audit qualification. Schedule B to this Part of the Report provides information about the nature of the audit opinions issued in respect of each entity during the audit cycle.

3.2.7 Qualified audit opinions were issued on a range of entities within the sector for the following reasons:

- Inappropriate disclosure of non-reciprocal grants in accordance with Australian Accounting Standard AAS 15 – *Revenue* (8 instances);
- Failure to consolidate a "controlled" entity in accordance with Australian Accounting Standard AAS 24 – *Consolidated Financial Reports* (4 instances);
- Failure to disclose prior period adjustments in accordance with Australian Accounting Standard AAS 1 – *Profit and Loss or Other Operating Statements* (2 instances);
- Inappropriate recognition of debtors (2 instances);
- Non-review of useful life of buildings in accordance with Australian Accounting Standard AAS 4 – *Depreciation* (1 instance);
- Failure to disclose Chief Executive Officer remuneration as required by the *Financial Management Act* 1994 (1 instance);
- Inappropriate asset write-down in the value of a hospital building (1 instance);
- Non-revaluation of land and buildings as required by the *Financial Management Act* 1994 (1 instance); and
- Limitation of scope as the audit of income classified as "charitable support" was limited to amounts recorded in the accounting records (1 instance).

3.2.8 The qualifications made in respect of inappropriate recognition of revenue occurred mainly in relation to the non-compliance of the particular entities with Australian Accounting Standard AAS 15 – *Revenue*, which requires that any income received by, or due to, an entity must be treated as income in the accounts of the recipient in the year of receipt, when the grants are regarded as non-reciprocal in nature. In the case of 8 health entities, where the grants were of a material size and non-reciprocal in nature and were recorded as current liabilities rather than recognised as revenue in the year of receipt, a qualified audit opinion was issued.

3.2.9 In the case of 4 hospitals, their financial statements were qualified on the grounds that they failed to consolidate foundations that are regarded as "controlled entities" in accordance with Australian Accounting Standard AAS 24 – *Consolidated Financial Reports*.

Timeliness of financial reporting

3.2.10 As previously mentioned, the legislative framework requires the audited financial statements of the public sector to be completed within 12 weeks of the end of the relevant financial year. Table 3.2B illustrates the performance of portfolio agencies in meeting this statutory requirement during the 1999-2000 reporting cycle.

TABLE 3.2B
TIMELINESS OF FINALISATION OF AUDITED FINANCIAL STATEMENTS, HUMAN SERVICES PORTFOLIO *(a)*

	Entities	
Number of weeks after end of financial period	*Number*	*Per cent (cumulative)*
Less than 8 weeks	1	1
8 to 10 weeks	10	9
10 to 12 weeks	46	46
12 to 14 weeks	31	72
14 to16 weeks	20	88
Over 16 weeks *(b)*	15	100

(a) This table does not include financial statements for the 1998-99 financial year, that were signed during the current audit cycle.
(b) Includes 3 entities where the audited financial statements are yet to be finalised.

3.2.11 The table demonstrates that **there is scope for improvement in the timeliness of completion of audited financial statements, with 46 per cent of entities meeting the 12 week legislated completion timeframe.** The audited financial statements of the majority of the remaining entities were available within 4 weeks of the legislated completion timeline (that is, within 16 weeks of year-end).

3.2.12 **Timeliness of reporting is an essential characteristic of an effective accountability process. Accordingly, it is important that avenues are identified and pursued to improve the timeliness of the financial reporting process.**

Restructure of health services

3.2.13 During the 1999-2000 financial year, the *Health Services Act* 1988 was amended by the *Health Services (Governance) Act* 2000 to facilitate the disaggregation of certain health care networks and the reorganisation of public health care agencies in the metropolitan area. The legislation also provided for the appointment of board members, established the terms and conditions of such appointments and the general operations of those boards, and provided the necessary transitional arrangements to facilitate the required changes brought about by the discontinuance of health care networks.

3.2.14 The new governance and management structures for metropolitan hospitals were introduced from 1 July 2000 replacing the 7 existing metropolitan health care networks with 12 smaller metropolitan health services.

3.2.15 In addition, on 1 July 2000 responsibility for Aboriginal Affairs Victoria transferred from the Department of Human Services to the Department of Natural Resources and Environment.

FINANCIAL VIABILITY OF HOSPITALS

3.2.16 In previous Reports to Parliament I have commented on the financial position of public hospitals and outlined measures taken by the Department of Human Services to address financial difficulties faced by hospitals. Specifically, when reviewing the financial position of hospitals the audit analyses have focused on the following 3 financial indicators:

- the working capital position at year-end;
- operating result for the year, prior to grants received for capital purposes and transactions of an extraordinary nature; and
- net cash flows generated from operating activities during the year.

3.2.17 My June 2000 *Report on Ministerial Portfolios* identified that, while the overall financial performance of hospitals had improved in the 1998-99 financial year compared with the previous year, there were 8 hospitals that were considered to be operating under financial difficulty as at 30 June 1999. In its response to the audit findings, the Department indicated that additional funding of $176 million would be provided to hospitals during the 2000-01 financial year, together with an increase in the price paid for casemix-funded services to hospitals to ensure that they remain viable.

3.2.18 A review panel, established in November 1999 by the Minister for Health to provide advice on new governance and management structures for the metropolitan hospitals, released its final report in May 2000. The review panel proposed that the 7 existing metropolitan health care networks be restructured as 12 metropolitan health services. In addition, the panel recommended that:

- hospitals' liquidity problems be addressed as a matter of urgency prior to the establishment of the new metropolitan health services; and
- additional funding be provided in the 2000-01 financial year to reduce to 5 per cent the proportion of activity funded at less than full variable rates.

3.2.19 In its response to the review panel's report, the Government indicated that a due diligence review had been commissioned by the Department of Treasury and Finance in order to determine the level and type of one-off equity injection required to restore hospital solvency levels. It also indicated that of the additional funding of $176 million in the 2000-01 budget, an allocation of $53 million would be supplied to increase the price paid for casemix-funded services, sub-acute beds and rural hospitals.

3.2.20 Following finalisation of the due diligence review in June 2000, the Government announced an injection of a further $34.6 million to address liquidity issues at the new metropolitan health services to be established on 1 July 2000. The health services to receive grants were the Austin and Repatriation Medical Centre ($20.7 million), Eastern Health ($5 million), Melbourne Health ($8.3 million), Northern Health ($300 000), and Western Health ($300 000).

Review of results for 1999-2000

3.2.21 We reviewed the financial position of public hospitals for the year ended 30 June 2000, using the earlier-mentioned financial indicators. Our examination showed that the overall financial condition of the public hospital sector had deteriorated in the 1999-2000 financial year. We found that the sector recorded:

- a deficit (prior to grants received for capital purposes and transactions of an extraordinary nature) of $147.4 million for the 1999-2000 financial year compared with a deficit of $2.7 million for the 1998-99 financial year;
- net cash inflows from operating activities of $64 million for the 1999-2000 financial year compared with net cash inflows of $116.9 million for the 1998-99 financial year; and
- a positive working capital position of $98.9 million as at 30 June 2000 compared with a positive working capital position of $170.6 million as at 30 June 1999.

3.2.22 **There are 3 hospitals which, based on the results of our analysis, were considered to be operating under financial difficulties as at 30 June 2000. These hospitals are identified in Table 3.2C.**

TABLE 3.2C
PUBLIC HOSPITALS DISPLAYING SIGNS OF FINANCIAL DIFFICULTY, AS AT 30 JUNE 2000 *(a) (b)*
($'000)

	Operating result prior to capital grants and extraordinary items		*Net cash inflows (outflows) from operating activities*		*Positive (negative) working capital position*	
Hospital	*1998-99*	*1999-00*	*1998-99*	*1999-00*	*1998-99*	*1999-00*
Mercy Public Hospitals Incorporated	1 011	**(1 355)**	5 775	**(2 570)**	(1 832)	**(3 818)**
Mt Alexander Hospital	528	**(483)**	1 503	**(7)**	(253)	**(885)**
Southern Health Care Network	61 415	**(24 915)**	8 022	**(8 808)**	(5 333)	**(21 406)**
Total	62 954	**(26 753)**	15 300	**(11 385)**	(7 418)	**(26 109)**

(a) Based on audited financial statements.
(b) Mildura Base Hospital not included as its acute health care component was transferred to a private operator.

3.2.23 **A further 13 hospitals had experienced an operating deficit prior to capital and extraordinary items for the 1999-2000 financial year and had a negative working capital position, (that is an excess of current liabilities over current assets) as at 30 June 2000, but had generated positive net cash flows from operating activities for the 1999-2000 financial year.**

3.2.24 It should be noted that while the Government acknowledged that certain hospitals were experiencing financial difficulties in the 1999-2000 financial year and committed additional funding to the sector, this funding was not provided until the 2000-01 financial year.

Review of projected financial performance to June 2001

3.2.25 In order to assess the ongoing condition of hospitals following the Government's 2000-01 budget initiatives and restructure of metropolitan health services, we analysed the projected financial performance for the year ending 30 June 2001 of the metropolitan health services, and certain other hospitals which had recorded unfavourable results in 2 or more financial indicators for the previous year.

3.2.26 Specifically, in relation to the metropolitan health services the information received indicates that they expect to record for the 2000-01 financial year:

- a deficit (prior to grants received for capital purposes and transactions of an extraordinary nature) of $106.3 million;
- net cash inflows from operating activities of $13.7 million; and
- a negative working capital position of $35.9 million.

3.2.27 There are 12 hospitals which, based on the hospitals subject to our analysis, are expected to be operating under financial difficulties as at 30 June 2001. These hospitals are shown in Table 3.2D.

TABLE 3.2D
PUBLIC HOSPITALS EXPECTED TO DISPLAY SIGNS OF FINANCIAL DIFFICULTY, AS AT 30 JUNE 2001 *(a)*
($'000)

Hospital	*Forecast operating result prior to capital grants and extraordinary items*	*Forecast net cash inflows (outflows) from operating activities*	*Forecast positive (negative) working capital position*
Bayside Health	(5 100)	(3 000)	(8 600)
Central Gippsland Health Service	(2 569)	(261)	(4 196)
Djerriwarrh Health Service	(154)	(84)	(214)
Mt Alexander Hospital	(764)	(207)	(1 783)
Peninsula Health	(11 701)	(2 108)	(5 200)
Portland and District Hospital	(1 853)	(346)	(1 184)
Southern Health	(7 000)	(9 505)	(35 252)
Rochester and Elmore District Health Service	(728)	(303)	(667)
Upper Murray Health and Community Services	(673)	(550)	(612)
Wangaratta District Base Hospital	(3 496)	(400)	(2 345)
Western District Health Service	(538)	(890)	(2 600)
Wimmera Health Care Group	(1 121)	(537)	(1 113)
Total *(b)*	**(35 697)**	**(18 191)**	**(63 766)**

(a) Based on projections provided by the hospitals which indicate negative results on the 3 indicators.

(b) In relation to metropolitan health services, the table does not include Austin and Repatriation Medical Centre; Dental Health Services Victoria, Eastern Health, Melbourne Health, Northern Health, Peter MacCallum Cancer Institute, Western Health and Women's and Children's Health which, based on the projections provided by the hospitals, indicate negative results on 2 of the 3 indicators.

Conclusion

3.2.28 **Despite the injection of supplementary funds over the past year or so, the financial condition of the public hospital system remains weak and vulnerable. Steps such as those recently undertaken to assess the viability of the financial structure of hospitals and the appropriateness of the casemix funding levels are positive initiatives designed to consider the underlying drivers of the financial performance in the sector. They may not, however, of themselves, challenge the cost-effectiveness of the current delivery mechanisms. Suitable financial structures need to be in place to reward innovation and cost-effectiveness if this ongoing issue is to be placed on a sounder footing in the future.**

RESPONSE *provided by Secretary, Department of Human Services*

Financial performance

The Report's calculation of the hospital sector's operating result for 1999-2000 includes capital expenses (depreciation), abnormal items and capital donations, but excludes capital income and extraordinary items. DHS's view is that that this calculation significantly understates the sector's performance because it does not match income with expenditure. As capital income is excluded, it follows that capital expenses should also be excluded. The public hospital sector, unlike the private sector, receives a separate stream of funding to pay for major new capital works and major items of equipment, and does not need to fund such capital expenditure from a charge for depreciation.

This measure is used by DHS in its financial monitoring of public hospitals and is consistent with the measure used in the Ministerial Review of Health Care Networks (dated May 2000). On this basis (excluding capital income, capital expenses, abnormal items, and extraordinary items), public hospitals overall achieved a small surplus of $23 million in 1999-2000.

The Government's 2000-01 budget provided an additional $242 million to acute health services to enable hospitals to meet growth in demand for both emergency and elective services, following a long period of budget restrictions. The Government also provided an additional equity injection of $35 million to 4 of the newly created metropolitan health services which had been identified in the Duckett Report as having inadequate liquidity.

The Report forecasts that metropolitan health services will end 2000-01 with a substantial deficit. As noted above, the measure used in the Report mismatches capital income and capital expenditure and so underestimates the financial performance of these hospitals.

In addition, it needs to be recognised that since information was provided from hospitals to the Auditor-General for this Report, a number of revenue payments from government have been resolved. These have improved the expected financial results of hospitals. These factors were:

- *a commitment made in March 2001 that the Department will assume the liability arising from the net increase on the long service leave provision of public hospitals;*
- *additional payments for inpatient services following adjustments to the formula used to measure the value of inpatient services; and*
- *recognition of infrastructure and other grants paid after January 2001.*

DHS estimates that public hospitals will report a small deficit for 2000-01 of up to $10 million. This is a preliminary estimate but reflects that prior to the 2000-01 budget, government had required significant savings from hospitals for a number of years. All metropolitan health services and other hospitals will publish annual reports with audited financial statements by September 2001.

Viability issues

Hospital Boards of Management, senior staff, and DHS closely monitor all metropolitan health services and hospitals, particularly those which are reporting financial difficulties. The Department, through the Acute Health Division and its regional offices, actively works with hospitals to facilitate the development and implementation of business plans which will result in the hospital achieving an acceptable financial result while maintaining quality services.

RURAL HOSPITAL INFORMATION TECHNOLOGY ALLIANCES

3.2.29 In the mid-1990s, the former Government recognised the need to improve information technology systems and management practices in Victoria's public hospitals. Existing systems for the effective management of hospital activities and reporting requirements were considered inadequate. An assessment of public hospitals' information technology capabilities was undertaken in 1996 by the Department of Human Services which identified that "*Victorian public hospitals were at least a decade behind other industry sectors and would not be able to support the emerging technology and knowledge based approach*".

3.2.30 To address these concerns, the Government initiated the Information, Information Technology and Telecommunications Strategy for Public Hospitals (I2T2 Strategy) to provide a framework for the development of information technology capability in public hospitals. The I2T2 Strategy, which was adopted by the Government in 1997 following consultation with metropolitan and rural hospitals and other health professional groups, consists of a 4-year period of phased change. The main programs of activity are:

- **Infrastructure** – comprising internal and external infrastructure, human and technical resources, and development of standards to support inter-operability and shared information;
- **Applications** – based on business and clinical priorities, and aimed at improving patient outcome and health service delivery;
- **Management Practice** – ensuring that organisational management and governance of information technology will support improvements in information capability and patient care;
- **Users of Information** – ensuring that clinicians, managers and other users of information have the capability and knowledge to use the information and technology in their work; and
- **Multi-year Investment Program and Risk Management** – recognising that a long-term investment commitment was required, and that risk needs to be carefully and strategically managed.

3.2.31 The scope of the I2T2 Strategy covers all services and facilities in Victorian public hospitals. Because each sector has a different set of priorities, the I2T2 Strategy addresses implementation arrangements for metropolitan and rural hospitals separately.

3.2.32 In 1997, the Department estimated the cost to implement the I2T2 Strategy at $350 million. To commence the project, the Department contributed initial funding of $5 million. The Department also made a commitment to provide further funding of $100 million over a 4-year period. Significant funding would also be provided by those hospitals participating in the I2T2 Strategy.

3.2.33 In January 2000, the Department commissioned a panel of external consultants to conduct a review of the I2T2 Strategy, whose key purpose was to review the progress, assess the impact of changing circumstances in the first 2 years of the implementation of the I2T2 Strategy and establish what needed to be done to deliver the I2T2 Strategy over the following 4-year period.

3.2.34 As previously mentioned, the I2T2 Strategy is being implemented in both metropolitan and rural public hospitals. **This audit report focuses on issues relating to the implementation of the I2T2 Strategy in the rural hospital sector.** Each public hospital located within one of the Department's 5 rural regions has established an I2T2 Strategy Alliance with the others in the region for the purpose of developing and implementing the I2T2 Strategy and an associated telecommunications service. The Department has approved the structure of the Alliances, which were originally established under a negotiated "*Heads of Agreement*" between all relevant parties to the Alliance.

3.2.35 **Currently, there are 68 rural hospitals (comprising 5 Lead Agencies and 63 participating hospitals) servicing in excess of 200 locations participating in the Alliances and although membership is voluntary, only one rural hospital has elected not to join a rural Alliance.** Table 3.2E below provides details of the 5 alliances established under the I2T2 Strategy, including the total number of participating hospitals.

TABLE 3.2E
RURAL HOSPITAL I2T2 STRATEGY ALLIANCES

Alliance	*Established*	*No. of hospitals*	*Lead Agency*
South West Alliance	September 1997	11	South West Healthcare
Grampians Alliance	September 1997	12	Ballarat Health Services
Loddon Mallee Alliance	March 1998	18	Bendigo Health Care Group
Hume Alliance	September 1997	17	Goulburn Valley Health
Gippsland Alliance	September 1997	10	West Gippsland Healthcare Group

3.2.36 As indicated in the above table, a Lead Agency has been nominated for each Alliance. The Lead Agency is appointed as the authorised agent with responsibilities for entering into contracts and undertaking other legal obligations on behalf of the Alliance and administering the finances of the Alliance. In addition, each Alliance has appointed a Chief Information Officer (CIO) to lead and co-ordinate the development and implementation of the I2T2 Strategy.

3.2.37 The scope of this audit review included a survey of all participating hospitals within the 5 Alliances, of which 48 provided responses, which accounts for 76 per cent of participating hospitals surveyed. In addition, information was provided by each of the Lead Agencies as part of this review.

Management framework

Agreements between the Lead Agency and the participating hospitals

3.2.38 The Alliances were originally established under a *"Heads of Agreement"* (Agreement). However, these Agreements provided only a basic framework for the operation of the Alliances and did not provide sufficiently for the rights and obligations of all parties to the Agreement. While 4 of the Alliances have continued to operate under these Agreements, the South West Alliance of Rural Hospitals (SWARH) was established under a *Joint Venture Agreement*, which was signed by all of its participating hospitals in February 1999.

3.2.39 The *Joint Venture Agreement*, which was established, clarifies the legal status of SWARH and provides a more comprehensive framework for the operations of the Alliance. The *Joint Venture Agreement* includes the aims and objectives of the Alliance, the obligations and responsibilities of the Lead Agency and the participating hospitals, empowers the Lead Agency to enter into and manage contracts on behalf of the Alliance, and outlines dispute resolution procedures and governing law.

3.2.40 The remaining Alliances are currently negotiating new contractual arrangements to govern the operations of their Alliance.

3.2.41 As part of the audit survey, participating hospitals were requested to identify any additional provisions their Agreements should contain. The responses received indicated that there is a need for the formalisation of the distribution of resources, the apportionment of costs, the designation of the rights, responsibilities and accountabilities of Alliance members, and the need to incorporate penalties for poor performance.

3.2.42 The responses to the audit survey indicate that the absence of a formal Agreement gives rise to confusion over responsibilities and difficulty in accessing the CIO, and results in the needs of bigger participating hospitals having priority over the smaller participating hospitals.

Alliance Steering Committees

3.2.43 Each Alliance has a Steering Committee comprising representatives (usually the Chief Executive Officer) of all participating hospitals and the Lead Agency. The major responsibilities of the Steering Committee are to develop and implement the I2T2 Strategy, manage the Alliance finances and report on the financial performance of the Alliance. Each Alliance Steering Committee meets on a regular basis, generally monthly.

3.2.44 Of the hospitals that responded to the audit survey, 81 per cent of the participating hospitals were of the view that they had adequate representation in the decision-making process via their representation on the Steering Committee and the various sub-committees established for specific tasks. Of those responses indicating that they did not have adequate representation in the decision-making process, a significant proportion were from the Loddon Mallee Alliance. The reasons given were that the interests of the bigger participating hospitals tend to dominate the interests of the smaller participating hospitals.

Funding arrangements

3.2.45 **In 1997, the Government announced an initial package of $5 million to support early initiatives in the implementation of the I2T2 Strategy and made a further commitment to spend $100 million over a 4-year period, to be allocated across metropolitan and rural public hospitals.**

3.2.46 Under the 1997 proposal, the Department's I2T2 Strategy 4-year budget allocation was $25 million per annum. Table 3.2F details the budget allocation and actual funding provided by the Department over the 4-year period from 1997-98 to 2000-01. Funding provided by the Department is for expenditure of a capital nature, with ongoing expenditure to be funded from within the individual hospitals operating budget.

TABLE 3.2F
I2T2 STRATEGY FUNDING BY THE DEPARTMENT
BUDGET ALLOCATION AND ACTUAL FUNDING FROM 1997-98 TO 2000-01
($million)

Funding	*1996-97*	*1997-98*	*1998-99*	*1999-00*	*2000-01*	***Total***
Proposed funding	5.0	25.0	25.0	25.0	25.0	**105.0**
Actual funding	-	*(a)* 30.0	25.0	12.5	12.5	**80.0**

(a) 1996-97 proposed funding of $5 million provided in 1997-98.
Source: Department of Human Services.

3.2.47 As the above table shows, the Department did not fund the I2T2 Strategy at the proposed funding level of $25 million per annum for the first 4 years. **The actual funding for the 1999-00 and 2000-01 years was only 50 per cent of the proposed funding for each financial year. This action by the Department created an element of uncertainty in the funding arrangements and has placed additional funding demands on the hospitals where these hospitals have entered into long-term contracts and were dependent on a secure cash flow from the Department over this period.**

3.2.48 At the time the Strategy was prepared in 1997, the full impact of the Year 2000 (Y2K) issue was not known and, consequently, the I2T2 Strategy did not allow for specific funding to meet Y2K compliance requirements. While specific one-off funding for the Y2K remediation was provided by the Department under separate funding arrangements, I2T2 Strategy funding for the 1999-2000 financial year was also used by hospitals towards meeting the Y2K compliance requirements.

3.2.49 **To compensate for the funding shortfall and in recognition of the delay in the progress of the I2T2 Strategy due to the impact of the Y2K issue, the Department has extended the timeline of the Strategy for another 2 years with projected funding for 2001-02 of $12.5 million and for 2002-03 of $7.5 million. Subsequent to the 2002-03 financial year, all IT-related expenditure will have to be met from the participating hospitals' operating budget.**

Funding to rural hospital I2T2 Strategy Alliances

3.2.50 Table 3.2G details the actual I2T2 Strategy funding received by the Alliances from the Department since 1997.

TABLE 3.2G
FUNDING FOR I2T2 STRATEGY RECEIVED BY THE ALLIANCES FOR IT INFRASTRUCTURE AND APPLICATIONS
($million)

Alliance	*1997-98*	*1998-99*	*1999-00*	*2000-01*	***Total***
South Western Alliance	0.96	0.61	0.32	0.33	**2.22**
Grampians Alliance	1.19	0.91	0.46	0.48	**3.04**
Loddon Mallee Alliance	1.49	1.16	0.59	0.58	**3.82**
Hume Alliance	1.56	0.90	0.55	0.56	**3.57**
Gippsland Alliance	1.24	0.99	0.49	0.52	**3.24**
Total	**6.44**	**4.57**	**2.41**	**2.47**	**15.89**

Source: Department of Human Services.

3.2.51 In addition to funding received for the I2T2 Strategy, the Alliances also received funding from the Department for non-information technology assets associated with this Strategy. The following table shows the additional funding received by all 5 Alliances for the period 1997-98 to 2000-01.

TABLE 3.2H
I2T2 STRATEGY FUNDING RECEIVED BY THE ALLIANCES FOR NON-IT ASSETS, 1997-98 TO 2000-01
($'000)

	South Western Alliance	*Grampians Alliance*	*Loddon Mallee Alliance*	*Hume Alliance*	*Gippsland Alliance*
Chief Information Officer	301	301	301	301	301
Change Management	77	150	98	178	70
I2T2 Strategy Plans	85	-	85	85	85
Telecommunications Plans	35	-	-	30	30
Set Up	50	30	55	30	30
Year 2000	100	100	100	100	100
Additional Rural Support	80	90	100	100	90
Supplementary Funding *(a)*	28	41	52	48	43
Other	-	150	-	-	-
Total	**756**	**862**	**791**	**872**	**749**

(a) Includes GST implementation costs.
Source: Department of Human Services.

3.2.52 In each Alliance, the allocation of the I2T2 Strategy funding to participating hospitals is determined by their respective Steering Committees, having regard to submissions from the various sub-committees established for particular purposes. Within all Alliances, funding to participating hospitals is for the most part allocated on a needs basis.

3.2.53 As part of the audit survey, participating hospitals were requested to advise whether they agreed with the allocation of the available funding to their particular hospital. **Eighty-one per cent of hospitals that responded to the survey believe they have received an equitable share of the available funds.**

3.2.54 The CIO plays a crucial role within each Alliance and is seen as pivotal in leading and managing the expectations of Alliance members and in guiding the decision-making process. Funding for the CIO position was initially guaranteed to, and including, the 2000-01 financial year. As a special concession to the rural Alliances, the Department has extended its funding for the CIO position to, and including, the 2001-02 financial year. After this period, the funding for the CIO position will have to be found by the Alliances from within their operating budget.

Strategy plans

3.2.55 All 5 Alliances have comprehensive strategy plans for the implementation of the I2T2 Strategy. These plans were developed in conjunction with external consultants and approved by the respective Alliance Steering Committee. Projects implemented under these plans are monitored by the Steering Committees. The strategy plans are regularly reviewed to take account of the ongoing I2T2 Strategy needs of the participating hospitals and to take into account current developments in technology.

3.2.56 **The progress in the implementation of the I2T2 Strategy has been impacted as a result of the diversion of the related funding to address the Y2K issue and the decision of the Department to delay the flow of funds to implement the Strategy. During the 2002-03 financial year, a detailed review will need to be undertaken to determine whether the I2T2 Strategy has been fully implemented and the Alliances have the capacity to fully support, on an ongoing basis, their enhanced IT systems and procedures.**

Confidentiality and security over information

3.2.57 As the introduction and development of sophisticated management information systems in the health sector continues, privacy and confidentiality of patient care information and security of patient records databases is a major emerging issue for the sector. The increased availability of on-line services and web-based technologies under the Alliances represents a risk to confidentiality of patient care information in rural hospitals.

3.2.58 To protect the privacy of health information held in both the public and private sectors, the Government has recently enacted the *Health Records Act* 2001.

3.2.59 **All participating hospitals responding to the audit survey considered that adequate controls exist to ensure the security of confidential information contained on their databases. The controls identified were password security, restricted access to systems and applications, network firewall security to prevent external access, virus protection and regular backup of systems.**

Training for users of information technology

3.2.60 The Lead Agencies have the responsibility of identifying and co-ordinating the training requirements for its participating hospitals. The audit survey requested advice as to whether IT training was adequately provided under the Alliance. The majority of the participating hospitals (87 per cent) who responded to the survey indicated that they received IT training. Some examples of training provided are e-mail and internet usage, training on the use of new systems such as finance systems, payroll/human resources system, patient information systems and administrative support applications.

3.2.61 Of the participating hospitals that indicated they have received IT training, 61 per cent indicated that the training did not adequately satisfy the operational needs of their hospital. Issues raised relate to the timeliness and quality of the training and that training was focused on the needs of the larger participating hospitals within the Alliances. Most identified the need for ongoing training to maintain and stay abreast of changes and updates, post-implementation training for all applications, further training for IT staff, new and casual staff, and for staff moving into different areas of hospital operations.

3.2.62 **Currently, post-implementation training is not funded by the Alliances but funded by participating hospitals through their operating budget. Accordingly, smaller hospitals may have difficulty meeting the funding commitments for the post-implementation training necessary for them to keep up-to-date with the IT developments within their Alliance.**

Technical support for information technology

3.2.63 To maximise the capability of the new systems acquired under the I2T2 Strategy, hospitals need to have access to IT support and expertise. The audit survey requested advice whether participating hospitals had sufficient IT expertise or access to IT expertise to maximise the IT facilities acquired. **Forty-six per cent of the respondents indicated they did not have the necessary IT expertise to maximise the IT facilities acquired under the I2T2 Strategy. Many identified a need for dedicated or additional IT staff and additional funding for IT resources.**

Financial reporting

3.2.64 The Lead Agency, on behalf of its Steering Committee and participating hospitals of the Alliance, is required to maintain a separate *Special Purpose Trust Fund* for the purpose of administering the financial transactions associated with the I2T2 Strategy.

3.2.65 The Lead Agency is responsible for the preparation of the financial reports associated with the I2T2 Strategy for distribution to participating hospitals for annual financial reporting purposes. Each participating hospital recognises their share of the I2T2 Strategy assets, liabilities, revenue and expenditure separately in their annual financial reports.

3.2.66 The audit survey requested advice from participating hospitals as to whether the financial information supplied by the Lead Agency was adequate and reliable for their annual reporting needs and if this information was provided on a timely basis. The majority of the respondents (73 per cent) indicated the information provided was adequate and reliable for their annual reporting needs. The respondents indicating a lack of detail in financial information provided were members of the Gippsland and Loddon-Mallee Alliances.

3.2.67 **Furthermore, 40 per cent of hospitals that responded indicated that financial information was not provided on a timely and regular basis**. Those indicating a problem with the timeliness of financial information were members from the Gippsland, Loddon-Mallee and Hume Alliances. Alliances have already identified this as an issue and have taken appropriate action to ensure that in future detailed financial information is provided on a timely basis.

Key achievements and benefits arising from rural I2T2 Strategy Alliances

3.2.68 The Department has identified the following key achievements in the rural alliances resulting from the overall I2T2 Strategy:

- development of Local Area Networks within each hospital to industry standards;
- upgrade of existing internal infrastructure to industry standard common infrastructure;
- introduction of common patient management and financial systems applications;
- implementation of e-mail for faster communication;
- collective purchasing power of the hospitals in acquiring IT;
- information exchange; and
- development of a model for effective change in the rural Victorian health sector.

3.2.69 **The audit survey revealed that participating hospitals were receiving significant benefit from their membership of an Alliance.** Standard infrastructure and applications have been implemented in each of the Alliances. Consequently, the benefits reported by hospitals within their Alliances were of a similar nature. The major benefits identified from the survey were as follows:

- access to the latest IT technology and common IT infrastructure which could not be obtained through their own resources;
- access to external IT expertise for operational needs, including assistance with the development of the strategic IT plan;
- improved communication capabilities, including new telephony systems, e-mail and internet access, video conferencing and voice calls;
- standardised patient administration systems and financial systems; and
- sharing of information and regular exchange of ideas.

Conclusion

3.2.70 In adopting the I2T2 Strategy in 1997, the Department recognised that a long-term investment commitment was needed to improve information technologies and service delivery capabilities in Victoria's hospitals. **While substantial benefits have been realised by participating hospitals under the Alliances, the Y2K issue and the delay in the flow of funds associated with the implementation of the Strategy have impacted on the progress of implementation of the I2T2 Strategy.**

3.2.71 To build on the achievements to date, the Department needs to ensure that the I2T2 Strategy is fully implemented and that the Alliances have the capacity to fully support, on an ongoing basis, their enhanced IT systems and processes.

3.2.72 The establishment of the rural alliances to provide IT facilities to rural hospitals represents a new model of operating initiated by the Department**. This model has successfully delivered benefits in the form of up-to-date IT technologies to all participating hospitals** through collaboration and co-operation, which would otherwise not have been achieved by individual hospitals, while at the same time maintaining their operational independence. **The results achieved under the Alliances model to date should encourage the Department to utilise this approach in other operational areas in rural hospitals.**

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

We agree that the Alliance model used for the rural hospitals in the I2T2 Strategy has been a major success factor in the delivery of benefits.

The Report is timely in that the issues raised and the conclusions support the direction the Department would like to take for information technology in the health sector. Closer collaboration with the rural Alliances and all hospitals is being actively encouraged to ensure integrated information and outcomes are delivered to benefit and inform the health system as a whole.

The Department is acutely aware of the issues of sustainability and ongoing funding for information technology in hospitals and health services. In line with an increased community demand for healthcare there is an increasing demand for quality health information and technology to better manage demand and more appropriately targeted services.

The rural sector, in particular, is grossly under serviced by telecommunications infrastructure that is critical to connectivity and communication stakeholders in the health system. The use of the Alliance model has been a valuable tool in establishing a resource base for acquisition and management of these technologies.

The I2T2 Strategy was designed to be a 4-year phased implementation of information and communications technology in the hospital sector with an estimated cost of $350 million. The Strategy was launched by the previous Government in 1997 with a funding commitment of $100 million. No additional funding was, in fact, allocated during the period, and the funding that was provided to hospitals was through internal reallocation of departmental resources. This led to a situation where, after 2 years, only $12.5 million was available. The duration of funding was extended for 2 years but with further reductions in funding.

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

The Department is in the process of establishing a Health Information and Information and Communication Technology Steering Committee to co-ordinate activities across the health portfolio and develop an integrated health information technology strategy that will incorporate hospitals, aged, mental and community-based services. This will include identification of the costs of information technology to support priority health reforms and an integrated health care model.

Processes have been established to address the issues in the Report regarding accountability and governance. Specifically, the Department (as part of the ongoing work of the Business Support and Development Group, Acute Health) will continue to work closely with the Alliances and member hospitals to:

- *Ensure all rural hospital Alliances have legal agreements in place within 6 months to improve governance and risk management;*
- *Further develop Statewide collaboration and planning which will support sustainability of rural hospital Alliances, including implications for ongoing funding, Chief Information Officer positions and support structure, management practice and governance, opportunities for consolidation and other issues specific to information and communications technology in the rural health sector beyond 2002-03;*
- *Develop a strategy for training users and information technology personnel, including innovative models such as e-learning, partnerships with hospitals with comparative technology and establishment of training and support networks;*
- *Develop and implement standards and business rules for accountability and financial reporting as part of the governance mechanism for each Alliance; and*
- *Conduct a post-implementation review of the I2T2 Strategy to identify benefits delivered and opportunities for leverage from the Alliance model.*

POST-ACUTE CARE PLANNING

EXECUTIVE SUMMARY

Introduction

3.2.73 The Victorian health system continues to experience increasing pressures, with growing demand for services but limited resources. These demands are due to a range of factors, including population ageing and growth, changes in clinical practice and treatment patterns, advances offered by new technologies, the introduction of new drug treatments and increased consumer expectations. Response to these pressures is requiring a rebalancing of the health system, with attention to priorities for resource allocation.

3.2.74 Over the past decade, there have been significant changes in acute health care[1], including declining patient length of stay in acute hospitals[2]. As a result of leaving hospital earlier, patients are increasingly receiving care in the community, subsequent to discharge, or "post-acute". In some cases, advances in medical technology and treatments mean that, compared with the past, the inpatient experience is less intrusive and care requirements are less after discharge from hospital.

3.2.75 Where services are required during the post-acute phase, they may include personal care, allied health services including physiotherapy and occupational therapy, home help from community support agencies or home nursing for treatments such as wound management. These services can be accessed from a range of service providers, including hospitals (ambulatory care services), primary care sector (general practitioners, allied health providers, community health services etc.) and home and community care providers including local government.

Audit objectives and scope

3.2.76 The audit assessed whether the Department of Human Services adequately managed its response to the pressures on post-acute and sub-acute care services resulting from changes in the nature of health service delivery. The audit examined changes over the past decade, but data availability limited analysis in many cases to more recent years.

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1 According to the Australian Institute of Health and Welfare *National Health Data Dictionary, Version 8.0, 1999, "an episode of acute care for an admitted patient is one in which the principal clinical intent is to do one or more of the following: manage labour (obstetric); cure illness or provide definitive treatment of injury; perform surgery; relieve symptoms of illness or injury (excluding palliative care); reduce severity of illness or injury; protect against exacerbation and/or complications of an illness and/or injury which could threaten life or normal functions; and perform diagnostic or therapeutic procedures"*. Acute care is generally provided to admitted and non-admitted patients in a hospital or institutional setting, but may be provided in the home under the care of hospital staff.

2 Acute hospitals are *"establishments that provide at least minimal medical, surgical or obstetric services for inpatient treatment and/or care, and which provide round-the-clock comprehensive qualified nursing service as well as other necessary professional services"*, ibid.

3.2.77 The audit:

- described the context and trends in post-acute and sub-acute services in Victoria; and
- reviewed the strategic planning, program monitoring and evaluation practices of the Department.

Audit conclusion

3.2.78 Over the past decade, initiatives to relieve the pressure on acute care services were, and continue to be, a high priority for the Department. In recent times, strategic planning across the health system has received greater focus. In this context, and in response to the increasing demand for post-acute and sub-acute care, some small-scale flexible policy and funding models for integrated services have been developed, both at State and Commonwealth levels.

3.2.79 In the latter part of the last decade, the Department, particularly through its Acute Health Division, has introduced a range of innovative programs and initiatives to address the demand for services in the sub-acute and post-acute sectors. Despite these innovations, limitations in available data precluded us from making a definitive judgment on the adequacy of the Department's actions.

3.2.80 This partly reflects the complexity of policy, funding and service arrangements for post-acute care, which restricts the capacity of the Department to directly manage post-acute care service provision and limits the availability of data to monitor the sector.

3.2.81 Our audit concluded that the Department has not adequately monitored or consistently evaluated the effectiveness of the service delivery models for the provision of post-acute care. In our view, the Department's performance indicators are not yet comprehensive and some important indicators (such as patient satisfaction) have not been collected and/or reported in recent times.

Audit findings

Demand for post-acute care services

3.2.82 There is increasing demand for post-acute care services due to:

- *Decreasing length of stay and bed availability in acute hospitals and in rehabilitation services.* There has been a growing demand within Victoria for acute inpatient services, in a period of declining numbers of inpatient beds. Between 1990-91 and 2000-01, the total number of patients treated in Victorian acute public hospitals increased by 62 per cent. However, the number of available beds in public hospitals fell by 4.1 per cent from 1992-93 to 1998-99, and rose again in 1999-2000 to be slightly above the 1992-93 level. The average length of public hospital stay for all patients decreased from 5.7 to 3.8 days from 1990-91 to 2000-01. Similarly, the average length of stay for patients receiving rehabilitation on an inpatient basis also reduced, from 26.3 days in 1996-97 to 17.0 days in 1998-99, although some of this decline reflects new initiatives such as transferring patients to community-based services. These declines in length of stay indicate that there may be more people requiring and seeking services in the community who may, in the past, have spent longer in hospital or rehabilitation;
- *Weaknesses in discharge effectiveness.* Unplanned readmission to hospital may indicate a lack of timely and effective post-acute or community care following hospital discharge. However, this measure has a number of difficulties. There is debate about the validity of unplanned readmission rates as an indicator of quality of care, unplanned readmission rates have not been published since 1997-98, benchmarking with other jurisdictions is difficult, and a more valid indicator of unplanned readmissions for the same or a related condition which was to be developed is still not available. An audit of patient records in June 2000, by an external consultant engaged by the Department, found that 45 per cent of hospitals had low compliance with the discharge standard developed for the audit. The audit identified major obstacles to the planned discharge of patients, including:
  - a lack of community health and welfare services, especially in rural areas (39 per cent of hospitals);
  - a lack of appropriate accommodation, particularly for elderly patients and in rural areas (29 per cent of hospitals);
  - poor communication and co-ordination between medical staff, general practitioners, and those parts of the hospital involved in discharge planning (24 per cent of hospitals); and
  - the attitudes and expectations of patients and their carers/families, including reluctance to go home and differing expectations of the health services between patients/carers and the hospitals (22 per cent of hospitals).

  This data indicates weaknesses in discharge effectiveness that would affect provision of post-acute care;

- *Patient perceptions of a need to improve discharge from public hospitals.* According to the Department's latest patient satisfaction survey conducted in 1997, the majority of patients (82 per cent) regarded the duration of their hospital stay as about right, with 11 per cent perceiving it as too short and 7 per cent as too long. Ninety-two per cent of respondents said they were given adequate notice of discharge, but a number of responses addressing the adequacy of information provided at discharge showed this was clearly a key area for improvement;
- *The swift take-up of projects funded under the Post-Acute Care Program.* The number of patient referrals to, and throughput for, the Post-Acute Care Program has increased steadily (347.9 per cent increase in new referrals and a 536.3 per cent increase in the number of episodes completed by post-acute care projects between 1996-97 and 1999-2000). This reflects an increasing number of projects and the swift take-up by patients as soon as places become available; and
- *Decreases in community care-type services provided by hospitals on an ambulatory basis.* During 1996-97 to 1998-99, while the reported number of non-admitted occasions of service provided by public hospitals was almost unchanged, community health services, district nursing services and other outreach services offered by public hospitals within Victoria declined. This may be partly due to some of these services now being provided outside the hospital sector.

New departmental initiatives

3.2.83 The Department has undertaken a number of relevant initiatives to enhance the provision of post-acute and sub-acute care, including:

- providing rewards and incentives for innovation and good practice (e.g. the Effective Discharge Strategy bonuses, and the Human Services Productivity Investment Fund);
- encouraging pilot projects to test new initiatives (e.g. the Post-Acute Care Program and the Continuum of Care model); and
- encouraging sharing of ideas between service providers and across jurisdictions (e.g. the Victorian Collaborative Breakthrough Series and the Victorian Centre for Ambulatory Care Innovation).

Assessing the Department s management of the changes in post-acute care

3.2.84 We assessed the Department’s management of post-acute care in the following areas and identified a number of matters where improvement is required:

- Strategic planning is essential to improve the quality of information available for decision-making and resource allocation so that service offerings mirror the emerging health needs of the community. Until recently, the Department gave insufficient attention to strategic planning across the health system. While the Department has access to, and collects considerable quantities of, data from providers of post-acute and sub-acute health services, there are data gaps, non-standard units of service and costs, and no mechanism that enables tracking of patient experiences through the system. The standard of documentation within the Department is poor and procedures for handover of key information when staff change have not been established, reducing accountability and risking the loss of corporate knowledge;
- A good policy and funding framework for post-acute care would encourage a focus on patient outcomes; give service providers the flexibility to provide, or enable patient access to, integrated services that meet patient needs; minimise program boundaries and duplication of services between levels of government that lead to inefficient service provision and difficulty for individuals navigating available services; and set clear quality standards, monitor their achievement and respond to the issues raised in such monitoring. The existing policy and funding framework requires much improvement in all these areas, although some flexible policy and funding models that provide integrated services have been developed at the State and Commonwealth levels. These include the Department’s Primary Care Partnerships Strategy and Healthstreams Program and the Commonwealth’s Multi-Purpose Services and Coordinated Care Trials. However, these initiatives have been small and have yet to demonstrate their broad applicability, although a recent evaluation of the Multi-Purpose Services Program concluded favourably on the effectiveness of the model for small rural communities. Continued co-ordination between the Department and the Commonwealth is required to reduce system complexity and duplication of services given the proliferation of programs and initiatives;
- Some encouragement of innovation and improved service delivery for services in the sub-acute and post-acute sectors occurred in the latter part of the decade. However, because of the limitations in the available data, we were unable to determine the adequacy of this action; and

- Program monitoring and evaluation which informs future strategic planning has been variable and has progressed slowly, with delays in developing indicators, non-collection and/or non-reporting of some important indicators (such as patient satisfaction) and limitations in the data available for performance monitoring and evaluation. Consequently, the Department cannot currently adequately monitor the effectiveness of post-acute care provision. To do so requires a more consistent and effective approach to program evaluation, including integrating evaluations into the design of programs, timing them to support decision-making, using them to develop effective performance measuring and monitoring regimes and allocating funds to evaluation activities.

Recommendations

3.2.85 A list of recommendations contained in the Report is set out below.

Report reference	*Paragraph number*	*Recommendation*
Assessing the Department's management	3.2.171	A co-ordinated approach should be taken by the Acute Health and Aged, Community and Mental Health Divisions to address data limitations. Particular consideration should be given to establishing consistent bases of counting across programs and across the service system. In order to facilitate analysis of data over extended periods of time, whenever new counting rules are introduced for programs consideration should be given to maintaining parallel counting for a period of time.
	3.2.176	The Department should take early action to improve documentation maintained on departmental policy and program files and to develop appropriate arrangements for handover and transition of activities.
	3.2.199	The Department needs to ensure that there is continued co-ordination between Divisions and with the Commonwealth for post-acute care services to avoid systems complexity and duplication of services, given the proliferation of programs and initiatives.
	3.2.228	The Department should address its inadequate monitoring of the effectiveness of the service delivery models for the provision of post-acute care, in particular the non-collection and/or reporting of some important indicators (such as patient satisfaction).
	3.2.239	The Department should establish a more consistent approach to program evaluation that requires integrating evaluations into the design of programs, timing them to support decision-making, using them to develop effective performance measuring and monitoring regimes and allocate funds to evaluation activities.

RESPONSE *provided by Secretary, Department of Human Services*

General

The Report acknowledges the complexity of this subject and the fact that initiatives to provide appropriate post-acute care to patients and to relieve the pressure on acute health care services have been, and continue to be, a high priority for the Department. The Department is pleased to note that the audit has commented favourably on a range of innovative programs initiated by the Department over the past few years.

Co-ordination and documentation

The Department acknowledges the need to improve data consistency and to ensure that there is close co-ordination between Divisions and with the Commonwealth. The Divisions of the Department will work together to address these issues and to improve documentation as suggested.

Performance indicators

The Department agrees that performance indicators to monitor the effectiveness of provision of post-acute care are not yet comprehensive but does not believe that the Report adequately acknowledges the conceptual and practical issues associated with development of a comprehensive set of performance indicators. There is no set of agreed valid indicators that are readily applicable to the Australian health care delivery system. There has been substantial and intensive work undertaken over the last few years to develop such indicators in Victoria. The Department has, for example, specifically commissioned work on effective discharge indicators as part of its Effective Discharge Strategy. In 2000-01, performance indicators for effective discharge were developed. Issues such as poor communication and co-ordination between medical staff, general practitioners and other parts of the hospital involved in discharge planning have been specifically considered – for example the indicator set includes measures for timely notification of community providers and a discharge summary to general practitioners within one day of discharge. These indicators will be implemented from 2001-02. The Commonwealth-funded study of unplanned readmissions concluded that this indicator was unsuitable for direct, external comparisons of hospital-wide performance, although they believed that it remained useful for quality improvement purposes within individual hospitals and for specific conditions and procedures. The Department dropped publication of unplanned hospital readmission rates as a result of the findings of this report and believes that the concerns expressed in 1998 about the validity and reliability of this indicator remain valid today. The Department has continued to commission ongoing work on appropriate clinical indicators and will continue to do so.

The Report also criticises the Department for a delay of 4 years in instituting the Patient Satisfaction Monitor. During the period between the conduct of the last survey in 1997 and the adoption of the current monitor the Department was undertaking the work required to investigate options and develop a system for regular patient satisfaction monitoring. It did not undertake an additional one-off survey - these are extremely expensive exercises and the decision was made to invest resources in investigating the best ways to undertake an ongoing survey. The Patient Satisfaction Monitor started in Victorian acute care hospitals in September 2000 for a 3-year period. It will provide regular, ongoing monitoring and reporting of patient satisfaction in key areas of service delivery in Victoria including discharge and follow up arrangements. In addition, work will start in 2001-02 specifically on ways to better elicit and act on patient satisfaction indicators specific to post-acute care including patient and carer experience. Other indicators for post-acute care may include community provider experience, and referring hospital experience. Stakeholders will be consulted in the development of these indicators.

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

Number of programs

The Department agrees that it is important that the various programs within Human Services, and between the Commonwealth and State, continue to communicate to minimise duplication and service gaps, and for communication between service providers at a local level to optimise effective service delivery.

Standard unit costs for post-acute care

The Report comments on the absence of standard units of service and standard unit costs for post-acute care services. The Department has specifically not set standard unit costs for the purchase of services in post-acute care. The reason is that at times a premium must be paid in order that patients can gain timely access to services, and in certain areas of the State, services will cost more because of difficulties accessing certain types of care or because of the patients' geographic location. The Post-Acute Care Program has intentionally kept flexibility as one its prime objectives so as to best meet the individual needs of patients discharged from hospital.

Primary care partnerships

Regular, 6 monthly, reporting is built into the Primary Care Partnerships Evaluation Framework. This will ensure regular flow of information from the evaluation for the purpose of refining implementation strategies. The initial report (December 2001) will include analysis of results of process evaluation including progress on the establishment of Primary Care Partnerships and the development, revision and finalisation of Community Health Plans. This information will assist the Department and Primary Care Partnerships refine strategies to strengthen Partnerships, improve planning processes and support effective implementation of Community Health Plans. Medium-term evaluation reports (June and December 2002) will provide information about the early effects of the Primary Care Partnerships on the quality of service provision and initial impacts on consumers. Data on consumer experiences will be used by Primary Care Partnerships to refine the design of innovative models of service delivery, particularly those under the Better Access to Services, Integrated Disease Management and Health Promotion streams of the Primary Care Partnerships. The final evaluation report (June 2003) will incorporate available data on consumer outcomes, provide an analysis of causal relationships between inputs, processes, impacts and outcomes, and assess the effects of the Primary Care Partnerships on the primary care service system as a whole.

Conclusion

The Department recognises that there continue to be major challenges to meet the needs of patients following an acute episode of care. It will continue to develop and evaluate the effectiveness of a range of programs to meet the needs of various client groups, recognising that there needs to be co-ordination of approaches both across Divisions of the Department and with the Commonwealth. The Department would like to acknowledge the audit team and thank them for their professional and co-operative approach to the conduct of this audit.

CONDUCT OF THE AUDIT

Audit objective

3.2.86 The objective of this audit was to assess whether the Department of Human Services adequately managed its response to the pressures on post-acute and sub-acute health care services as a result of changes in the nature of health service delivery over the past decade. In particular, the audit:

- describes the changes in activity throughout the decade in acute, sub-acute and post-acute care and the level of resources;
- determines whether the Department of Human Services has planned for, and implemented service offerings which respond to, the demand for services in the sub-acute and post-acute sectors; and
- assesses whether comprehensive performance measures and evaluative processes have been developed to monitor the effectiveness of this response.

Audit approach

3.2.87 The audit examined changes over the past decade, but data availability has limited analysis in many cases to more recent years. The audit:

- Described the Victorian health system and the changes over the past decade using qualitative data on health care system trends from international, national and State perspectives; and quantitative and qualitative data identifying trends in acute, post-acute and sub-acute services at national and State levels; and
- Reviewed the strategic planning, program monitoring and evaluation practices of the Department, having regard to the changes in health service delivery for post-acute and sub-acute care over the past decade. Focusing within the Acute Health, Aged, Community and Mental Health, and Policy and Strategic Projects Divisions of the Department, the audit included file examinations and interviews with departmental staff in policy development and program areas.

Compliance with auditing standards

3.2.88 The audit was performed in accordance with Australian Auditing Standards applicable to performance audits and, accordingly, included such tests and other procedures considered necessary in the circumstances.

Assistance to the audit team

3.2.89 Health Outcomes International Pty Ltd, a firm of health and community care consultants, was engaged to assist the audit team describe the changes in the Victorian health system over the past decade.

3.2.90 Significant support and assistance was provided to my officers and Health Outcomes International Pty Ltd by the management and staff of the Acute Health, Aged, Community and Mental Health, and Policy and Strategic Projects Divisions of the Department of Human Services. I wish to express my gratitude to the Department for this assistance.

BACKGROUND

3.2.91 Our May 1998 Special Report No. 56 *Acute health services under casemix: A case of mixed priorities* reported there was a case for further examination of the pressures placed on the non-hospital sector through the earlier discharge of patients from public hospitals. At that time, concerns were raised by clinicians regarding the availability of both community services for patients on discharge, and places in nursing homes and special accommodation. Further reductions in the length of stay in the ensuing years and the possibility of continued pressure on the providers of post-acute care led to the decision to undertake this audit.

3.2.92 International comparisons show that Australians enjoy good health, and that the underlying health trends are broadly in step with health improvements occurring in other developed countries. In the recent *World Health Report 2000*, the World Health Organisation ranked Australia as the twelfth highest attaining nation in terms of overall health system performance, and second in terms of overall health status.

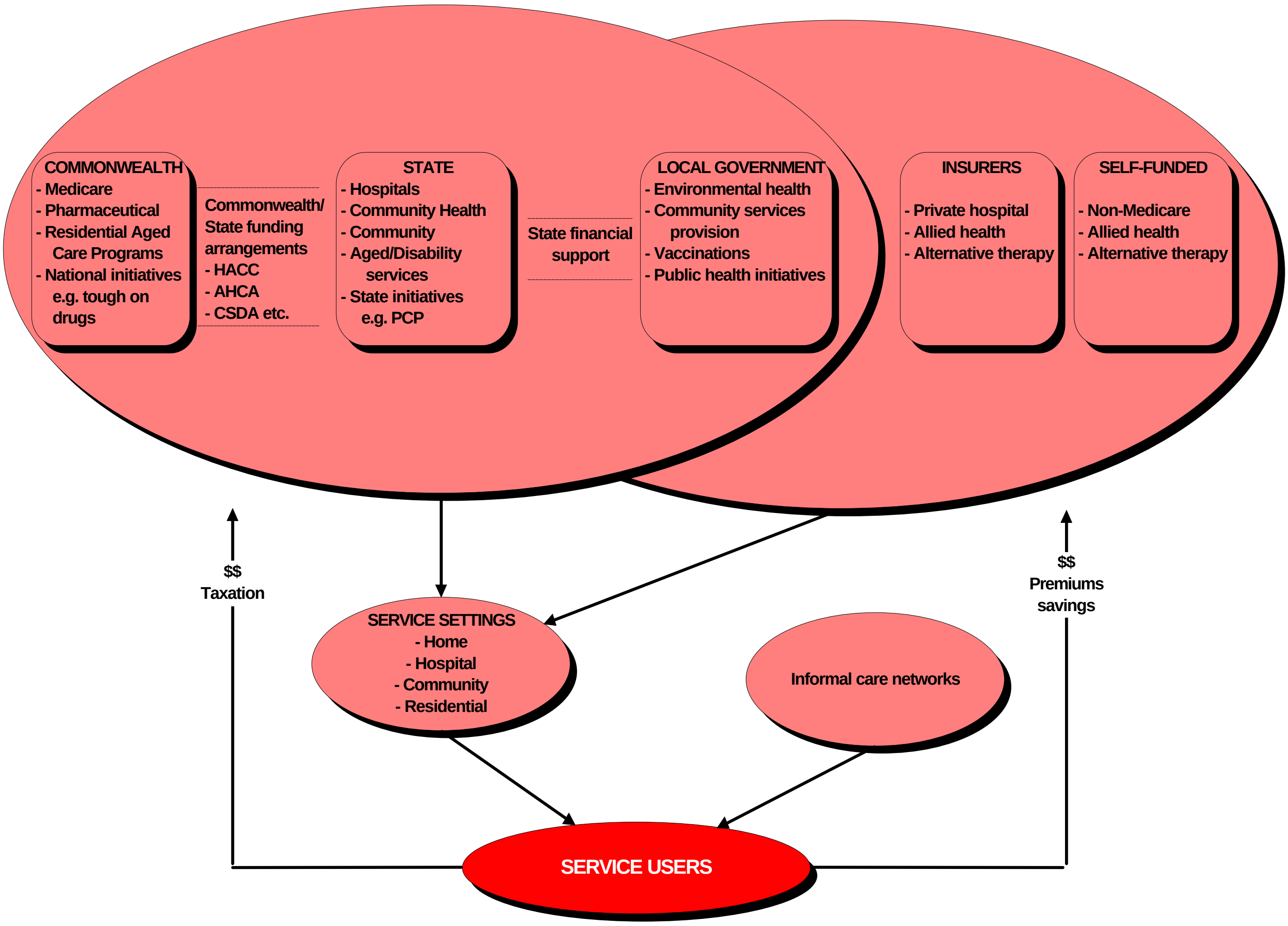
3.2.93 The Australian health system is complex, with many types and providers of services, and a range of funding and regulatory mechanisms. Service providers include medical practitioners, other health professionals, private and public hospitals, aged care facilities and other government and non-government agencies. Funding is provided by the Commonwealth Government, State and Territory Governments, health insurers, individual Australians and from a range of other sources.

3.2.94 The Victorian health system is experiencing increasing pressures, with growing demand for services but limited resources. These demands are due to a range of factors, including population ageing and growth, changes in clinical practice and treatment patterns, advances offered by new technologies, the introduction of new drug treatments and increased consumer expectations.

Priority setting in the health system

3.2.95 The Australian and Victorian health systems are a pluralistic and complex mix of responsibilities and funding arrangements, as depicted in Chart 3.2I.

CHART 3.2I
SCHEMATIC OF THE AUSTRALIAN AND VICTORIAN HEALTH SYSTEMS



Abbreviations:

HACC: Home and Community Care.
AHCA: Australian Health Care Agreement.
CSDA: Commonwealth State Disability Services Agreement.
PCP: Primary Care Partnerships.

3.2.96 The Victorian health system has the following unique attributes:

- Local government has historically assumed a significant role in the delivery of a range of health and related services in Victoria. Recent research shows that around 40 per cent of total Home and Community Care Program moneys in Victoria are expended through local government. The role of local government in other jurisdictions is not as great[3];
- Victoria has been a leader State in the introduction of case-based or output-based funding mechanisms in the acute inpatient area. Victoria has also extended this concept to other program areas (e.g. ambulatory care, rehabilitation in public hospitals) where it, again, has been a leader;

3 Dr Anna Howe, *HACC Status Report for Victorian Local Government*, Municipal Association of Victoria, 2000.

- It is widely accepted that Victoria is a leader in service innovation and, in particular, innovations around the interface between acute and sub-acute care. For example, the Hospital in the Home program introduced in the mid-1990s, and subsequently extended, is regarded as a pioneering service development in Australia (particularly of the scale of implementation in Victoria);
- Victoria has assumed a significant leadership role in the development of strategies to address the problem of illicit drug use. For example, the Turning the Tide drug strategy was a major inter-sectoral initiative where the Department of Human Services played a significant role. Much of the emphasis and content of recent national drug strategies has been strongly influenced by the Victorian experience;
- The organisational structures and arrangements for public health services are unique to Victoria. The metropolitan hospital and regional structures developed in Victoria have no direct parallels elsewhere in Australia;
- Some hospital services are more specialised in Victoria (e.g. the Royal Victorian Eye and Ear Hospital, Peter MacCallum Cancer Institute);
- There is a relatively higher rate of employment of medical practitioners in community health centres; and
- Victoria has a relatively long history of exposure to service provider contracting arrangements, accompanied by a significant emphasis on performance measurement.

3.2.97 Over time health care service delivery has been evolving in 2 main ways:

- enhanced clinical treatment in the acute care phase, accompanied by reductions in average length of stay; and
- enhanced access to rehabilitation and post-acute care options.

3.2.98 Table 3.2J sets out an example which illustrates these changes in service response, outcome and resource implications for a common cause of hospitalisation (fractured neck of femur in an 85 year old woman living at home).

TABLE 3.2J
CHANGES IN SERVICE RESPONSE *(a)*

Era	*Treatment response*	*Inpatient activity*	*Rehabilitation*	*Common service options*	*Likely outcome(s)*
1950s	Hospitalisation: "conservative management" and immobilisation.	Average length of stay often greater than 30 days.	Limited access.	Hospital. Nursing home. Family carer.	Institutionalisation. Occasional discharge home. Eventual death due to complication (e.g. deep vein thrombosis).
1980s	Hospitalisation: corrective surgery (prosthesis).	Average length of stay much reduced from "conservative management" era.	Inpatient rehabilitation.	Nursing home or hostel. Conversion to nursing home type patient in hospital. Family carer. Access to some post-acute services (Home and Community Care Program).	Discharge to home likely with some post-acute or support services. Chance of institutionalisation if length of stay is long or support services lacking.
Present day	Hospitalisation: surgery (prosthesis).	Further reductions in average length of stay due to access to post-acute care options and improved clinical management.	Inpatient and outpatient rehabilitation.	Post-acute and/or ongoing community care, e.g. Hospital in the Home, Post-Acute Care or Home and Community Care Programs. Access to improved discharge programs such as Effective Discharge Program. Residential care alternatives such as Community Options Packages, Community Aged Care Package, and Extended Aged Care in the Home. Family carer.	Discharge to home with community-based support service, full recovery. Institutionalisation less common.

(a) The above information serves as an example only, actual length of stay, treatment response and outcomes are subject to significant variability.

3.2.99 As in most health systems in developed economies, Victoria is facing increasing pressures for change in its health system, driven by:

- rising costs of health care;
- growing demand for services, reflecting population ageing, increased clinical and community expectations regarding access to high quality health care and medical technology, and the impact of increasing chronic illness resulting from higher survival rates and new lifestyle diseases (e.g. diabetes);

- inequalities between groups and regions in access to health care and health outcomes; and
- complexity in the service delivery system that results in duplication and additional costs[4].

3.2.100 Response to these pressures will require a rebalancing of the health system, setting priorities for resource allocation at a number of levels[5], including:

- public expenditure - between different areas of government expenditure (e.g. health versus education versus other areas of expenditure);
- geographical - between regions and localities, particularly rural areas;
- service - between areas of health care (e.g. prevention versus acute health versus mental health versus rehabilitation versus primary care etc.);
- treatment - between types of treatment for the same condition or for different conditions (e.g. acute versus community-based treatment options); and
- individual - between individuals with similar needs.

3.2.101 In general, clinical judgement determines priority setting for treatments and for individuals, although this is increasingly subject to scrutiny and external direction through quality measurement and enhancement processes and enforcement of budgetary controls. Government determines the priorities in expenditure for the first 3 levels, with priority setting usually undertaken as part of the budget process.

3.2.102 The rebalancing of the health system is likely to continue to require attention to cost control and efficient service provision in all areas of the health system, but also to focus on:

- additional effort in prevention of disease and injury;
- developing partnerships between the community and private sector to minimise the call on the public purse;
- ensuring that more expensive acute services are used only for acute patients;
- removal of organisational and financial barriers against smooth transfer of patients between care settings, including the home;
- investment in post-acute and sub-acute care services to facilitate these transfers, including averting admissions to acute care;
- improvements in discharge planning and effectiveness; and
- identification, and implementation of best practice approaches to service delivery.[6]

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4 Secretary, Victorian Department of Human Services, "Drivers for change in health provision", speech to IPAA Conference on Social Policy under the Microscope, April 2001.

5 Drawn from Joan Busfield, *Health and Health Care in Modern Britain*, Oxford University Press, 2000.

6 For a discussion of rebalancing the system, see Associate Professor Judith Dwyer and Dr Terri Jackson, Literature Review: *Integrated Bed and Patient Management* commissioned for Patient Management Task Force, Department of Human Services, February 2001.

What is post-acute care?

3.2.103 Over the past decade, there have been significant changes in acute health care. For example, patient length of stay in acute hospitals has continued to decline because of improvements in medical technology enabling more hospital treatments to be provided on a sameday basis, expanded treatment options providing acute medical care in the home environment, and increased efficiencies in the hospital system with a focus on increased bed utilisation.

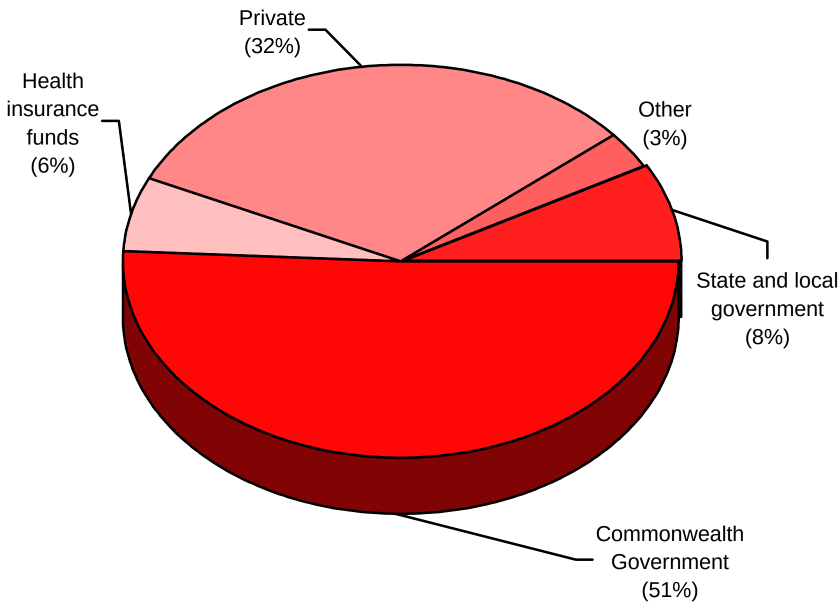
3.2.104 As a result of leaving hospital earlier, patients are increasingly receiving care in the community, subsequent to discharge or "post-acute". However, in some cases, advances in medical technology and treatments mean that, compared with the past, the inpatient experience is less intrusive and care requirements are less after discharge from hospital. Where services are required during the post-acute phase, they may include personal care, allied health services including physiotherapy and occupational therapy, home help from community support agencies or home nursing for treatments such as wound management. These services can be accessed from a range of service providers, including hospitals (ambulatory care services), primary care sector (general practitioners, allied health providers, community health services etc.) and home and community care providers including local government.

3.2.105 Post-acute care is not easily defined. Under the Department of Human Services' Post-Acute Care Program, post-acute care is defined as *"a time limited short term intervention designed to assist patients to recuperate following an acute hospital admission and to facilitate their independence or transition to continuing care where required"*. As patients move from an acute care episode to post-acute care and beyond, there will be variations both in time elapsed and in the type of care required, depending on the specific health condition and other individual circumstances. There is no clear milestone at which a person ceases to require care following an acute admission, that is, post-acute care, and takes over individual responsibility for his or her own health care within the primary care sector. Consequently, we are unable to estimate the level of service provision and expenditure specifically on post-acute care.

3.2.106 The primary care sector is the sector with which most people make initial contact when they are sick, injured, or having difficulty coping with their life circumstances. Services provided by the sector include medical treatment and advice from general practitioners, community nursing and allied health services, rehabilitation and support for people with long-term illness, disability or continuing care needs, and community support for frail elderly people to enable them to live at home.

3.2.107 All 3 levels of government, as well as private insurers and individuals, contribute to the funding of primary care services, some of which would provide post-acute care. The Australian Institute of Health and Welfare's *Health Services Bulletin No. 16* shows that for 1997-98, the most recent year for which data on a State-by-State basis is available, expenditure relating to primary care-type services in Victoria totalled $5.6 billion. The major contributors were the Commonwealth Government ($2.8 billion) and private individuals ($1.8 billion). Other contributors were the State and local governments ($0.46 billion), health insurance funds ($0.35 billion) and others ($0.14 billion). "Other" includes providers of workers' compensation and transport accident insurance. Chart 3.2K presents the contributions on a percentage basis.

CHART 3.2K
SOURCES OF FUNDS
VICTORIAN PRIMARY CARE SECTOR
1997-98



Source: Australian Institute of Health and Welfare.

3.2.108 These figures cover a much wider range of services than just post-acute care. On the other hand, they exclude expenditure by the State and local governments under the Home and Community Care Program. This Program provides a range of personal, health and domestic services to help frail aged and younger people with disabilities, and their carers, to enhance their independence and to avoid premature or inappropriate admissions to long-term residential care. The figures also exclude that portion of the Commonwealth funding under the Home and Community Care Program for non-health type services.

3.2.109 The available data does not enable an estimate of the proportion of these expenditures which are for post-acute care to be determined.

3.2.110 A third category of care, sub-acute care, is provided within the Victorian health system. The Acute Health Division's *Victoria – Public Hospitals Policy and Funding Guidelines 2000-2001* indicate that *"the sub-acute service system has both an inpatient and community focus on rehabilitation, restorative care and community support"*. Because it occurs after the discharge of patients from the acute setting, sub-acute care is also regarded as "post-acute" for the purposes of this audit.

3.2.111 Sub-acute inpatient services are provided in extended care centres or in dedicated sub-acute units within acute hospitals. There are also a range of specialist ambulatory care services such as community rehabilitation clinics and specialist clinics for continence, falls and mobility and pain management, as well as home-based care. The Division's Policy and Funding Guidelines indicate that *"the expansion of the sub-acute service system* [an increase in the number of beds, which made service available in some rural areas where no service was previously available, an increase in the per diem rate paid for services and increases in funding for community rehabilitation centres] *has enabled older people to be admitted directly to sub-acute care, or to be transferred to sub-acute care from either emergency departments or inpatient acute settings"*.

3.2.112 In 2000-01, the total budget for sub-acute admitted services within Victoria is $200 million comprising 318 310 rehabilitation bed days, 249 035 geriatric evaluation and management bed days, and 9 016 geriatric respite/nursing home-type bed days. A further $26.2 million has been provided for 122 229 places in Community Rehabilitation Centres. This sub-acute funding compares with some $1.97 billion budgeted for public acute inpatient services.

Difficulties in examining the trends in health service delivery

3.2.113 In examining the impact of changes in health service delivery on post-acute care over the last decade, we have been hampered by a lack of reliable, consistent data, especially relating to the post-acute, non-acute and other non-hospital dimensions of the Victorian health system. In particular, the difficulty results from:

- the lack of a clear definition of post-acute care;
- changes to data and service definitions over time;
- limited comparability between data collections, partly due to unclear definition of service units, or inconsistent bases of data collection across jurisdictions; and
- the lack of a unique patient identifier to enable tracking of experiences of individuals through the health system.

3.2.114 The limitations have made it difficult to describe or model trends in health service delivery over the past decade. In general, data for the earlier period of the decade are either absent or sufficiently different in composition that make comparisons difficult.

HEALTH EXPENDITURE TRENDS

3.2.115 The Commonwealth Government, under the Australian Health Care Agreement, contributes to the cost of State-funded health services and funds areas of Commonwealth responsibility within each State. The Commonwealth's key areas of responsibility include:

- payment for medical services such as services provided by general practitioners, through the Medical Benefits Scheme;
- payments to the States and Territories for public hospital services;
- payment of subsidies for pharmaceuticals under the Pharmaceuticals Benefits Scheme; and
- provision of subsidies for aged care.

3.2.116 The Victorian Government also provides significant funding for health. As indicated in Table 3.2L, for the 2000-01 year, the health-related budget outlays of the Department of Human Services, including Commonwealth contributions administered through the Department, totalled $5.4 billion.

TABLE 3.2L
VICTORIAN HEALTH-RELATED BUDGET OUTLAYS, 2000-01

Output group	*$million*
Acute services	3 621.9
Ambulance services	220.6
Aged care and primary health services	855.6
Mental health services	493.5
Public health services	214.1
Total	5 405.7

Source: Department of Treasury and Finance, *Budget Paper No. 3, 2000-01*.

3.2.117 In addition to funding from the Commonwealth and State Governments, local government, and the non-government sector also contribute to the cost of Victorian health care. Table 3.2M shows the level of government and non-government expenditure in the Victorian health system for 1997-98, the most up-to-date data available.

TABLE 3.2M
VICTORIAN HEALTH SERVICES RECURRENT EXPENDITURE BY FUNDING SOURCE *(a)*, 1997-98

Source	*$million*	*per cent*
Government -		
Commonwealth government	5 030	46
State and local government	2 064	19
Non-government -		
Health insurance funds	1 084	10
Individuals	2 202	20
Other *(b)*	515	5
Total	**10 895**	**100**

(a) Includes expenditure relating to primary care-type services as presented earlier in this Report, as well as expenditure relating to public and private hospitals, nursing homes, ambulance services, community and public dental services and administration and research.

(b) “Other” includes expenditure on health services by providers of workers’ compensation and compulsory motor vehicle third party insurance cover.

Source: Australian Institute of Health and Welfare, *Health Expenditure Bulletin No. 16*.

3.2.118 Across Australia, there has been significant change in the service composition of total health expenditure since the introduction of Medicare in 1984-85 as outlined in Table 3.2N.

TABLE 3.2N
PROPORTION OF RECURRENT EXPENDITURE ON AUSTRALIAN HEALTH SERVICES, 1984-85 AND 1997-98
(per cent)

Area of expenditure	*1984-85*	*1997-98*	*Change in share*
Public hospitals	32.7	29.2	–3.5
Repatriation hospitals *(a)*	1.6	-	–1.6
Private hospitals	5.6	8.3	+2.7
Public psychiatric hospitals	4.0	0.9	–3.1
Total hospitals	43.9	38.4	–5.5
Nursing homes	9.2	7.5	–1.7
Ambulance	1.7	1.5	–0.2
Other institutional *(a)*	0.2	-	–0.2
Total institutional	**55.0**	**47.4**	**–7.6**
Medical services	17.6	19.3	+1.7
Other professional services	3.2	3.8	+0.6
Total pharmaceuticals	8.7	12.1	+3.4
Aids and appliances	2.0	1.9	–0.1
Community and public health	3.9	4.8	+0.9
Dental services	4.7	5.9	+1.2
Administration	3.5	3.3	–0.2
Research	1.4	1.5	+0.1
Total non-institutional	**45.0**	**52.6**	**+7.6**

(a) Subsumed into other service types.
Source: Australian Institute of Health and Welfare, *Australia's Health 2000*.

3.2.119 In the period between 1984-85 and 1997-98, the proportion of recurrent expenditure in all types of services in the institutional sector fell, except for the proportion of expenditure on private hospitals which increased by 2.7 per cent. There were increases in the proportion of expenditure for most services in the non-institutional sector, with the greatest increases in the areas such as medical services and pharmaceuticals. While there has been some increase in expenditure on community and public health, the overall proportion of funding remains relatively small.

DEMAND FOR POST-ACUTE CARE SERVICES

3.2.120 Notwithstanding the difficulties outlined above, there is evidence suggesting that there is increasing demand for post-acute care services including:

- an increase in sameday inpatient services and a decrease in the average length of stay for patients in acute hospitals and in rehabilitation services;
- reductions in acute bed availability and residential aged care placements;

- weaknesses in discharge effectiveness, as evidenced by unplanned readmissions to acute hospitals and poor compliance with effective discharge standards as identified in Effective Discharge Strategy Patient Record Audits, especially in hospital relationships with community services;
- patient perceptions of a need to improve discharge from public hospitals;
- the swift take-up of projects funded under the Post-Acute Care Program; and
- increases in inpatient-type services provided by hospitals on an ambulatory basis, but decreases in community care-type services.

3.2.121 Each of these trends is discussed in the following sections.

Decreased length of stay in hospital and rehabilitation services

Acute inpatient services

3.2.122 There is a growing demand within Victoria for acute inpatient services. Between 1990-91 and 2000-01, the total number of patients treated in Victorian acute public hospitals increased by 62 per cent. The number of sameday patients increased over the period by 178 per cent. Table 3.2O shows the trend in throughput for non-sameday and sameday patients treated in public acute hospitals over the period.

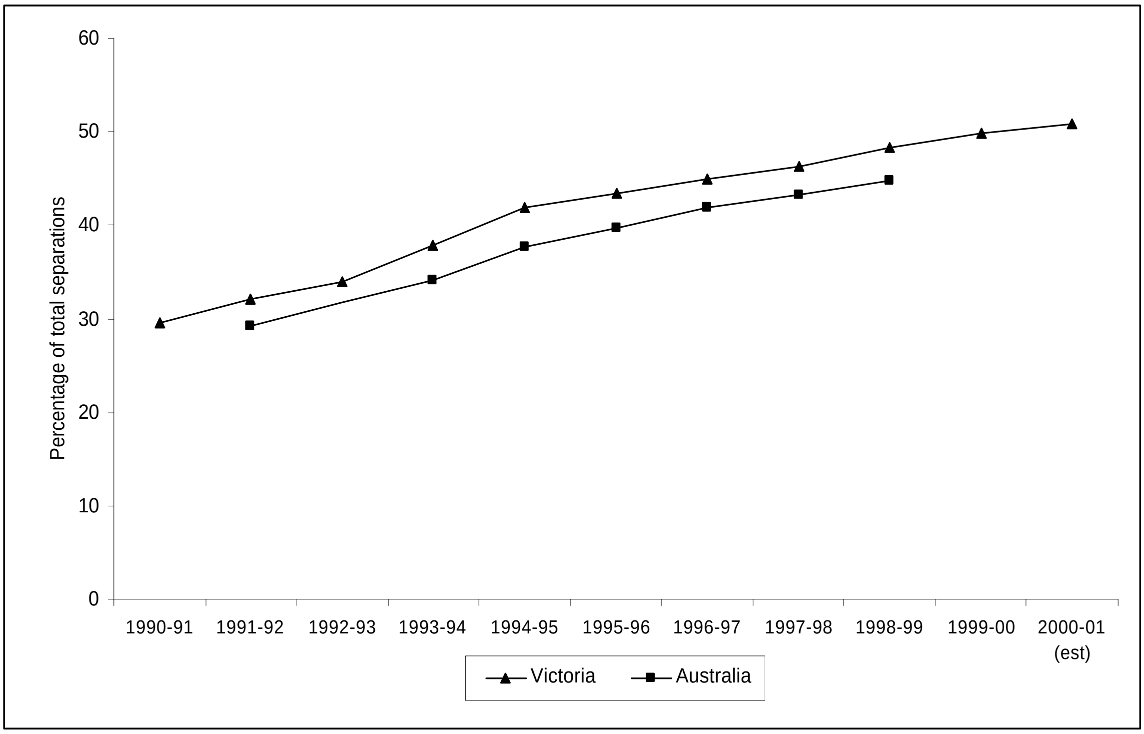
TABLE 3.2O
VICTORIAN PUBLIC HOSPITAL SEPARATIONS, *(a)*
1990-91 TO 2000-01

	1990-91	*1993-94*	*1995-96*	*1997-98*	*1999-00*	*(b) 2000-01*	*Change (%)*
Sameday separations *(c)*	187 405	288 268	376 208	430 066	500 495	521 812	178.4
Non-sameday separations	444 937	474 747	490 663	497 284	502 596	505 334	13.6
Total	**632 342**	**763 015**	**866 871**	**927 350**	**1 003 091**	**1 027 146**	**62.4**

(a) Patients are counted as they are discharged (separated) from hospital. Excludes unqualified newborn.
(b) Estimated by the Department of Human Services.
(c) Sameday patients are admitted and discharged on the same day.
Source: Department of Human Services.

3.2.123 Sameday separations as a proportion of total separations for Victoria and Australia are shown in Chart 3.2P. In Victoria more than half of all separations are now sameday. The resulting reduction in length of stay has enabled the increased number of separations over the decade to occur, in a period of declining numbers of acute beds.

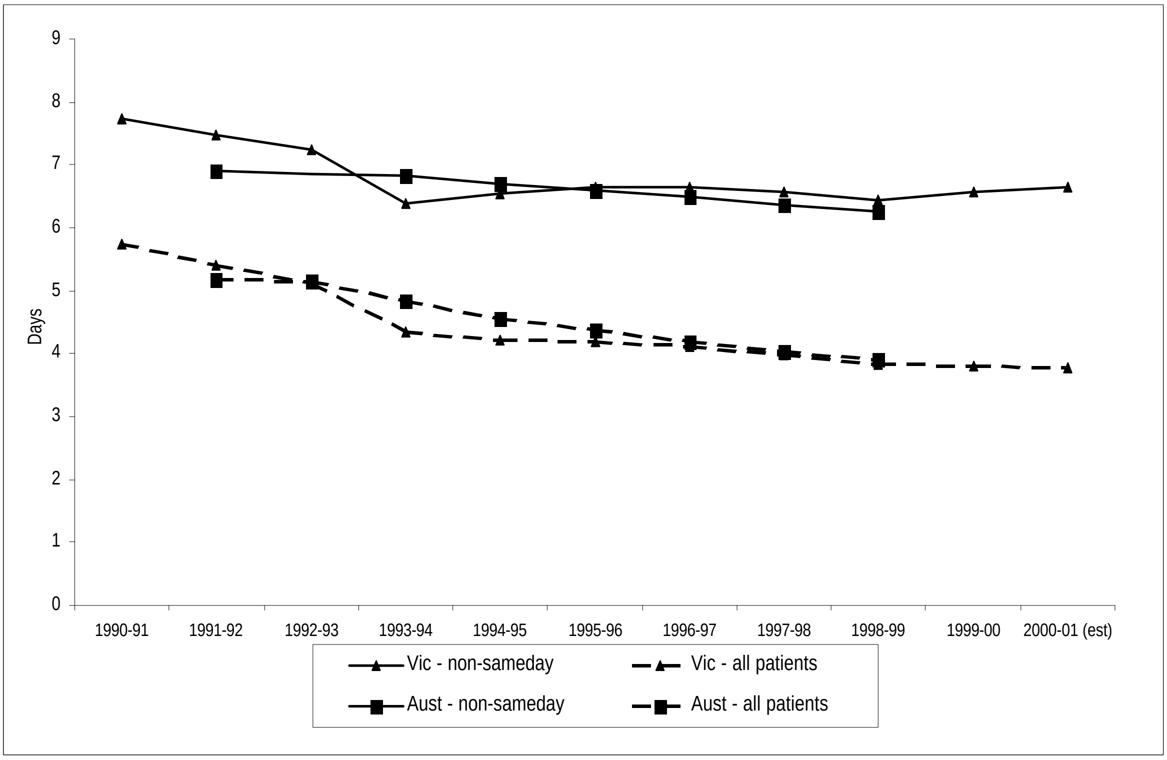
CHART 3.2P
SAMEDAY SEPARATIONS AS A PROPORTION OF TOTAL SEPARATIONS, VICTORIAN AND AUSTRALIAN PUBLIC HOSPITALS *(a)*, **1990-91 TO 2000-01**



(a) Australian data for the periods 1990-91, 1992-93 and 1999-2001 is not available.
Source: Department of Human Services and Australian Institute of Health and Welfare.

3.2.124 Chart 3.2Q depicts the reduction in length of stay for public hospitals in Victoria and for Australia from 1990-91 to 2000-01.

CHART 3.2Q
AVERAGE LENGTH OF STAY,
VICTORIAN AND AUSTRALIAN PUBLIC HOSPITALS *(a)*,
1990-91 TO 2000-01



(a) Data for non-sameday patients for Australia for 1992-93 is not available.
Source: Department of Human Services and Australian Institute of Health and Welfare.

3.2.125 The average length of stay of non-sameday separations declined over the 1990s, with the average length of stay reducing from 7.7 days in 1990-91 to 6.4 days in 1993-94 in Victoria, and remaining at about that level since. The average length of public hospital stay for all patients decreased from 5.7 to 3.8 days over the period 1990-91 to 2000-01. While there has been a reduction in length of stay for very long stay patients over the decade, facilitated by improvements in medical technology, the overall reduction in length of stay since 1993-94 has been mostly due to the increase in proportion of sameday activity.

3.2.126 Charts 3.2P and 3.2Q show that the trends in Victoria are consistent with national trends.

Rehabilitation services

3.2.127 In Victoria, rehabilitation services are provided both as sub-acute services and through the casemix acute hospital system. Victoria's sub-acute service system has both an inpatient and community focus on rehabilitation, restorative care and community support. There is a strong correlation between age and demand for medical and hospital services. In mid-2000, 55 per cent of public hospital bed days were utilised by older people. The expansion of the sub-acute service system has enabled older people to be admitted directly to sub-acute care, or to be transferred to sub-acute care from either emergency departments or inpatient acute settings. This frees up acute hospital beds and assists in deferring entry to residential care for older people with chronic illness or severe disability.

3.2.128 The average length of public hospital stay for rehabilitation patients reduced from 26.3 days in 1996-97 to 17.0 days in 1998-99 in Victoria. Care should be taken in interpreting this trend as a number of new initiatives were implemented that provided for these patients to be transferred to community-based services. Data at the national level over the same period shows a decline from 17.7 days to 14.6 days.

3.2.129 These declines in length of stay indicate that there may be more people requiring and seeking services in the community, who may have in the past spent longer in hospital or rehabilitation.

Reduced bed availability

3.2.130 Increases in patient throughput have occurred at the same time as a reduction of the number of public acute hospital beds per capita. Nationally, between 1985-86 and 1997-98 the number of public acute hospital beds declined by almost 40 per cent. Table 3.2R shows that, in Victoria, the number of available beds in public hospitals fell by 4.1 per cent from 1992-93 to 1998-99, despite an increase in separations and bed days over the period. The number of acute health beds declined by 10 per cent from 1993-94 to 1998-99. Overall bed numbers rose again in 1999-2000 to be slightly above the 1992-93 level.

TABLE 3.2R
AVERAGE AVAILABLE BEDS IN VICTORIAN PUBLIC HOSPITALS, 1992-93 TO 1999-2000

Year	*Acute Health*	*Aged Care*	*Mental Health (a)*	*Other (b)*	*Total beds*
1992-93	n.a.	n.a.	n.a.	n.a.	12 056
1993-94	10 373	1 284	354	129	12 140
1994-95	10 615	1 165	420	114	12 314
1995-96	10 145	1 169	871	103	12 288
1996-97	9 815	1 273	884	104	12 076
1997-98	9 753	1 254	861	93	11 961
1998-99	9 336	1 278	855	96	11 565
1999-2000	9 703	1 411	863	96	12 073

(a) The number of available mental health beds more than doubled, due to the redesignation in 1995-96 of around 450 beds from acute health to mental health.

(b) "Other" includes public health, youth and family services, primary care and co-ordinated care.

Source: Department of Human Services.

3.2.131 The results of a bi-monthly census of patients waiting in acute and sub-acute settings for residential care placements, reported by the Department in the *Hospital Services Report, December Quarter 2000*, showed that elderly patients were waiting in hospital beds for an increasing number of days prior to placement in residential aged care facilities. The number of acute bed days occupied by these patients increased by 88 per cent, from 4 492 in September 2000 to 8 445 in January 2001. Over the same period, the number of bed days occupied by patients waiting in sub-acute facilities for residential placement increased by 18 per cent, from 6 295 to 7 403.

3.2.132 An earlier census of patients in public hospitals in September 2000 revealed that, on any one day, approximately 350 beds are taken up by people waiting for nursing home and hostel placement. This means that the equivalent of a major suburban hospital is being diverted from people needing acute hospital care to accommodate people who could be placed in residential care. At the same time, the Department noted an increasing number of older people presenting to public hospitals, with more complex needs. Over the 9 months to September 2000, there was a 34 per cent increase in referrals to emergency departments from nursing homes.

3.2.133 The Commonwealth Government has responsibility for most regulation of residential care facilities, provides the majority of annual funding for them and controls the number of subsidised bed places. The remainder of the funding is mostly provided by the residents. Where facilities are operated by the State, a reduced proportion of funding is received from the Commonwealth and the State contributes to the recurrent costs.

3.2.134 The *Report on Government Services 2000*, showed that at June 1999 Victoria had fewer residential care places per thousand persons over 70 years of age than any other Australian State or Territory. The number of operational nursing home, hostel and community care packages in Victoria was 89.4 places per thousand persons over 70 years of age, compared with 94.4 places per thousand across Australia. The lack of high-care residential aged care places puts additional pressures on the hospital system.

Weaknesses in discharge effectiveness

Effective Discharge Strategy

3.2.135 The Effective Discharge Strategy is intended to assist hospitals and sub-acute services to improve discharge processes and practices. It is a 5-year strategy that applies to acute hospitals, aged care services, extended care services and multi-purpose services. The Strategy is based on the premise that good discharge planning processes ensure that patients can be discharged in a timely manner with appropriate care and support. In this way, hospitals can optimise the use of beds and hospital services.

3.2.136 Audits of patient records were conducted for the Department by an external consultant in June 1999 and June 2000 to assess recorded evidence of discharge activities. The 2000 audit found that 23 per cent of hospitals had high compliance with the discharge standard developed for the audit. A further 32 per cent were assessed as achieving medium compliance and the remaining 45 per cent were assessed as having low compliance.

3.2.137 The patient records audits found that there was:

- inferior compliance in acute hospitals, with rehabilitation and small rural hospitals having generally higher compliance;
- superior compliance in aged care and, to a lesser extent, extended care and multi-purpose services; and
- significantly higher compliance for intensive post-discharge needs patients.

3.2.138 The aspects of discharge where hospitals had low compliance were:

- Involvement of community service providers in decision-making around discharge. Overall, the compliance score was around one-third of the possible maximum and was particularly low for metropolitan hospitals. The better performers were rehabilitation, aged care and multi-purpose services, and small rural hospitals; and
- Involvement of patients and carers in decision-making around discharge. Overall, the compliance score was just over one-third of the possible maximum.

3.2.139 The major obstacles to the discharge of patients as planned were reported by hospitals as being:

- lack of community health and welfare services to support discharge, especially in rural areas where the isolation of patients reduces the potential for early discharge (39 per cent of hospitals);
- lack of appropriate accommodation, particularly for elderly patients and in rural areas (29 per cent of hospitals);
- poor communication and co-ordination between medical staff, general practitioners, and those parts of the hospital involved in discharge planning (24 per cent of hospitals); and
- attitudes and expectations of patients and their carers/families, including reluctance to go home and differing expectations of the health services between patients/carers and the hospitals (22 per cent of hospitals).

Unplanned readmission rates

3.2.140 Unplanned readmission to hospital may indicate a lack of timely and effective post-acute or community care following hospital discharge, and an increase in the rate could suggest an increase in the level of unmet need for such care. However, there has been some debate about the validity of unplanned readmissions as an indicator of quality of care.[7] A Commonwealth Government funded study of 2 chronic conditions across 10 hospitals indicated that unplanned readmissions had poor validity for cross-hospital comparisons of quality of care.

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7 Commonwealth Department of Health and Family Services, *Pilot Hospital-Wide Clinical Indicators Project, Final Report*, July 1998.

3.2.141 The Department of Human Services regularly published unplanned readmission data until September 1997. Table 3.2S shows that the percentage of unplanned readmissions rose marginally from 9.3 per cent in the September quarter 1993 to 10.5 per cent in the September quarter 1996 before declining to 10.2 per cent one year later.

TABLE 3.2S
UNPLANNED READMISSIONS TO VICTORIAN PUBLIC HOSPITALS

	September quarter 1993	*September quarter 1996*	*September quarter 1997*	*Change 1993 to 1997*
	(no.)	*(no.)*	*(no.)*	*(%)*
Total patients treated *(a)*	181 696	218 134	216 321	19.1
In-scope patients treated *(b)*	170 883	200 921	199 026	16.5
Total readmissions *(c)*	42 325	63 105	65 652	55.1
Unplanned readmissions *(d)*	15 905	21 067	20 321	27.8
Unplanned readmissions *(e)* (per cent)	**9.3**	**10.5**	**10.2**	**+0.9**

(a) Public hospital separations.
(b) Excludes patients with change in care type, transfers from other acute hospitals, patients leaving at own risk.
(c) Patients readmitted. May be for chronic or unrelated condition. Excludes patients readmitted to a different hospital.
(d) Patients with unplanned readmissions within 28 days of discharge.
(e) Equals unplanned readmissions as a percentage of in-scope patients treated.
Source: Department of Human Services, *Hospital Services Report*, November Quarter 1996 and September Quarter 1997.

3.2.142 The Department stopped publishing unplanned readmission rates beyond 1997-98, noting that a more valid indicator of unplanned readmissions for the same or a related condition was being developed. However, this indicator is still not available, some 3 years after the last data was published.

3.2.143 Unfortunately, definitions of unplanned readmission to hospital are applied differently across jurisdictions in Australia, making comparisons among States difficult. Without such benchmarks, or more recent data, it is difficult to determine what the rate of unplanned readmissions is now and whether this indicates increasing unmet need for post-acute care. However, the Department's patient record audit data indicates weaknesses in discharge effectiveness that would affect provision of post-acute care.

Patient perception of discharge

3.2.144 According to the Department's latest patient satisfaction survey conducted in 1997 across all hospitals, 97 per cent of patients were satisfied with their overall hospital experience, with 76 per cent being very satisfied. Of interest for our consideration of post-acute care, the majority of patients (82 per cent) regarded the duration of stay as about right, with 11 per cent perceiving it as too short and 7 per cent as too long.

3.2.145 In terms of their discharge, 92 per cent of respondents said they were given adequate notice of discharge. However, information at discharge was clearly a key area for improvement. For those where the question was applicable, 36 per cent commented that they were not told about possible side effects of medicine, 21 per cent said they were not told of things that could be done to help recovery at home, and 13 per cent believed that they were not given sufficient information on how to cope with their condition at home or asked if they had help at home after discharge. These results (from an earlier period) are consistent with the more recent findings of the Effective Discharge Strategy Patient Record Audits, which indicated that only half of patients and less than one-third of carers were consulted in preparing for discharge.

Swift take-up of post-acute care places

3.2.146 The Post-Acute Care Program can assist hospitals to optimise the use of inpatient beds by providing discharge support services that allow some patients to be discharged earlier. By helping people to recuperate after hospital treatment, post-acute care services can also assist in reducing the risk of unplanned readmissions.

3.2.147 The number of patient referrals to, and the throughput for, the Post-Acute Care Program has increased steadily over the years (347.9 per cent increase in new referrals and a 536.3 per cent increase in the number of episodes completed by post-acute care projects between 1996-97 and 1999-2000), as shown in Table 3.2T.

TABLE 3.2T
POST-ACUTE CARE PROGRAM, NEW REFERRALS AND COMPLETED EPISODES, 1996-97 TO 1999-2000

	1996-97 (a)	*1997-98*	*1999-2000*	*Increase*
	(no.)	*(no.)*	*(no.)*	*(%)*
New referrals	4 858	8 102	21 761	347.9
Episodes completed	2 486	5 093	15 819	536.3
No. of services provided *(b)*	104 879	198 430	437 758	210.7
No. of participating projects	6	13	18	200

(a) Also includes data for May and June 1996.
(b) Care should be taken in interpreting the number of services provided as there is no standard unit of measurement for the various services.
Source: Department of Human Services, Post-Acute Care Program, *Consolidated Activity Reports*, various editions.

3.2.148 Data for the first 6 months of 2000-01 shows a continuing growth in activity. The large rise in Post-Acute Care Program patients and services provided is partly related to an increase in the number of participating projects offered but also due to the apparent swift take-up by patients as soon as places become available. The main constraints on patient numbers are the number of funded places, the ability to staff the services and the speed of development of links with agencies who refer patients to the services.

Decreases in community care-type services provided by hospitals on an ambulatory basis

3.2.149 Non-admitted care is an important component of hospital service provision. Non-admitted patient occasions of service have changed dramatically both in coverage and enumeration methods over the last 10 or so years. Traditionally, non-admitted patient services covered outpatient clinics and non-admitted patients treated in emergency service departments within hospitals. Over the years, this has expanded to include home and community care services, community services, health education and outreach services offered by hospitals.

3.2.150 During the period from 1996-97 to 1998-99, when enumeration of data appears to have been more consistent, the reported number of non-admitted occasions of service provided by public hospitals was almost unchanged and activity in community health services, district nursing services and other outreach services offered by public hospitals within Victoria declined. This may partly be because some services, previously offered on a non-admitted basis, now form part of the inpatient episode of care under substitution programs. Other possible explanations include the capping of Home and Community Care services introduced by the Commonwealth, and the extent to which some of the services previously provided by hospitals have been shifted to the non-hospital setting such as, community health centres or private community nursing providers.

3.2.151 During the period, throughput increased in those services that account for the highest proportion of non-admitted services activity, such as accident and emergency services, pathology services, radiology and organ imaging, other medical/surgical/obstetric services, mental health services and allied health services. Some of this may be due to enumeration changes, but it does indicate that hospitals are providing more inpatient-type services on a non-admitted basis. These may reflect an increase in provision of post-acute clinical care by hospitals.

3.2.152 Unfortunately, due to differences in definitions, and changes in what is included or excluded from particular service types, the above trends are unable to be compared with those for other States or nationally.

Summary

3.2.153 The evidence presented above indicates that there is increasing demand for post-acute care services. The actions of the Department's in response to this increasing demand are set out below.

NEW DEPARTMENTAL PROGRAMS AND INITIATIVES AFFECTING POST-ACUTE CARE

3.2.154 Over the decade, a range of new programs or initiatives relevant to the transition from acute care to sub-acute care, or from acute care to post-acute care or care in the community, were introduced. The most relevant of these are summarised in Table 3.2U.

TABLE 3.2U
STATE PROGRAMS AND INITIATIVES

Program/ initiative	*Purpose*	*Division and year introduced*	*Budgeted activity 2000-01 (a)*	*Budgeted expenditure 2000-01*
				($m)
Geriatric Evaluation and Management (sub-acute services)	To provide clinical evaluation and management for frail aged people admitted as a result of an acute illness or injury.	Acute Health *(b)* 1993	249 035 bed days	85.9
Rehabilitation (sub-acute services)	To provide inpatient services to frail aged people with an acute illness or injury.	Acute Health *(b)* 1993	318 310 bed days	111.6
Hospital in the Home	To give patients the choice to receive hospital care in their own homes.	Acute Health 1994	96 976 bed days *(c)*	*(d)* 5.0
Community rehabilitation centres (sub-acute services)	To provide multi-disciplinary rehabilitation services to clients who are disabled, frail, chronically ill or recovering from traumatic injury.	Acute Health *(b)* 1995	122 229 places	26.2
Continuum of Care Program	To enable a sequence of care in sub-acute services through inpatient, outpatient and community-based services.	Acute Health *(b)* 1996	n.a.	*(e)* n.a.
Healthstreams	To enable small rural health services to provide health care, including sub-acute, acute, post-acute services, to meet identified local community needs.	Policy and Strategic Projects Division *(f)* 1996	n.a.	*(c)* 1.9
Post-Acute Care Program	To assist recuperation of patients following an acute hospital admission, or to prepare them for long-term support.	Acute Health *(g)* 1996-97	20 000 clients	14.4
Specialist clinics (sub-acute services)	To provide continence, pain, falls and mobility management and sub-acute specialist services.	Acute Health *(b)* 1997-98	n.a.	4.35
Quality Improvement Funding Rounds (annually)	To improve safety and quality in hospitals through the application of research findings including those relating to continuity of care.	Acute Health 1997-98	n.a.	*(h)* 3.0
Primary Health and Community Support Services Strategy	To create an integrated, consumer responsive service system in the community sector.	Aged, Community and Mental Health 1998	*(i)* n.a.	n.a.

TABLE 3.2U
STATE PROGRAMS AND INITIATIVES - *continued*

Program/ initiative	*Purpose*	*Division and year introduced*	*Budgeted activity 2000-01 (a)*	*Budgeted expenditure 2000-01*
				($m)
Unassigned Geriatric Evaluation and Management (sub-acute services)	To provide additional services to older patients who would otherwise require admission to acute or sub-acute inpatient care.	Acute Health *(b)* 1998-99	4 164 bed days	1.4
Effective Discharge Strategy	To improve the effectiveness of hospital discharge practices and to improve integration between general practitioners and hospitals.	Acute Health *(g)* 1998-99	n.a.	8.5
Maternity Enhancement Program	To increase ante and postnatal care provision; improve special needs services; promote care during pregnancy and childbirth, and improve information provision.	Acute Health 1998-99	80 per cent of women to receive post-natal domiciliary visits	16.4
Winter Emergency Demand Strategy/ Emergency Demand Management Strategy	To provide an integrated package across the acute, sub-acute and post-acute sectors in response to increased demands on hospitals, and to improve access to emergency services, in partnership with aged and sub-acute services.	Acute Health 1999-2000	n.a.	34.0
Primary Care Partnership Strategy *(j)*	To assist primary health providers and professionals to co-ordinate their work for clients they have, or may have, in common.	Aged, Community and Mental Health 2000	32 partnerships	*(k)* 8.8
Hospital to Home	To bring together initiatives, aimed at encouraging an integrated approach to discharge planning and post-discharge care.	Acute Health 2000-01	n.a.	*(l)* n.a.

(a) Some programs or initiatives are funded on a project basis and, therefore, have no budgeted activity levels.
(b) Initially the responsibility of the Aged, Community and Mental Health Division but transferred to the Acute Heath Division during 2000.
(c) Target not specified for 2000-01. Figure is actual activity for 1999-2000.
(d) $4 million for base grants and bonuses and $1 million for quality improvement grants. This is in addition to funding provided within the casemix system from which most Hospital in the Home conditions can be funded.
(e) This initiative has now been "mainstreamed", i.e. rolled into the main funding stream for hospitals and as a result, the level of funding is unable to be identified separately.
(f) Managed by the Policy and Strategic Projects Division, funded by the Acute Health and Aged, Community and Mental Health Divisions.
(g) Administered by the Acute Health Division but jointly funded by the Acute Health and Aged, Community and Mental Health Divisions.
(h) The Department advised this figure is approximate only.
(i) The Strategy comprises a number of projects within the Acute Health and Aged, Community and Mental Health Divisions and is co-ordinated by the Emergency Demand Co-ordination Group within the Acute Health Division.
(j) The Primary Care Partnerships replaced the Primary Health and Community Support Services initiative in 2000.
(k) Includes an allocation of $257 000 per Partnership plus variable weighted population-based payment.
(l) A policy umbrella rather than a funded service initiative.

3.2.155 In addition to the programs and initiatives outlined in the Table 3.2U, the Department has continued to fund its share of the Commonwealth Government's Home and Community Care Program. The Department advised that the State's budgeted contribution for that program for 2000-01 was $116.2 million, to provide 2 million units of community care and support; 1.2 million units of nursing and allied services; and 3 023 case management packages. The contribution includes an amount of $18.9 million above the required contribution under the agreement with the Commonwealth Government.

ASSESSING THE DEPARTMENT'S MANAGEMENT OF THE CHANGES IN POST-ACUTE CARE

3.2.156 When considering the management of complex health systems that are both publicly and privately funded across several jurisdictions, it is difficult to ascertain success or to attribute the source of failure. The demand for most publicly provided health services is growing rapidly, while the resources are not, and the control over available resources in the system is split across jurisdictions and organisations and individuals. The existence of unmet demand for post-acute services for some individuals in some places does not therefore necessarily imply failure on the part of the Victorian Government or its Department of Human Services.

3.2.157 We recognise that this Report provides a partial analysis, due to some extent to the lack of information on which to make judgements regarding outcomes and partly due to constraints on our ability to audit the actions of organisations that fall outside our legislative mandate. In assessing whether the Department's management of the changes in post-acute care provision over this period has been effective, we therefore rely on an assessment of the appropriateness of the actions it has taken rather than the outcomes for individuals, which will be affected by a range of personal and other factors, including the activities of the Commonwealth Government and private organisations.

3.2.158 If the Department's management of changing health service delivery in the area of post-acute care has been effective, we would expect to see:

- a strategic planning framework that ensures that the most important issues are addressed and that appropriate data is used to inform decisions;
- provision of an appropriate policy and funding framework;
- encouragement of innovation and improved service delivery, through mechanisms such as:
    - providing rewards and incentives, financial or otherwise, for innovation and good practice;
    - encouraging pilot projects to test new initiatives; and
    - encouraging sharing of ideas between service providers and across jurisdictions; and
- program monitoring and evaluation which informs future strategic planning.

3.2.159 An assessment against each of these criteria is set out below.

Strategic planning framework

3.2.160 The need for improved planning for health services has been raised by at least 2 previous reviews. In June 1995, the Phase 1 Report of the Metropolitan Hospitals Planning Board recommended the establishment of a planning authority to advise the (then) Minister for Health. The Final Report of the Ministerial Review of Health Care Networks, issued in May 2000, recommended establishment of a Health Services Planning Council to develop a strategic vision for health service planning in the future.

3.2.161 Discussions with the Department revealed that during the early to mid period of the last decade there was a priority on implementing efficiency gains, particularly within the acute health sector; and establishing new funding models, including the casemix funding model and purchaser/provider arrangements. More recently, strategic planning has become a greater priority to address the broad changes in the health sector. In December 1999, the Department established the Policy Development and Planning Division to strengthen its planning activities. It was considered that the establishment of the Division addressed the concerns raised by the Ministerial Review.

3.2.162 According to the *Department of Human Services 1999-2000 Annual Report*, the role of the Division included strategic policy development and whole-of-department planning and budget development. We were advised that the Division does not take over the policy development and planning functions of other divisions, but rather provides quality assurance for policy development and planning by other divisions. The Division played a major role in co-ordinating the Department's recent budget process.

3.2.163 In March 2001, the Division was restructured and became the Policy and Strategic Projects Division, with the aim of providing a cross-program focus for research, policy analysis and strategic planning.

3.2.164 Evidence of the Department's increased focus on strategic planning are:

- The recent emphasis being given to emergency demand management, concentrating on the service system as a whole and on the pathways of care for users of health services and consideration of areas of interface between acute, sub-acute and post-acute care. The Department has established the Emergency Demand Management Strategy comprising a range of projects including the Sub-Acute Interface, Aged-Acute Interface and Substitution, Diversionary and Care Co-ordination Services projects to examine the movement of patients between service sectors and to assess how services can assist optimal use of hospital services;
- Research commissioned to describe and analyse specific aspects of service delivery to identify aspects that could lead to improved performance and resource allocation. Examples of these include the Medical Inpatients Study and the Short Stay/Observation Unit Project;
- Establishment of the Patient Management Task Force to identify specific areas for improvement in hospital patient management processes. The Task Force will also advise on the system drivers that may lead to best practice in patient management; and

- Development of the Primary Care Partnerships Strategy aimed at delivering integrated service planning and service co-ordination. The Strategy is intended to complement the Emergency Demand Management Strategy, through integration of acute and community-based services to prevent admissions to hospital and provide better service coordination, within the community particularly for management of chronic illness. Underlying this Strategy is a focus on the burden of disease and an evidence-based approach to population health, health promotion and integrated disease management.

Whole-of-system strategic planning

3.2.165 A strategic planning focus across the whole health system is a challenge for the Department that, while desirable, may be difficult to achieve, particularly given the number of players in the system able to impact on service delivery. For example, actions of the Commonwealth Government and private operators can have significant impacts on the service offerings available in the system and on the actions required by the Department to meet emerging needs. Also, due to its ongoing obligations under the Australian Health Care Agreement to fund public hospitals, only a relatively small portion of the State's annual health budget is available to address emerging pressure points in the system.

3.2.166 These restrictions make it even more important that the Department invest significant effort into strategic planning. The ability to ensure scarce resources are allocated to the areas of greatest priority is particularly important, placing an increased importance on a robust and rigorous departmental budget process informed by good strategic planning.

Data

3.2.167 The availability of relevant, complete and accurate data on a timely basis is crucial for strategic planning and resource allocation. We found that the Department has access to, and collects considerable quantities of data from providers of health services, usually under the terms of their funding and service agreements. Under their health service agreements, hospitals provide data regularly to the Department's Victorian Admitted Episode Dataset, Victorian Emergency Minimum Dataset and Agency Information Management System. Data collection is also an important part of the State's contribution to various Commonwealth data sets, including the Home and Community Care Minimum Dataset.

3.2.168 Despite the volume of data gathered, it is acknowledged within the Department and the health industry that there are limitations to the data. For example, there are substantial gaps relating to services provided by the community sector and unmet need for home and community care and post-acute services. To some extent data gaps may be overcome by drawing inferences from other data collected, for example estimating unmet demand using data on hospital discharge and readmission rates. However, in other cases such as for the Post-Acute Care Program, the absence of standard units of service and standard unit costs mean that the data collected from funded services has limited use for planning, benchmarking or service monitoring purposes.

3.2.169 Other constraints, including the absence of unique patient identifiers along with privacy considerations that restrict access to records, impact on the ability to track patient experiences through the system and therefore can severely hamper planning and an understanding of how the health system is affecting individuals.

3.2.170 As indicated, the problem of data quality, quantity, relevance and accuracy has repercussions not only for planning but also for monitoring and evaluation activities. As such, it is an area that warrants concerted action by the Department. We were advised that action is being taken within the Aged, Community and Mental Health Division to address data collection issues relating to funded services.

Recommendation

3.2.171 It is important that a co-ordinated approach is taken by divisions to address data limitations. In particular, consideration should be given to establishing consistent bases of counting across programs and across the service system. In order to facilitate analysis of data over extended periods of time, whenever new counting rules are introduced for programs consideration should be given to maintaining parallel counting for a period of time.

Standard of documentation

3.2.172 We experienced considerable difficulty in assessing whether the development and planning of specific programs and initiatives was sufficiently strategic, due to gaps in documentation and the inability of staff to recall past events. In many cases, the official records failed to document key aspects of program development and delivery, particularly:

- the rationale or justification for introducing the program or initiative;
- decisions relating to the development phase, such as the best means to roll-out the program, whether or not to undertake a pilot etc;
- justification of the quantity, size and number of pilots to be established, if any; and
- the level of funding to be allocated.

3.2.173 This was particularly the case in relation to the Geriatric Evaluation and Management and Unassigned Geriatric Evaluation and Management initiatives, the Continuum of Care project and the Post-Acute Care Program. In the case of the sub-acute service initiatives, where responsibility had been transferred between divisions in the past year, the lack of records and organisational knowledge was particularly noticeable. Our examinations covering the implementation of programs and initiatives also revealed significant gaps in documentation, particularly in regard to analysis of data, progressive monitoring of program performance, and recording of ongoing strategies and key decisions.

3.2.174 We also found that a number of restructures, staff movements across divisions and between program areas, and staff departures over the decade meant that it was difficult to obtain a complete history of events.

Conclusion

3.2.175 Early in the decade, the Department gave insufficient attention to strategic planning across the health system. In recent times, strategic planning is being given a greater focus. This is essential to improve the quality of information available for decision-making and resource allocation so that service offerings mirror the emerging health needs of the community.

Recommendation

3.2.176 Documentation of key information is necessary to maintain an adequate management trail and to enhance accountability, especially where there are periodic restructures and frequent staff movement. Accordingly, we consider it advisable that the Department take early action to improve documentation maintained on departmental policy and program files and to develop appropriate arrangements for handover and transition of activities. As well as enhancing accountability, this action is essential to retain corporate knowledge so that past successes can be replicated and failures avoided.

Policy and funding framework

Aspects of a good policy and funding framework

3.2.177 A good policy and funding framework for post-acute care would:

- encourage a focus on patient outcomes;
- give service providers the flexibility to provide, or enable patient access to, integrated services that meet patient needs;
- minimise program boundaries and duplication of services between levels of government that lead to inefficient service provision and difficulty for individuals navigating available services; and
- set clear quality standards, monitor their achievement and respond to the issues raised in such monitoring.

3.2.178 The existing policy and funding framework requires much improvement in all these areas, although some flexible policy and funding models that provide integrated services have been developed at the State and Commonwealth levels, as discussed below.

3.2.179 The Department's Primary Care Partnerships Strategy, launched in April 2000, is intended to develop an integrated system within community health that focuses on early intervention, prevention and planning. The intention is that clients should be able to access the system at any point, with service providers using a common measurement approach, a common referral process and guaranteed client confidentiality. The Strategy provides funding and support to groups of primary care providers who form voluntary, local alliances, and aim to create a genuine primary care service system. The Strategy, which grew from the original Primary Health and Community Support Services Strategy launched in 1998, has not yet progressed sufficiently to assess its impact.

3.2.180 A number of flexible funding options have appeared over the last decade. The principal benefit of these programs lies in flexibility, allowing services to be delivered according to community needs. Examples include the Healthstreams and Multi-Purpose Services models of rural health and aged care provision. Both these models focus on care in the rural and remote areas of the State and are heavily dependent, both for departmental approval and for ongoing success, on community involvement.

3.2.181 The Healthstreams Program is delivered as part of an agency's health care program and provides a number of State-funded health and community services, decided according to a service plan. In 1999-2000, a total of $1.8 million was provided to the 8 Healthstreams services operating in the State, namely:

- Moyne Health Services;
- Heywood and District Memorial Hospital;
- Lorne Community Hospital;
- Penshurst and District Health Service (now a campus of the Western District Health Service);
- Yarram and District Health Service;
- Beaufort and Skipton Health Service;
- Tallangatta Health Service; and
- Maryborough District Health Service.

3.2.182 Under the Multi-Purpose Services Program, funds from other Commonwealth and State programs are pooled within a multi-purpose service to form a single budget, to provide care to suit the health and aged care needs of individual communities as stipulated by a community driven service plan. Departmental documentation shows that care provided under the model can cover the spectrum of health services including acute hospital care, residential aged care, community health, inpatient respite beds, home and community care services, home nursing, geriatric assessment and rehabilitation, day care, immunisation or meals on wheels. The Program has been operational since the early 1990s, although was not introduced in Victoria until 1995. Seven services currently operate within the State, namely:

- Otway Health and Community Services: servicing a catchment in excess of 3 200 persons;
- Mallee Track Health and Community Service: set on 4 sites (Ouyen, Patchewollock, Underbool and Murrayville) servicing a population of around 2 400;
- Alpine Health: a multi-site service based at Myrtleford, Bright and Mt Beauty servicing an area with a population of more than 13 000;
- Upper Murray Health and Community Services: based in Corryong on the Victorian border with New South Wales. It provides support to an isolated rural community of around 3 200 people;
- Far East Gippsland Health and Social Support: based in Orbost servicing a population of around 4 500;

- Robinvale District Health Service: based in Robinvale on the Murray River servicing a diverse population of around 5 000 that includes Tongan and Aboriginal communities; and
- Timboon and District Health Service: located in Victoria's western district servicing a population of around 8 000.

3.2.183 The Report of a recent evaluation of 5 Victorian multi-purpose services observed that the program *"… serves as an exceptional demonstration of a flexible care service model for small rural communities. The flexibility inherent in the model provides the foundation for that success, but it has also been established that experienced management, vision and an entrepreneurial perspective is required to realise its potential"*.

3.2.184 The Unassigned Geriatric Evaluation and Management model of sub-acute care is another flexible funding model provided by the State. It enables hospitals to "cash in" sub-acute bed days to enable purchase of community services to meet patient needs. Budgeted expenditure under the model for 2000-01 is $1.4 million, the equivalent of 4 164 bed days.

3.2.185 The Coordinated Care Trials, initiated by the Commonwealth, pool State and Commonwealth funds, and are designed to develop and test innovative service delivery and funding arrangements with the aim of improving access to allied health, community and hospital services for people with long-term, complex care needs. Two rounds of Trials have been initiated. In the first round, which was conducted from 1997 to 1999, 2 Trials were undertaken in Victoria, namely:

- the North Eastern Health Care Network: covering the municipalities of Whittlesea, Banyule, Nillumbik, and the northern part of Darebin with a target group of 1 056 patients with diseases and disabilities typical of, but not exclusive to, old age; and
- the Southern Health Care Network: covering the municipalities of Greater Dandenong, Casey and Cardinia. The Trial had a target group of 2 500 patients with a broad range of chronic/complex health conditions.

3.2.186 A report on the evaluation of the Trials is due in the next few months. We note the findings of recent research[8] that co-ordinated care is beneficial for appropriate patients, but is unlikely to have a major impact on acute care utilisation in the short-term. It is expected that the second round of Coordinated Care Trials will commence later in 2001.

8 Dwyer and Jackson, op. cit.

Co-ordination within and between levels of government

Co-ordination within the Department

3.2.187 We found that within the Department there were divergent approaches to dealing with the changing trends in health service delivery over the decade under review. Overall, the Department's approach could have been more pro-active and co-ordinated by establishing policies and funding to deal with forecast trends.

3.2.188 Within the Acute Health Division we found there had been a large number of programs and initiatives introduced within hospitals or on the perimeter of the acute hospital sector, particularly over the last 5 years, although the level of additional resourcing allocated was relatively small. A number of pilots had been undertaken, but decisions to roll-out on a wider scale or to allow them to continue were at times made prior to evaluation of the pilots being undertaken or finalised. The Post-Acute Care Program and the Continuum of Care initiative were examples of this.

3.2.189 The response to emerging trends by the Aged, Community and Mental Health Division in relation to the areas of interface between care settings has been slow. This has reflected the Division's perspective that:

- Change in the primary care system is effective only if conducted at a measured pace, given the large number of individual service providers in the sectors; and
- The sector is largely driven by Commonwealth priorities because the majority of funds for aged care and primary care are provided by the Commonwealth Government, through either its own programs and initiatives or, in the case of general practitioners, through the Medical Benefits Scheme.

3.2.190 While some communication and co-ordination between the Divisions took place during the planning and development phases of programs and initiatives, co-ordination during the implementation phase was less evident. For example, in relation to the Post-Acute Care Program, while the Aged, Community and Mental Health Division and Acute Health Divisions each took part in the development and implementation of the pilot phase, once roll-out of the Program commenced, departmental documentation showed that communication between the Divisions related to periodic requests for transfer of funds between the Divisions rather than ongoing communication about the Program's implementation. The Department advised that the Aged, Community and Mental Health Division was involved in the development of the Resource Allocation Model and the Health Outcomes and Cost Benefit Study.

Commonwealth/State co-ordination

3.2.191 We found there are a number of programs and initiatives of the Commonwealth with the potential to impact on the activities of the State. Table 3.2V provides a summary of some of the programs and initiatives relevant to the interface between the acute and post-acute settings, funded by the Commonwealth during the past decade.

TABLE 3.2V
COMMONWEALTH OR JOINT PROGRAMS AND INITIATIVES

Program/initiative	*Purpose*	*Responsibility and year introduced*
Aged Care Assessment Program	To comprehensively assess frail elderly people either in hospitals or in the community and make recommendations for their long-term care needs, including determination of eligibility for residential aged care and Community Aged Care Packages.	Commonwealth/ State 1984
Multi-Purpose Services Program	To provide a full range of health and support services to small, isolated rural communities through integrated health, community and residential services.	Commonwealth/ State 1992
Divisions of General Practice Program	To provide the infrastructure to enable general practitioners to develop local networks and to engage in co-operative activities and projects to improve integration with other sections of the health industry.	Commonwealth 1992
Coordinated Care Trials	To test whether multi-disciplinary care planning and service co-ordination improve health and wellbeing for people with chronic health conditions or complex care needs.	Commonwealth 1997
Enhanced Primary Care Package	To assist people with chronic illnesses and complex care needs, carers and health professionals.	Commonwealth 1999
Regional Health Services Program	To incorporate multi-purpose centres, multi-purpose services and multi-purpose health and family services networks, and to work with small rural communities to enhance access to primary health and aged care services.	Commonwealth 1999
National Demonstration Hospitals Program	To develop best practice in hospitals and linkages with primary and community care to enable seamless transition from one care environment to another.	Commonwealth 1994
More Doctors, Better Services (Regional Health Strategy)	To bring together existing and new initiatives to attract more doctors and allied health professionals to regional, rural and remote communities, and to provide better health services in those areas.	Commonwealth 2000 and 2001

3.2.192 The Commonwealth also administers nationally the Home and Community Care Program, introduced in 1985. Each State and Territory administers the Program in its jurisdiction. Designed to provide community care services to frail aged and younger people with disabilities, and their carers, to enhance independence and avoid long-term residential care, the Program is joint funded by the Commonwealth and the State with the Commonwealth providing approximately 60 per cent of the total budget. In 2000-01, the Commonwealth's budgeted contribution to Victoria for services provided under the Home and Community Care Program is $157.2 million.

3.2.193 In addition, the Commonwealth has provided $25 million from the National Health Development Fund to support the implementation of the Primary Care Partnerships Strategy. The funding is to assist development of information management capacities within the Partnerships ($15 million over 5 years) and development of a telephone Health Information Advice and Referral Service ($10 million over 5 years).

3.2.194 The State's partial capacity to drive the health sector increases the need for well-managed communication and co-ordination with the Commonwealth. The Commonwealth has collaborated with the State to strengthen primary health and community care under the auspice of the Australian Health Ministers' Advisory Council. The Council comprises the heads of the health authorities of the Commonwealth, State and Territory Governments.

3.2.195 We were advised that officers of the State and Commonwealth Departments meet regularly for the development and integration of primary health and community support services, to facilitate integration with general practice and acute services. Examples include:

- Participation by the Commonwealth Department of Health and Aged Care in the Victorian Advisory Committee on General Practice. The Departments are working collaboratively with the Divisions of General Practice to support the general practitioners to participate in health promotion and service co-ordination within community-based services and between acute/sub-acute services and community-based services. The introduction of the Commonwealth's Enhanced Primary Care Package and Medical Benefits Scheme items will facilitate the involvement of general practitioners;
- Close liaison on recent initiatives such as the Commonwealth's Coordinated Care Trials, the State's Integrated Disease Management Project under the Primary Care Partnerships Strategy and the Aged-Acute Interface project under the Emergency Demand Management Strategy;
- Regular communication with the Commonwealth in relation to matters such as the Home and Community Care Program, Aged Care Assessment Services and development of information systems; and
- Participation in a Commonwealth/State Work Plan dealing with acute/aged care interface issues. The Australian Health Ministers' Conference, consisting of Commonwealth, State and Territory Government Health Ministers, as well as the Australian Health Ministers' Advisory Council have agreed the Work Plan.

Administrative duplication and inefficiency

3.2.196 Given the proliferation of programs and initiatives from within the Department and from the Commonwealth, there is the potential for overlap of services and administrative duplication. Therefore it is particularly important that the activities of the Commonwealth and State, and between divisions of the Department, are well co-ordinated. The Department advised that "*the Primary Care Partnerships Strategy, Healthstreams Program, Multi-Purpose Services Program and Coordinated Care Trials represent significant advances in community-based planning and service co-ordination and have been shown to reduce duplication and create better outcomes for clients*". The recent evaluation of the Multi-Purpose Services Program reported favourably on the model.[9] However, of the remaining 3 models, only the Coordinated Care Trials has been evaluated. The final report of that evaluation is not yet available.

3.2.197 Comments received by us during the planning phase of the audit, and in response to a limited survey of peak bodies and service providers, indicated that there is still improvement required to ensure that administrative duplication and complexity in service offerings is minimised both for service providers and patients. The comments received by us were in line with comments raised in the report on the Review of Primary Health Development issued in December 1999 following a review of the Primary Health and Community Support System.

Conclusion

3.2.198 The policy and funding framework which impacts on post-acute care is highly complex. Some flexible models have been developed at the State and Commonwealth level which attempt to provide integrated services and reflect the requirements of local communities or patient groups, but they have been small-scale and have yet to demonstrate their broad applicability.

Recommendation

3.2.199 Given their respective roles and the proliferation of programs and initiatives from within the Department and from the Commonwealth, continued co-ordination is required to avoid systems complexity and duplication of services.

9 Sach & Associates in association with Centre for Applied Gerontology, *Multi-Purpose Services Program Evaluation (Victoria)*, Commonwealth Department of Health and Aged Care and Victorian Department of Human Services, November 2000.

Encouraging innovation and improved service delivery

3.2.200 While the development of policy and allocation of public resources to address the health needs of the community are the responsibility of both the Commonwealth and State Governments, the delivery of health care is the responsibility of individual health service providers such as hospitals, community health services, general practitioners and allied health professionals. Given their direct service delivery role and proximity to patients, health service providers are in a prime position to identify and monitor the direct impacts of government resource allocation and to contribute to identification and implementation of quality improvements.

3.2.201 In order to encourage innovation and improve the quality of health service delivery, the Department can employ a number of mechanisms including:

- providing rewards and incentives, financial or otherwise, for innovation and good practice;
- encouraging pilot projects to test new initiatives; and
- encouraging sharing of ideas between service providers and across jurisdictions.

3.2.202 The following paragraphs discuss each of these mechanisms.

Providing rewards and incentives for innovation and good practice

3.2.203 There are a number of examples in recent years of the funding of health services through incentive mechanisms linked to innovation and good practice, with payment directly linked to success. The disadvantage of such approaches is that, on their own, they do not provide resources that might assist poor performers to improve.

3.2.204 Examples of incentive systems used by the Victorian Department of Human Services include:

- The Effective Discharge Strategy, introduced in 1998 to encourage improvement in hospital discharge processes and practices, thus facilitating better outcomes for patients during their transition from the acute health sector. During 1998-99 and 1999-2000, the Strategy provided funding for the establishment and/or improvement of discharge plans, and made bonuses available for good performance. This approach has the benefit of providing some base resources to support improvements in practice, as well as incentives. The allocation of bonuses was based on the results of the June 1999 and June 2000 audits of patient records. In 1999-2000, bonuses totalled $4.1 million, including an amount of $374 000 paid subsequent to the distribution of bonuses, to address a miscalculation in the initial payments. Between the 2 audits, there were significant improvements in discharge performance. However, the extent to which this was due to the incentive arrangements is unknown. The funds available for each hospital under the Strategy were relatively limited and it is unclear whether the right balance was struck between provision of base resources and incentives.

The Department's longer-term strategy was to develop indicators to monitor implementation of the Strategy. These indicators were released in November 2000. Payments for 2000-01 will not be in the form of bonuses for good performance. Instead, the $3.9 million available has been distributed to hospitals to fund establishment of data collection systems for the effective discharge performance indicators. The allocations were calculated based on the level of patient separations. The use of incentive arrangements in future is unclear;

- The Hospital in the Home Program, was introduced in 1994 to provide patients with greater options in health care during their acute illness by giving them the choice of receiving part, or all, of their hospital care in their own homes. This Program initially provided establishment funding plus per patient bonuses to hospitals, over and above the casemix payment. A costing study undertaken in December 1999 found that Hospital in the Home can be funded from the casemix system for most conditions and was less costly than inpatient stays for some conditions and some patients. Hospitals providing Hospital in the Home care now receive an annual base grant to be used to enhance medical and nursing leadership capacity and the quality of service delivery. Each participating hospital is grouped into one of 6 bonus pools and receives a bonus if it exceeds the average "substitution rate" for its pool. The substitution rate is number of days of care provided through Hospital in the Home days as a proportion of total inpatient days. Quality improvement grants are also available for projects to improve quality, accessibility, promote growth and to improve the efficiency and effectiveness of the Program; and
- The Department recently launched a $10 million Human Services Productivity Investment Fund which is intended to provide financial assistance to improve the efficiency of organisations in the Human Services sector, either through one-off project funding or feasibility funding to develop and pilot projects to improve efficiency and financial viability. Agencies will be required to demonstrate quantifiable savings which will assist them to meet the Government's 1.5 per cent productivity goal.

3.2.205 The Department advised that rewards for performance against measured targets have also been used for the Hospital Access Program.

Encouraging pilot projects to test new initiatives

3.2.206 The Department has a long history of funding pilot projects to test or aid development of new service delivery approaches. There have been several important pilot projects in the suite of responses to demand for post-acute care:

- The Post-Acute Care Program that commenced in 1996 was intended to develop new models of service delivery for post-acute care services and develop appropriate performance indicators and measures for future policy. Six post-acute care pilots were established and operated over a period of 18 months. The Program was subsequently rolled-out in stages, prior to any formal assessment of the success of the pilots. The level of activity and the breadth of coverage of the Program is gradually increasing. However, the Program remains small and the boundaries with Home and Community Care and other community services are poorly defined. In 2000, the Program became a Statewide program by expanding the geographic boundaries of the existing 18 Post-Acute Care projects to cover the entire State. Prior to that expansion, and recent changes to the resource allocation basis and increase in funding, the services were not well distributed across the across the State. The impact of these recent changes cannot be determined at this stage. We were advised that while the Post-Acute Care Program was piloted, it was always the intention that it would be rolled-out on a wider basis. This indicates that the pilot phase was a pilot in name only;
- Piloting of the Continuum of Care funding model commenced during 1997 and continued for approximately 12 months. The pilot was to test the model's feasibility and application and to determine whether it would enable more appropriate funding of sub-acute services through the delivery of cost-effective, integrated care. The approach enables a hospital to "cash in" sub-acute geriatric evaluation and management bed days for community services provided by staff of the hospital. We were advised that following the initial 12-month period, despite problems with the funding formula, the model continued to operate at some of the pilot sites for a further 6 to 12 months. It was not until November 1999, 2 years after the pilot period, that a report on the pilot, containing largely favourable conclusions, was issued. Since the transfer of sub-acute services to the Acute Health Division in August 2000, the model has been incorporated into sub-acute care funding options available to public hospitals under the Policy and Funding Guidelines; and
- Since 1998, the Department has provided funding to public hospitals through an annual project submission process. The Quality Improvement Funding Round encourages the use of health care practices known to improve health outcomes, and to encourage best practice use of resources through systems redesign. The Department advised that around $3 million is available for projects under the Acute Quality Improvement Program for 2000-01, including $1.4 million for ongoing projects or continuing programs from previous years and around $1.5 million for new projects. In addition, around $364 000 will be spent in 2000-01 on 3 quality improvement projects continuing from the 1999-2000 Sub-Acute Quality Funding Round.

3.2.207 The above pilots appear well conceived in that they piloted worthwhile initiatives. However, it is of concern that the success of the pilots was not always fully assessed prior to the programs being integrated into the suite of service offerings.

Encouraging sharing of ideas between service providers and across jurisdictions

3.2.208 The Department can encourage innovation through supporting the sharing of information and good practice between players in the health system. There are some examples of this:

- The Department provided seed funding for the establishment and maintenance of an industry resource centre, the Victorian Centre for Ambulatory Care Innovation, for a period of 3 years from 1997-98. The Centre promotes clinical research, development, trialling and evaluation of Hospital in the Home-type initiatives; and provides information and advice on the latest developments in the field of home-based care. The Centre maintains a reference database, facilitates seminars and conferences, and develops standards and clinical guidelines for Victorian health care providers.

  The Department advised that at the time of providing the initial funding it was intended that the Centre should build up income from other sources such as tenders and grant applications. Since the expiry of the initial funding period, the Department has agreed to provide a reduced level of funding for a further 3 years. The Department advised that the grant was adjusted to bring it into scale with other infrastructure grants, given the scope of work undertaken by the Centre;
- During 1999, the Department provided funding to the Royal Melbourne Hospital to participate in the Breakthrough Series in the United States. The Breakthrough Series is an initiative that provides clinical, technical and social support for health care organisations to make major, rapid change to produce better outcomes, while also lowering costs. In 2000, the Department funded the Victorian Collaborative Breakthrough Series involving all hospitals in Victoria that have major emergency departments, with a focus on “Reducing Waits and Delays and Improving Patient Satisfaction in the Emergency Department”. The Department and the Royal Melbourne Hospital are joint sponsors of the project and the hospital is managing the project using the knowledge gained from its involvement in the United States; and
- A condition of funding of the recent Quality Improvement Funding Round is that funded services disseminate the results of their projects through participation in seminars and conferences or through other means.

3.2.209 Over recent times, the Commonwealth Government has introduced several initiatives designed to encourage service innovation and improvements in service delivery via information sharing between service providers, including:

- Funding the Australian Resource Centre for Hospital Innovations to provide information about innovations in acute care in the hospital or in the community, to health sector personnel and to provide links between professionals to aid problem solving; and
- Establishing the National Demonstration Hospitals Program to create relationships between hospitals, facilitate sharing of information and expertise among hospitals, and support the implementation and evaluation of systems and processes to improve hospital services, including their co-ordination and integration with community providers and general practitioners.

Conclusion

3.2.210 We found that some encouragement of innovation and improved serviced delivery for services in the sub-acute and post-acute sectors occurred in the latter part of the decade, mostly through the Acute Health Division. While the Department introduced a range of programs and initiatives to respond to demand for services in the sub-acute and post-acute sectors, because of the limitations in the available data, we were unable to conclude on the adequacy of that action.

Program monitoring and evaluation

3.2.211 Program monitoring and evaluation are key components of a sound performance management framework. Considerable activity has been, and is being, expended at the national, State and program level to develop performance measures and indicators for monitoring public sector performance. Our audit focused on the development of indicators for sub-acute and post-acute care, in the Department of Human Services.

Development of the Department s performance management framework

3.2.212 The development of the Department’s performance management framework has, over time, been the responsibility of the Business Improvement Branch, then the Business Development Branch and finally, from March 2001, the Policy and Strategic Projects Division.

3.2.213 Over an extended period, performance indicators for sub-acute and post-acute care have been developed and published in the *Human Services 2000-01 Departmental Plan*. The relevant indicators include:

- *Acute Health Division:*
  - Existence of discharge improvement plans;
  - Development of performance indicators for effective discharge;
  - Provision of hospital contact details upon discharge from public hospitals and sub-acute services;

    - Coverage of acute public hospitals by the Post-Acute Care Program;
    - Level of district nursing and home support services; and
    - The number of open post-acute and sub-acute beds;
- *Aged, Community and Mental Health Division:*
    - Existence of guidelines to support health promotion and community health plans for Primary Care Partnerships;
    - Completion of Community Health Plans;
    - Hours of assessment services;
    - Participation by rural and regional health services agencies in Rural Healthstreams, Multi-Purpose Services and Commonwealth Health Service programs;
    - Access to Home and Community Care services by vulnerable older people;
    - Existence of streamlined assessment and information services to enable older Victorians to receive services that meet their individual needs; and
    - Effectiveness of allocation and targeting of Home and Community Care resources.

3.2.214 Examination of the above indicators reveals a focus on activity levels, that is, units of throughput, and processes rather than measures of quality such as relapse, complication and readmission rates, the level of client satisfaction with hospital discharge and with community services funded by the Department, or measures of efficiency. The indicators also do not address continuity of care. Patient-focused indicators are discussed in later paragraphs.

3.2.215 We were advised that recent activity has been aimed at providing better links between departmental objectives, output groups and outcomes, and rationalising performance indicators in funding and service agreements between the Department and external service providers. Attention was also to be given to developing indicators of quality for each of the Department's activities. Documentation provided to us at the time of preparation of this Report indicated that the review of the Department's output structure has been completed. However, the development of indicators to link performance to the output structure is continuing.

Activity within divisions

3.2.216 The Department's health-related divisions have focused activity on the development of performance indicators for specific programs or components of health service delivery. Relevant areas for sub-acute and post-acute care include:

- patient satisfaction with hospital services;
- clinical indicators relevant to the acute health sector, including unplanned readmissions;
- effective discharge; and
- streamlining and improving indicators for the Aged, Community and Mental Health Division, including those in service agreements with service providers.

3.2.217 The Acute Health Division's *Victoria – Public Hospitals Policy and Funding Guidelines 2000-2001* reveal a number of proposed activities for the current year, including developing indicators for effectiveness and safety, the organisation of systems for quality improvement and progress on developing indicators to monitor quality of care, reporting on quality of care provided to older Victorians, and integrating the approach to measurement and quality improvement in acute and sub-acute services. Departmental officers advised us that performance indicators for the Post-Acute Care Program are to be developed in 2001-02.

3.2.218 While acknowledging the planned activity, we consider it is important that action be taken at an early stage to develop means for monitoring the effectiveness of the range of programs and initiatives overseen by the divisions.

Patient-focused measures

Patient satisfaction

3.2.219 The Department has used "one-off" or "point-in-time" surveys of patient satisfaction since the introduction of the casemix system in 1993 to measure patient perceptions of their hospital care. The most recent major survey was carried out in 1997. Following that survey, work was undertaken to focus surveys on aspects of care identified as being of importance to patients and to broaden the range of indicators.

3.2.220 During 1999-2000, a model for regular monitoring of patient satisfaction in Victorian hospitals was developed. The model, referred to as the "Patient Satisfaction Monitor", was introduced in October 2000 and the first 6-monthly report from all hospitals other than small rural hospitals is due in May 2001. The first annual report with results from all hospitals is due in October 2001.

3.2.221 These surveys are an important aspect of monitoring the effectiveness of Victoria's health system. While we are aware that individual hospitals undertake surveys of their patients, we consider that a period of 4 years without a comprehensive survey of all hospitals is unacceptable. Consideration should also be given to the release of data on a hospital basis to assist patient decision-making, and on extending the approach beyond the acute hospital system.

Continuity of care

3.2.222 Provision of continuous care to meet the individual needs of a patient, that is, to provide the right type of care, at the right time, across the spectrum of health services, has emerged as a key aim for health systems in developed nations. Development of performance indicators measuring continuity of care is a complex and demanding task challenging health professionals around the world.

3.2.223 A suite of indicators of care continuity would ideally track the experience of patients as they interact with the health system and would need to include indicators relating to each of the care categories, that is, pre-admission, acute, sub-acute, post-acute, community and aged care and within each category could address:

- availability of, and access to, required services;
- timeliness of service provision;
- incidence of inappropriate discharge from one care setting to another;
- follow-up of patients after transition from one care category to the next, including timeliness of follow-up;
- provision of care in accordance with the discharge plan; and
- patient satisfaction with the care provided.

3.2.224 Our audit revealed that much of the progress to date in developing performance indicators for health service delivery has focused within the individual divisions of the Department, rather than on developing across system indicators of performance, which could measure continuity of care. We acknowledge the difficulty in measuring across-system performance in the absence of unique patient records in electronic form.

3.2.225 We found that some of the indicators developed by the Acute Health Division could be incorporated into a suite of indicators of care continuity, e.g. indicators of timeliness of admission to acute hospitals, effective discharge and patient satisfaction with public hospital services. The Acute Health Division's *Victoria – Public Hospitals Policy and Funding Guidelines 2000-2001* stated that development of performance indicators for continuity of care and indicators of access to, and acceptability of, care was to be undertaken during the year. We acknowledge that some important indicators have not been publicly collected and/or reported since 1997, in particular patient satisfaction.

3.2.226 Activity within the Aged, Community and Mental Health Division was focused primarily on improving its performance management framework as a whole, rather than specifically on developing indicators of continuity of care.

Conclusion

3.2.227 Based on our examinations of the Department's performance management framework, we concluded that progress to date has been slow. Due to the delays in developing indicators, non-collection and/or reporting of some important indicators (such as patient satisfaction) and limitations in the data available for performance monitoring, the Department cannot currently adequately monitor the effectiveness of post-acute care provision.

Recommendation

3.2.228 The Department should address its inadequate monitoring of effectiveness of the service delivery models for the provision of post-acute care, in particular the non-collection and/or reporting of some important indicators (such as patient satisfaction).

Program evaluations

3.2.229 Program evaluation should form part of an organisation's strategic planning and resource allocation processes and should contribute to improved program management, greater accountability, informed decision-making and better use of resources. Key questions to be asked when evaluating programs to determine whether they have met their objectives include:

- Are the program objectives clearly specified?;
- Is the program achieving its objectives?;
- Does the design of the program contribute to the achievement of objectives and reflect good practice in the area?; and
- Is the program providing value-for-money?

3.2.230 Our discussions with departmental officers indicated that the need for evaluation of program performance is well understood. While we found no formal guidelines requiring evaluations to be undertaken, we noted instances such as the Post-Acute Care pilots and the Hospital in the Home Program where the intention to evaluate was flagged early in the development stage. We also found examples of recent evaluations undertaken by, or on behalf of, the Department such as the Review of Chest Pain Evaluation Areas and the Evaluation of Multi-Purpose Services.

3.2.231 Despite the acceptance of evaluations within the Department, we found that evaluations of programs and initiatives had not always been carried out. In some cases, decisions to roll-out or continue programs and initiatives had, at times, been made despite the lack of an evaluation or, where evaluations had taken place, prior to the results being finalised.

Barriers to evaluation

3.2.232 The ability to undertake evaluations is affected by the availability of sufficient relevant and reliable data upon which to base the analysis and the establishment of relevant indicators against which to measure performance.

3.2.233 Problems relating to performance indicators and the quality of data have been discussed in earlier paragraphs. The evaluation of relatively new programs or initiatives can be difficult given that sufficient data will generally not be available for analysis. In such cases, the focus of evaluation activity should be on the establishment of appropriate data collection arrangements to facilitate ongoing monitoring and evaluation.

3.2.234 As mentioned earlier, the Department often pilots programs or initiatives to monitor potential impacts, prior to rolling them out on a wider scale. These pilots usually run for a period of 6 to 12 months but may extend over a longer period. We found the evaluation of pilots to be problematic in that the impacts of new health programs or initiatives may not be realised until some time after their introduction and sufficient data to enable evaluation may not be available within the pilot phase. However, in such cases it is important that the Department has in place alternative means of establishing the success of pilots and informing decision-making prior to roll-out of the programs or initiatives.

3.2.235 We did find that the Department generally establishes Steering Committees or Advisory Committees, comprising representatives of the Department and pilot groups, to monitor the pilot phase. We consider that, in addition to these Committees, there is benefit in undertaking formal mid-term reviews of progress against pilot program objectives in order to inform decision-making.

Examples of evaluation practice

3.2.236 A review of a selection of programs and initiatives dealing with the interface between acute and post-acute care revealed a range of evaluation practices had been adopted. The following provides a summary of findings in relation to specific programs and initiatives examined:

- The Hospital in the Home Program was piloted in 1994. An evaluation of the pilots including consideration of whether the objectives of the Program had been achieved, was undertaken in 1996. However, the Program was expanded in May 1996, 7 months prior to release of the evaluation findings. Adjustments to the Program were then made later, after release of the evaluation findings, including the conduct of further more detailed studies. To date, the Department has spent $529 000 on evaluations of the Program, an equivalent of 1.8 per cent of the total funds allocated to the program since its inception;
- Early in development of the Post-Acute Care pilots, the Department signalled its intention to appoint an independent consultant to evaluate the pilots. It was subsequently determined however, that an evaluation should not proceed until sufficient data was to hand to form the basis of the evaluation. Delays in development of the database meant that consistent and reliable data was not available at the completion of the pilot phase. The Post-Acute Care Program was subsequently rolled-out in 4 stages from 1997 to 2000 without an evaluation of the Program having been undertaken.

We consider that evaluation of the outcomes of the pilots would have been of great benefit given that a key objective of that phase was to inform decision-making about the most appropriate methods for the funding and delivery of post-acute care in the future. The failure to evaluate the pilots meant that the opportunity to analyse the effectiveness of the various models piloted and to identify the most appropriate model prior to the roll-out of the Program, was forgone.

In 1998, after completion of the pilot phase and after Program roll-out had commenced, consultants were engaged by the Department to evaluate the health outcomes and cost-benefits of the Program. We found the scope of the evaluation to be limited in that it did not set out to evaluate whether all of the Program's objectives were being achieved. However, it did seek to evaluate the cost-benefit of the Program compared to post acute care offered through existing arrangements. At the time of preparation of this Report, the results of the consultancy were yet to be released and were not provided to the audit team for review. However, the Department has advised that the results are to be released in May or June 2001 and indicate that the sample of patients in the study who received services under the Post-Acute Care Program had a better health related quality of life and reduced readmission rates in the 6 months post-discharge and that the program was cost-effective.

The cost of the evaluation has been $293 176, equivalent to 1.3 per cent of the total funds allocated to the Program to date. The Department advised that a broader evaluation of the Program is to take place in 2001-02;

- The Continuum of Care model was officially piloted in 1997, in 3 extended care centres, over a period of 12 months, but was then extended at some sites and ultimately incorporated into the range of sub-acute care funding options available to hospitals. A concurrent evaluation process involving patient satisfaction surveys, patient, carer and staff focus groups, and measurement against a pre-established performance indicator was set in place at the outset of the pilot. As mentioned earlier, a report on the pilot was released in late 1999.

  In early 2001, the Department invited tenders *"to examine the performance of the sub-acute service system and models for future sub-acute service delivery, and prepare a strategic planning framework for the future provision of sub-acute care services in Victoria"*. We consider it likely that the evaluation will consider the effectiveness of the above model as well as the Geriatric Evaluation and Management and Unassigned Geriatric Evaluation and Management initiatives for funding sub-acute services;

- The Effective Discharge Strategy was introduced in 1998-99. Since its implementation, hospitals have participated in 2 annual patient record audits during which levels of compliance with requirements relating to discharge planning were assessed. However, the audits were limited to an assessment of processes and documentation and did not directly assess the effectiveness of the Strategy in achieving better outcomes for patients discharged from hospitals. The total cost of the 2 audits was $907 970, or 3.7 per cent of the total budget to 2000-01.

In late 2000, the Department launched a suite of performance indicators focused on processes of care, to provide a more cost-effective means of assessing continued performance. Data relating to these performance indicators is to be collected by participating services and reported to the Department;

- The Multi-Purpose Services Program pilot, a joint Commonwealth/State initiative commenced in 1992-93 and was first evaluated in 1994, prior to the establishment of any services within Victoria. The first Victorian multi-purpose services were established in 1995 and in 2000 an evaluation covering 5 of the 7 Victorian services was performed. The primary aim of the evaluation was to evaluate the effectiveness of the Program. The report on the evaluation was released in early 2001 and we were advised that action is underway between the Commonwealth and the State to address recommendations raised in the report; and
- The Primary Care Partnerships Strategy was announced in April 2000. The Department recently sought tenders for an evaluation of the Strategy to commence in mid-June 2001 and to be completed in June 2003. According to the tender documents, the objective of the evaluation is to *"provide information to the Department of Human Services, Primary Care Partnerships and the sector more generally to maximise learning from the service system redevelopment experience, and provide a basis for refinement of policy and service development"*. The long lead-time for the completion of this evaluation will limit its impact in the medium-term.

3.2.237 In addition to the above, evaluations of the Chest Pain Evaluation Area Units and the Maternity Services Enhancement Strategy to date have cost $66 000 (0.4 per cent of the total budget) and $966 430 (2.1 per cent), respectively.

Conclusion

3.2.238 Our examination of the selected programs and initiatives revealed that the Department's evaluation practices and expenditure vary considerably. A more consistent and effective approach to program evaluation is required.

Recommendation

3.2.239 The Department should establish a more consistent approach to program evaluation that requires integrating evaluations into the design of programs, timing them to support decision-making, using them to develop effective performance measuring and monitoring regimes and allocate funds to evaluation activities.

SCHEDULE A
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS

Report	*Subject*	*Status at date of preparation of this Report*
	MATTERS RESOLVED OR ACTION COMMENCED	
DEPARTMENT OF HUMAN SERVICES		
FINANCIAL VIABILITY OF PUBLIC HOSPITALS		
Ministerial Portfolios, June 2000, p. 80-2	As at 30 June 2000, there were a number of public hospitals showing signs of financial difficulty.	Further comment on the viability of hospitals is provided in this Part of the Report.
Maintenance of public hospital buildings		
Ministerial Portfolios, June 2000, p. 83-4.	The lack of a consistent methodology for the conduct of building condition assessments by hospital managers has resulted in a lack of reliable information being available on the estimated costs required to bring hospital buildings up to the required standards.	The Department of Human Services has implemented a number of initiatives in order to standardise its approach to asset management, planning and reporting. Condition-based surveys are in the process of being finalised for facilities in the Department's Acute Health, Aged Care, Community Health and Disability Services programs. The surveys have established the nature and extent of works required to bring facilities to the required standard, the prioritisation of the works and the related costs necessary to achieve compliance. The Department has advised that the broad-based surveys will be supported in the longer-term by site-specific masterplans, each with consistently derived asset data regarding age, condition and priority of remedial works.
Ministerial Portfolios, June 2000, p. 84-7.	Given the level of outstanding maintenance works, there is a need for the Department of Human Services to critically assess the maintenance requirements of all public hospital buildings and the associated funding implications.	The Department advised that the responsibility for ongoing maintenance of assets rests with individual hospitals and service delivery agencies. However, the Department has prepared a detailed schedule of infrastructure upgrade requirements for metropolitan hospitals, based on the abovementioned surveys. The Department has also advised that this schedule is to be continuously monitored and revised annually and that a similar schedule is to be developed covering rural facilities.

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS			
FINANCIAL YEAR ENDED 30 JUNE 2000			
Department of Human Services	28 Sept. 2000	19 Oct. 2000	✓
HEALTH			
Advanced Dental Technicians Qualifications Board *(a)*	12 Sept. 2000	21 Sept. 2000	✓
Alexandra and District Ambulance Service	25 Oct. 2000	25 Oct. 2000	✓
Ambulance Service Victoria - Metropolitan Region	28 Aug. 2000	5 Sept. 2000	✓
Chiropractors Registration Board of Victoria	17 Oct. 2000	20 Oct. 2000	✓
Dental Board of Victoria *(a)*	21 Dec. 2000	22 Dec. 2000	✓
Dental Technicians Licensing Committee *(a)*	12 Sept. 2000	20 Sept. 2000	✓
Infertility Treatment Authority	12 Sept. 2000	13 Sept. 2000	✓
Mental Health Review Board	29 Sept. 2000	2 Oct. 2000	✓
Nurses Board of Victoria	25 Aug. 2000	5 Sept. 2000	✓
Optometrists Registration Board of Victoria	28 Sept. 2000	29 Sept. 2000	✓
Osteopaths Registration Board of Victoria	28 Sept. 2000	28 Sept. 2000	✓
Pharmacy Board of Victoria	16 Aug. 2000	31 Aug. 2000	✓
Physiotherapists Registration Board of Victoria	29 Sept. 2000	2 Oct. 2000	✓
Podiatrists Registration Board of Victoria	13 Sept. 2000	13 Sept. 2000	✓
Psychosurgery Review Board	29 Sept. 2000	2 Oct. 2000	✓
Rural Ambulance Victoria	5 Sept. 2000	13 Sept. 2000	✓
Victorian Health Promotion Foundation	27 Sept. 2000	10 Oct. 2000	Qualified opinion
(Reason for Qualification:	*Failure to disclose prior period adjustments)*		
Victorian Institute of Forensic Mental Health	29 Aug. 2000	13 Sept. 2000	✓
Public hospitals			
Alexandra District Hospital	29 Sept. 2000	3 Oct. 2000	✓
Alpine Health	21 Aug. 2000	18 Sept. 2000	✓
Austin and Repatriation Medical Centre *(c)*	25 Sept. 2000	24 Oct. 2000	Qualified opinion
(Reason for Qualification:	*Inappropriate disclosure of non-reciprocal grants)*		
Bairnsdale Regional Health Service	23 Aug. 2000	31 Aug. 2000	✓
Ballarat Health Services	23 Aug. 2000	27 Sept. 2000	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS - *continued*			
Public hospitals - *continued*			
Barwon Health	23 Aug. 2000	22 Sept. 2000	Qualified opinion
(Reason for Qualification:	*Inappropriate disclosure of non-reciprocal grants)*		
Beaufort and Skipton Health Service	20 Aug. 2000	6 Oct. 2000	✓
Beechworth Hospital	21 Aug. 2000	12 Sept. 2000	✓
Benalla and District Memorial Hospital	22 Aug. 2000	20 Sept. 2000	Qualified opinion
(Reason for Qualification:	*Failure to consolidate a "controlled" entity)*		
Bendigo Health Care Group	20 Sept. 2000	29 Sept. 2000	Qualified opinion
(Reason for Qualification:	*Inappropriate disclosure of non-reciprocal grants)*		
Bethlehem Hospital Incorporated	28 Sept. 2000	6 Oct. 2000	✓
Boort District Hospital	5 Sept. 2000	13 Sept. 2000	✓
Caritas Christi Hospice Limited	21 Sept. 2000	22 Sept. 2000	✓
Casterton Memorial Hospital	15 Aug. 2000	11 Sept. 2000	✓
Central Gippsland Health Service *(b)*	23 Oct. 2000	23 Oct. 2000	✓
Cobram District Hospital	4 Aug. 2000	24 Aug. 2000	✓
Cohuna District Hospital	20 Sept. 2000	4 Oct. 2000	Qualified opinion
(Reason for Qualification:	*Failure to consolidate a "controlled" entity)*		
Colac Community Health Services	21 Aug. 2000	13 Oct. 2000	Qualified opinion
(Reason for Qualification:	*Non-review of the useful life of buildings)*		
Coleraine and District Hospital	26 Sept. 2000	12 Oct. 2000	✓
Dental Health Services Victoria *(c)*	2 Oct. 2000	2 Oct. 2000	✓
Djerriwarrh Health Services	28 Aug. 2000	29 Sept. 2000	✓
Dunmunkle Health Services	9 Oct. 2000	17 Oct. 2000	✓
East Grampians Health Service	8 Sept. 2000	23 Oct. 2000	✓
East Wimmera Health Service	26 Sept. 2000	12 Oct. 2000	✓
Echuca Regional Health	30 Aug. 2000	4 Oct. 2000	✓
Edenhope and District Memorial Hospital	9 Oct. 2000	11 Oct. 2000	✓
Far East Gippsland Health and Support Service	11 Oct. 2000	20 Oct. 2000	✓
Gippsland Southern Health Service	1 Sept. 2000	15 Sept. 2000	✓
Goulburn Valley Health	22 Aug. 2000	5 Sept. 2000	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS - *continued*			
Public hospitals - *continued*			
Hepburn Health Service	28 Aug. 2000	2 Oct. 2000	✓
Hesse Rural Health Service	24 Aug. 2000	2 Oct. 2000	✓
Heywood and District Memorial Hospital	31 Aug. 2000	14 Sept. 2000	✓
Inglewood and Districts Health Service	5 Sept. 2000	11 Sept. 2000	✓
Inner and Eastern Health Care Network	23 Aug. 2000	9 Nov. 2000	Qualified opinion
(Reason for Qualification:	*Failure to disclose prior period adjustments)*		
Kerang and District Hospital	5 Sept. 2000	12 Sept. 2000	✓
Kilmore and District Hospital	4 Oct. 2000	18 Oct. 2000	✓
Kooweerup Regional Health Service	11 Sept. 2000	22 Sept. 2000	✓
Kyabram and District Memorial Community Hospital	11 Aug. 2000	31 Aug. 2000	✓
Kyneton District Health Service	24 Aug. 2000	22 Sept. 2000	✓
Latrobe Regional Hospital	18 Sept. 2000	27 Sept. 2000	✓
Lorne Community Hospital	24 Aug. 2000	11 Oct. 2000	✓
Maldon Hospital	14 Sept. 2000	4 Oct. 2000	✓
Mallee Track Health and Community Service	25 Sept. 2000	25 Sept. 2000	✓
Manangatang and District Hospital	5 Sept. 2000	15 Sept. 2000	✓
Mansfield District Hospital	8 Sept. 2000	9 Oct. 2000	Qualified opinion
(Reason for Qualification:	*Failure to disclose CEO's remuneration)*		
Maryborough District Health Service	14 Sept. 2000	19 Sept. 2000	✓
McIvor Health and Community Services	6 Sept. 2000	13 Sept. 2000	✓
Mercy Public Hospitals Inc.	12 Dec. 2000	19 Dec. 2000	Qualified opinion
(Reason for Qualification:	*Failure to consolidate a "controlled" entity and inappropriate disclosure of non-reciprocal grants)*		
Mildura Base Hospital	14 Feb. 2001	9 Mar. 2001	✓
Moyne Health Services *(d)*	19 Sept. 2000	25 Sept. 2000	✓
Mt Alexander Hospital	20 Sept. 2000	4 Oct. 2000	✓
Nathalia District Hospital	22 Aug. 2000	15 Sept. 2000	✓
North Western Health Care Network	12 Oct. 2000	12 Oct. 2000	Qualified opinion
(Reason for Qualification:	*Inappropriate asset write-down)*		
Numurkah District Health Service	21 Aug. 2000	7 Sept. 2000	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS - *continued*			
Public hospitals - *continued*			
O'Connell Family Centre (Grey Sisters) Inc.	17 Oct. 2000	17 Oct. 2000	✓
Omeo District Hospital	12 Oct. 2000	27 Oct. 2000	Qualified opinion
(Reason for Qualification:	*Non-revaluation of land and buildings)*		
Otway Health and Community Services	25 Sept. 2000	2 Oct. 2000	✓
Peninsula Health Care Network *(c)*	21 Aug. 2000	22 Sept. 2000	Qualified opinion
(Reason for Qualification:	*Inappropriate disclosure of non-reciprocal grants)*		
Portland and District Hospital	24 Aug. 2000	11 Sept. 2000	✓
Queen Elizabeth Centre	21 Aug. 2000	20 Sept. 2000	Qualified opinion
(Reason for Qualification:	*Failure to consolidate a "controlled" entity)*		
Robinvale District Health Services	12 Oct. 2000	16 Oct. 2000	✓
Rochester and Elmore District Health Service	18 Aug. 2000	8 Sept. 2000	✓
Rural North West Health	14 Sept. 2000	13 Oct. 2000	✓
Seymour District Memorial Hospital	21 Aug. 2000	31 Aug. 2000	✓
South Gippsland Hospital	16 Oct. 2000	20 Oct. 2000	✓
South West Health Care *(e)*	28 Aug. 2000	31 Aug. 2000	✓
Southern Health Care Network	21 Aug. 2000	22 Sept. 2000	Qualified opinion
(Reason for Qualification:	*Inappropriate disclosure of non-reciprocal grants)*		
St Vincent's Hospital (Melbourne) Limited	27 Oct. 2000	30 Oct. 2000	Qualified opinion
(Reason for Qualification:	*Inappropriate recognition of debtors)*		
Stawell District Hospital	22 Sept. 2000	4 Oct. 2000	✓
Swan Hill District Hospital	25 Sept. 2000	10 Oct. 2000	✓
Tallangatta Health Service *(f)*	21 Aug. 2000	22 Sept. 2000	✓
Terang and Mortlake Health Service	30 Aug. 2000	14 Sept. 2000	✓
Timboon and District Healthcare Service	18 Aug. 2000	12 Sept. 2000	✓
Tweddle Child and Family Health Service	17 Aug. 2000	15 Sept. 2000	✓
Upper Murray Health and Community Services	31 Aug. 2000	21 Sept. 2000	✓
Wangaratta District Base Hospital	4 Sept. 2000	22 Sept. 2000	Qualified opinion
(Reason for Qualification:	*Inappropriate recognition of a receivable)*		
Western District Health Service	22 Aug. 2000	19 Sept. 2000	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS - *continued*			
Public hospitals *- continued*			
West Gippsland Healthcare Group	18 Sept. 2000	25 Sept. 2000	✓
West Wimmera Health Service	3 Oct. 2000	20 Oct. 2000	✓
Wimmera Health Care Group	19 Oct. 2000	25 Oct. 2000	✓
Wodonga Regional Health Service	18 Aug. 2000	22 Sept. 2000	Qualified opinion
(Reason for Qualification:	*Inappropriate disclosure of non-reciprocal grants)*		
Women's and Children's Health Care Network *(c)*	24 Aug. 2000	22 Sept. 2000	✓
Wonthaggi and District Hospital	6 Sept. 2000	19 Sept. 2000	✓
Yarram and District Health Service	18 Sept. 2000	22 Sept. 2000	✓
Yarrawonga District Hospital	21 Aug. 2000	20 Sept. 2000	✓
Yea and District Memorial Hospital	18 Sept. 2000	20 Sept. 2000	✓
FINANCIAL YEAR ENDED 30 SEPTEMBER 2000			
HEALTH			
Medical Practitioners Board of Victoria	21 Dec. 2000	22 Dec. 2000	✓
FINANCIAL YEAR ENDED 31 DECEMBER 2000			
HEALTH			
Anti-Cancer Council of Victoria	19 Apr. 2001	24 Apr. 2001	Qualified opinion
(Reason for Qualification:	*Limitation of scope)*		
Prince Henry's Institute of Medical Research	13 Mar. 2001	28 Mar. 2001	Qualified opinion
(Reason for Qualification:	*Inappropriate disclosure of non-reciprocal grants)*		
Psychologists Registration Board of Victoria	4 Apr. 2001	4 Apr. 2001	✓
Public Cemeteries -			
Anderson's Creek Cemetery Trust	29 Mar. 2001	30 Mar. 2001	✓
Ballaarat General Cemeteries Trust	6 Apr. 2001	10 Apr. 2001	✓
Bendigo Cemeteries Trust	19 Mar. 2001	2 Apr. 2001	✓
Cheltenham and Regional Cemeteries Trust	2 Mar. 2001	21 Mar, 2001	✓
Geelong Cemeteries Trust	28 Mar. 2001	30 Mar. 2001	✓
Keilor Cemetery Trust	20 Mar. 2001	20 Mar. 2001	✓
Preston Cemetery Trust	7 May 2001	22 May 2001	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS - *continued*			
FINANCIAL YEAR ENDED 31 DECEMBER 2000 - continued			
HEALTH - *continued*			
Trustees of the Fawkner Crematorium and Memorial Park	1 Mar. 2001	16 Mar. 2001	✓
Trustees of the Memorial Park	28 Feb. 2001	13 Mar. 2001	✓
Trustees of the Necropolis Springvale	30 March 2001	3 April 2001	✓
Wyndham Cemeteries Trust	2 April 2001	9 April 2001	✓
OTHER FINANCIAL PERIODS			
HEALTH			
Ambulance Officers Training Centre *(g)* (financial year ended 30 Nov. 1999)	1 Sept. 2000	13 Sept. 2000	✓
Preston Cemetery Trust (financial year ended 31 Dec. 1999)	12 July 2000	20 July 2000	✓
Templestowe Cemetery Trust (financial year ended 31 Dec. 1999)	12 June 2000	12 July 2000	✓
Trustees of the Lilydale Memorial Park and Cemetery (financial year ended 31 Dec. 1999)	18 May 2000	29 May 2000	✓
Wyndham Cemeteries Trust (financial year ended 31 Dec. 1999)	17 April 2000	18 April 2000	✓
PUBLIC HOSPITALS			
Kooweerup Regional Health Service (financial year ended 30 June 1999)	30 June 2000	26 July 2000	✓
Latrobe Regional Hospital (four month period ended 31 October 2000)	5 Mar. 2001	19 Mar. 2001	✓
INCOMPLETED AUDITS			
HEALTH			
Mildura Cemetery Trust	*Audited financial statements yet to be finalised*		
Templestowe Cemetery Trust	*Audited financial statements yet to be finalised*		
Trustees of the Lilydale Memorial Park and Cemetery	*Audited financial statements yet to be finalised*		

(a) From 1 July 2000, entities ceased operations and were combined to form the Dental Practice Board of Victoria.

(b) Central Gippsland Health Service was created following the amalgamation of Central Wellington Health Service and Maffra and District Hospital.

(c) Incorporation of entity cancelled and all property, rights and liabilities transferred to a metropolitan health service as its successor in law.

(d) Moyne Health Services formerly known as Port Fairy Hospital.

(e) South West Health Care was created following the amalgamation of Warrnambool and District Base Hospital and Corangamite Regional Hospital.

(f) Tallangatta Health Service formerly known as Tallangatta Hospital.

(g) Entity ceased operation at reporting date.

Part 3.3

Infrastructure

KEY FINDINGS

Summary of audit results

- Deficiencies in the recognition and valuation of infrastructure assets controlled by local government entities may adversely impact on the effectiveness of their management and may expose ratepayers to unexpected renewal and replacement costs.

  Paras 3.3.12, 3.3.20 to 3.3.25

- In view of the differing risks for municipal councils involved in the creation and operation of entrepreneurial arrangements, such as companies created under section 193 of the *Local Government Act* 1989, including the potential exposure to public funds, the legislative responsibilities and accountability requirements of these arrangements require further clarification.

  Paras 3.3.26 to 3.3.31

Local government performance reporting

- Despite the substantial challenges of implementing performance reporting, the local government sector leads the Victorian public sector in this area. As other elements of the public sector seek to improve their performance reporting practices, the lessons learnt by the local government sector will provide a helpful guide to those that follow the path of comprehensive performance reporting.

  Paras 3.3.35 to 3.3.67

- Performance reporting arrangements within local government have evolved over time, but are fragmented and have had some serious implementation challenges. These arrangements should have strong linkages with key elements of the strategic corporate planning and management framework within the context of the Best Value regime, which may need further reinforcement and clarification to ensure a consistent, coherent and effective framework.

  Paras 3.3.35 to 3.3.67

KEY FINDINGS - *continued*

Local government performance reporting - *continued*

- Public accountability now requires more than just audited financial outcomes and other general information on operations in annual reports. Externally reported performance-based information is an essential obligation of all public sector entities, including local government, to achieve an adequate level of accountability to the community.

  Paras 3.3.64 to 3.3.67

- The value and credibility of performance-based information is seriously diminished if that information is not subjected to a mandatory external audit by my Office, and consequential issue of an audit opinion for inclusion in councils' annual reports. Accordingly, I strongly support the continuation of the current concept of the preparation of an annual performance statement, subject to my audit, by municipal councils. ***Paras 3.3.46 to 3.3.51 and 3.3.64 to 3.3.67***

Property valuations used for rating purposes

- During 2000, all rateable properties were required to be valued for municipal rating and other State taxing purposes. It was the first time that all rateable properties were required to be valued as at the same date. The valuations process was a massive and ambitious undertaking.

  Paras 3.3.68 to 3.3.77

- Contract and time management, together with a shortage of appropriately skilled valuers, emerged as some of the key issues identified during the 2000 valuation process.

  Paras 3.3.83 to 3.3.91, 3.3.109 to 3.3.113 and 3.3.117 to 3.3.121

- Only 42 per cent of councils met the legislative deadline for the conduct of valuations by June 2000. Further, it was not until mid-November that the last valuation report was prepared.

  Paras 3.3.89 to 3.3.96

- The delays in the conduct of the valuations seriously impacted on the ability of both councils and the Valuer-General to verify the valuers' information in a timely fashion and, in a number of instances, resulted in rate notices being issued without sufficient verification of the accuracy of property valuations, including underlying property details. ***Paras 3.3.83 to 3.3.96 and 3.3.117 to 3.3.121***

- The Valuer-General had not prepared, in respect of the 2000 valuation, any certifications under the *Valuation of Land Act* 1960 as to the truth and correctness of any municipality valuations, and the Minister for Environment and Conservation had not declared any municipality valuations pursuant to the Act as being suitable for adoption and able to be used for the intended purpose.

  Paras 3.3.93 to 3.3.99

KEY FINDINGS *- continued*

Property valuations used for rating purposes *- continued*

- As a matter of best practice, and in order to ensure ratepayers have the benefits of independent review and certification of the property valuations which underpin certain municipal rates, it is my opinion that the adoption and use of the 2000 general property valuation by municipal councils prior to the Valuer-General's certification and the Minister's declaration was imprudent. ***Paras 3.3.93 to 3.3.99 and 3.3.117 to 3.3.122***

- It is estimated that some 93 000 rate notices (4 per cent) issued by municipal councils resulted in a query by ratepayers. Approximately 44 000 rate notices have been subject to a supplementary valuation to correct deficiencies in the 2000 valuation process. In addition, some 18 900 rate notices were subject to a formal objection. However, the level of objections varied significantly between municipalities.

  Paras 3.3.103 to 3.3.105

- It will be important that appropriate provision is made in the 2002 valuation strategy to ensure that valuations are not adopted or used by municipal councils and other rating or taxing bodies, such as the State Revenue Office, until the Valuer-General has prepared his certification and the Minister has declared that the valuation is suitable for adoption and can be used for rating purposes.

  Paras 3.3.93 to 3.3.99 and 3.3.117 to 3.3.122

SUMMARY OF AUDIT RESULTS

3.3.1 The Infrastructure portfolio comprises a number of entities including the Department of Infrastructure as the lead agency and local government, as set out in paragraph 3.3.3 of this Report. Key areas of activity within the portfolio include:

- planning, heritage and building policy and operations;
- public transport services and safety regime;
- road development and road use services and safety;
- marine and port policy and safety;
- strategic planning for transport, urban and regional development; and
- local government.

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

3.3.3 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 1999-2000 financial year.

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

Ministerial portfolio	*Entities subject to audit*
Local Government	CityWide Service Solutions Pty Ltd
	Melbourne Wholesale Fish Market Pty Ltd
	Municipal councils (78)
	Prahran Market Pty Ltd
	Regent Management Company Pty Ltd
	Regional library corporations (16) *(a)*
	Queen Victoria Market Pty Ltd
	Streetsahead Cleaning Services (joint venture)
Planning	Architects Registration Board of Victoria
	Building Control Commission
	Heritage Council
	Plumbing Industry Commission
	ULC Real Estate Services Pty Ltd
	Urban Land Corporation
Ports	Marine Board of Victoria
	Hastings Port (Holding) Corporation *(b)*
	Melbourne Port Corporation *(b)*
	Victorian Channels Authority *(b)*
Transport *(c)*	Melbourne City Link Authority
	Roads Corporation
	Public Transport Corporation
	Victorian Rail Track *(b)*

(a) The Board of the Swan Hill Regional Library Corporation resolved on 27 June 2000 that, effective from 30 June 2000, all obligations and entitlements of the Corporation be transferred to the Swan Hill Rural City Council and that the Corporation cease trading as of that date and be wound-up.

(b) These entities are also accountable to the Treasurer (within the Treasury and Finance portfolio).

(c) A new entity, the Spencer Street Station Authority, will be subject to my audit during the 2000-01 financial year. On 31 December 2000, and pursuant to the *Rail Corporations Act* 1996, certain property, rights, employees and liabilities of V/Line Passenger Corporation (a public sector body within the Treasurer's Ministerial Portfolio) were transferred to the new Authority.

Audit opinions issued within Infrastructure portfolio (other than local government)

3.3.4 During the 1999-2000 audit cycle, 14 clear audit opinions were issued on financial statements prepared by portfolio entities other than local government, with one set of financial statements relating to the Melbourne City Link Authority subject to audit qualification.

Accounting for City Link concession fee notes

3.3.5 Under the arrangements established for the development and operation of the Melbourne City Link, concession fee notes (promissory notes) are received by the Melbourne City Link Authority on behalf of the State from Transurban CityLink Limited, in consideration of Transurban's obligation to pay concession fees to the State. These arrangements have been outlined in my previous Reports to the Parliament[1].

3.3.6 The Melbourne City Link Authority reports the concession fee notes (the Notes) as both an asset (that is the value of the Notes which is receivable from Transurban) and a liability (that is the value of the Notes which is payable to the State) in its financial statements. The Notes were included in the Authority's 1999-2000 financial statements at an estimated net present value of $103.3 million, based on a number of assumptions. This valuation was subject to audit qualification as set out below.

3.3.7 One of the key determinates of the estimated net present value of the Notes is the timing of when Transurban will achieve a specified return on equity after tax. Once the specified return on equity after tax has been achieved, the concession fees become payable. One of the key assumptions made by the Authority when calculating the net present value of the Notes was to assume that the Notes will be deductible for income tax purposes by Transurban in the year in which each Note was raised.

3.3.8 We were advised that the Australian Taxation Office has issued a tax assessment to Transurban without the Notes being claimed as a deductible expense and Transurban has lodged a formal objection to the tax assessment. This matter had not been resolved at the time of audit.

3.3.9 Based on the existing Australia Taxation Office assessment and the known position at the time of the 1999-2000 audit, in our opinion an inappropriate assumption had been made by the Authority in respect to the deductibility of the Notes for income tax purposes. Consequently, I issued a qualified audit opinion on the basis that the estimated net present value of the Notes in the Authority's financial statements inappropriately assumed deductibility of the Notes and was, therefore, overstated by $62.7 million.

Audit opinions issued   local government

3.3.10 During the 1999-2000 audit cycle, 83 clear audit opinions were issued on the financial statements prepared by local government entities (94 for 1998-99), and a further 17 subject to audit qualification (5 for 1998-99).

3.3.11 In addition, 70 clear audit opinions were issued on the performance statements prepared by municipal councils (39 for 1998-99); and a further 8 performance statements were subject to audit qualification (39 for 1998-99). Further comment on local government performance reporting is made later in this Report.

[1] *Report of the Auditor-General on the Finances of the State of Victoria, 1999-2000*, November 2000.

3.3.12 Schedule B to this Part of the Report sets out the audit opinions issued in respect of each Portfolio entity for the 1999-2000 financial year. Table 3.3B summarises the nature of each qualified audit opinion issued within the local government sector.

TABLE 3.3B
QUALIFIED AUDIT OPINIONS ISSUED IN LOCAL GOVERNMENT

Name of entity	*Nature of qualified audit opinion*
Darebin City Council, Golden Plains Shire Council, Melton Shire Council, Mornington Peninsula Shire Council, Nillumbik Shire Council, Surf Coast Shire Council, Swan Hill Rural City Council, Towong Shire Council, Whitehorse Manningham Regional Library Corporation, Wodonga Rural City Council.	Uncertainty over the written-down value of certain non-current assets within the financial statements.
Alpine Shire Council, Horsham Rural City Council, Hume Moonee Valley Regional Library Corporation, Indigo Shire Council, Southern Grampians Shire Council, Swan Hill Rural City Council, Wyndham City Council.	Failure to revalue all classes of non-current assets as at 1 January 2000 as required by the *Local Government Act* 1989, for inclusion in the financial statements.
Bass Coast Shire Council, Indigo Shire Council.	Certain infrastructure assets had not been recognised in the financial statements.
Campaspe Shire Council, Colac Otway Shire Council, Glen Eira City Council, Indigo Shire Council, Wangaratta Rural City Council, West Wimmera Shire Council, Wodonga Rural City Council.	The performance statement did not incorporate all of the Business Plan performance measures and targets as required by the *Local Government Act* 1989.
Glenelg Shire Council.	The Council's Business Plan did not identify performance measures and targets for inclusion in the performance statement.

Timeliness of financial reporting within Infrastructure portfolio (other than local government)

3.3.13 The annual reporting and audit requirements for entities within the portfolio other than local government entities are set out in the *Financial Management Act* 1994 and the *Audit Act* 1994. In particular, under section 45 of the *Financial Management Act* 1994, each department and public body must submit its annual financial statements to the Auditor-General within 8 weeks of the end of the financial year. Under the *Audit Act* 1994, the Auditor-General is then required to make a report on the audit of the financial statements within 4 weeks of their receipt. Within 4 months of the end of the financial year, or the next sitting day after the end of the fourth month, the relevant Minister is required under section 46 of the *Financial Management Act* 1994 to table in each House of the Parliament the annual report of each entity, which includes a report of operations and the audited financial statements.

3.3.14 Table 3.3C illustrates the performance of portfolio agencies, other than local government, in meeting the statutory requirement to have audited financial statements completed within 12 weeks of the end of the relevant financial year, during the 1999-2000 reporting cycle.

TABLE 3.3C
TIMELINESS OF FINALISATION OF AUDITED FINANCIAL STATEMENTS, INFRASTRUCTURE PORTFOLIO AGENCIES, (OTHER THAN LOCAL GOVERNMENT)

	Entities	
Number of weeks after end of financial period	*Number*	*Per cent (cumulative)*
Less than 10 weeks	1	7
10 to 12 weeks	5	40
12 to 14 weeks	3	60
14 to 16 weeks	3	80
16 to 18 weeks	3	100

3.3.15 The table demonstrates that there is scope for improvement in the timeliness of audited financial statement completion by portfolio entities (other than local government) with only 40 per cent of entities able to meet the 12 week statutory timeframe.

Timeliness of reporting local government

3.3.16 The annual reporting and audit requirements for local government entities are set out in the *Local Government Act* 1989 and the *Audit Act* 1994. In particular, under section 126 of the *Local Government Act* 1989, each municipal council and regional library corporation must submit its annual report, including a report of operations, audited financial statements and audited performance statement, to the Minister for Local Government within 3 months of the end of each financial year. Under the *Audit Act* 1994, the Auditor-General is required to make a report on the audit of the financial statements within 4 weeks of their receipt.

3.3.17 Table 3.3D illustrates the performance of municipal councils and regional library corporations in meeting the statutory annual reporting requirements by reference to the completion of audited statements within 3 months of the end of the relevant financial year, during the 1999-2000 reporting cycle.

TABLE 3.3D
TIMELINESS OF FINALISATION OF AUDITED FINANCIAL STATEMENTS, MUNICIPAL COUNCILS AND REGIONAL LIBRARY CORPORATIONS

	Entities	
Number of months after end of financial period	*Number*	*Per cent (cumulative)*
Less than and up to 3 months	34	36
3 to 4 months	35	73
4 to 5 months	15	89
5 to 6 months	6	95
6 to 7 months	4	100

3.3.18 The above table demonstrates that there is scope for improvement in the timeliness of completion of annual reports for municipal councils and regional library corporations, with only 36 per cent of those entities completing their statements within the 3 month statutory timeframe. The Minister for Local Government approved, pursuant to the *Local Government Act* 1989, 69 requests from local government entities for an extension to the statutory date for submission of their annual report (46 approved requests for extension – 1998-99). This outcome is reflective of the major issues that arose during the preparation and audit of the 1999-2000 statements of municipal councils and regional library corporations as discussed below.

3.3.19 A number of key issues impacted on the timeliness of the preparation and audit of the 1999-2000 statements within local government, including:

- the modification and/or introduction of new information technology systems by several local government entities, which were in part driven by the GST and Y2K issues;
- the turnover of key accounting and other senior officers, including vacancies of key accounting staff in certain municipalities;
- the introduction of the GST and its application to local government;
- the legislative requirement on municipal councils to revalue all rateable properties within their municipality within the year;
- the conduct of elections in 53 of the State’s 78 municipalities during March 2000; and
- the legislative requirement upon municipal councils and regional library corporations to revalue all non-current assets, including infrastructure assets, during the course of the year.

Asset revaluation

3.3.20 During the 1999-2000 financial year, all municipal councils were required to undertake a valuation of rateable properties within their municipalities for the purposes of setting municipal rates. The requirement to undertake the valuation of rateable properties arose from a determination of the Minister for Environment and Conservation, pursuant to the *Valuation of Land Act* 1960, that all municipal councils are to conduct biennial valuations of all rateable properties commencing 1 January 2000. Further comment on the revaluation of properties for the purposes of setting municipal rates is contained later in this Report.

3.3.21 In addition, Regulation 89 of the *Local Government Regulations* 1990 required municipal councils and regional library corporations to revalue all of their non-current assets at the same date that rateable property valuations are undertaken under the *Valuation of Land Act* 1960. Consequently, all municipal councils and regional library corporations were required under the Regulations to revalue all of their non-current assets as at 1 January 2000 for inclusion in their 1999-2000 financial statements. The non-current assets controlled by municipal councils and libraries as at 30 June 2000 totalled approximately $27 billion.

3.3.22 Key issues identified during the audit of non-current asset revaluations, some of which lead to qualification of the audit opinion issued on the financial statements, included:

- Not all non-current assets were revalued, as required by the Act;
- Substantial adjustments to asset valuations were identified and made during the preparation and audit of several entities' financial statements. These adjustments related to the non-recognition, or the inappropriate recognition of assets in the financial statements or incorrect valuations. The total value of required adjustments made during 1999-2000 amounted to $750 million ($290 million in 1998-99);
- Some entities experienced significant delays in the preparation of their financial statements due to having under-estimated the complexity and extent of work required to revalue all non-current assets; unavailability of appropriately skilled staff to undertake the valuation; and/or poor planning resulting in a late start to the valuation process;
- Some entities failed to properly undertake and account for non-current asset revaluations, including failing to undertake an assessment of the present condition of an asset when determining its written-down replacement cost and had not maintained adequate documentation supporting the revaluation calculations, as required by current professional accounting pronouncements and other authoritative guidance; and
- Several complex issues involved in the valuation and accounting for a revaluation of infrastructure assets (such as roads and drains), heritage and cultural assets (including library and art collections), were highlighted during the audit.

3.3.23 The *Local Government Regulations* 1990 lapsed during April 2001. During March 2001, the Government announced the publication of a Regulatory Impact Statement (RIS) for the Local Government Regulations, containing the proposed *Local Government Regulations* 2001. The new Regulations, dated 10 April 2001, do not contain an equivalent requirement to the current Regulation 89, which required municipal councils and regional library corporations to revalue all of their non-current assets at the same date that rateable property valuations are undertaken under the *Valuation of Land Act* 1960. However, the Australia Accounting Standards currently require entities that record their non-current assets at valuation to regularly revalue these assets.

3.3.24 My June 2000 *Report on Ministerial Portfolios* commented that in *"… May 1999, the Local Government Division of the Department of Infrastructure advised my Office that steps would be taken during 1999 to develop best practice guidelines for infrastructure asset accounting for municipalities. Additionally, following consultation with councils on the findings of the Government's Study of Local Government Infrastructure, the Local Government Division will recommend to Minister strategies to improve infrastructure management in councils"*. At the date of preparation of this Report, best practice guidelines had not been issued. I understand, however, that the Department intends to create an industry-based working party to investigate these matters.

3.3.25 **I reiterate my previously expressed view that deficiencies in recognition and valuation practices for infrastructure assets may adversely impact on the effectiveness of their management and may expose ratepayers to unexpected renewal and replacement costs. Councils, therefore, need to ensure that asset registers for infrastructure holdings are complete and accurate to ensure the effective management of these significant resources.**

Accountability framework for local government companies

3.3.26 Section 193 of the *Local Government Act* 1989 governs the formation of companies and other entrepreneurial arrangements by municipal councils. The Act provides that the accounts and records of a company formed under that section are to be subject to audit under Part 6 of the Act as if they were the accounts and records of the council. Part 6 of the Act deals with the annual accounts (financial statements) and the audit of municipal councils.

3.3.27 In prior years, it was understood companies formed by municipal councils had a legislative requirement to publicly report arising from section 193 of the Act and to be subject to audit by my Office. However, one local government company tested this requirement during the 1999-2000 audit cycle. That company obtained written legal advice that *"… section 193(11) does not require [the Company's] accounts to be kept in the manner prescribed by Part 6. Rather, it requires those accounts … to be audited in the way prescribed by Part 6"*. The legal advice also acknowledged that *"… while the principle that only those provisions of Part 6 relating to audit and inspection apply to [the Company] is easy to state, it is less easy to unravel the provisions of Part 6 and to conclude precisely which provisions apply and which do not*".

3.3.28 This legal advice suggests that companies and other entrepreneurial arrangements formed by municipal councils under section 193 of the Act do not have any external reporting obligations under that Act unless one or both of the relevant Ministers create an expressed external reporting obligation as part of the approval to create the relevant company or other arrangement under the Act.

3.3.29 While some companies will have certain external reporting obligations arising from the Corporations Law, some companies or other entrepreneurial arrangements established under section 193 will not be required to externally report under that legislation.

3.3.30 **In view of the differing risks for municipal councils involved in the creation and operation of entrepreneurial arrangements, such as companies created under section 193 of the Act, including the potential exposure to public funds, the legislative responsibilities and accountability requirements of section 193 entrepreneurial arrangements require further clarification.**

3.3.31 The Local Government Division of the Department of Infrastructure is currently reviewing the scope and operation of section 193 of the Act and a related discussion paper was released late last year for comment by municipal councils.

Accounting for rail infrastructure assets

3.3.32 Victorian Rail Track's (VicTrack) financial statements include certain rail track and associated infrastructure assets which are leased by VicTrack to the Director of Public Transport (Department of Infrastructure). The Director of Public Transport, in turn, leases these assets to the various transport franchisees. These arrangements were outlined in my June 2000 *Report on Ministerial Portfolios.*

3.3.33 Under the lease agreement between VicTrack and the Director of Public Transport, all improvements to those assets vest and remain with the Director of Public Transport. During 1999-2000, track improvements to the value of $13.1 million were treated by the Director of Public Transport as an asset in the financial statements of the Department of Infrastructure.

3.3.34 It is my opinion that this asset expenditure, comprising improvements to the leased assets, are integral to the transport network and should be accounted for together with the entire transport network by one public sector reporting entity rather than being split between VicTrack and the Department. This matter is under consideration by the relevant entities within the Portfolio.

RESPONSE *provided by the Chief Executive Officer, Melbourne City Link Authority*

Accounting for City Link concession fee notes

As in previous years, in the preparation of its financial statements, the Authority has adopted certain assumptions with respect to estimating the value of concession notes for accounting purposes.

One of the variables affecting the value, in the current financial year and prior financial years, is the income tax treatment of the concession notes by Transurban and in particular, whether they are deductible for income tax purposes in the year in which each concession note is issued.

On 24 August 1999, Transurban announced to the Australian Stock Exchange that it had been unable to reach agreement with the Australian Taxation Office (ATO) as to the tax deductibility of the concession notes for income tax purposes. An assessment was issued by the ATO and Transurban has subsequently lodged a formal objection. The objection has not been resolved and the matter is yet to be determined by agreement or by the courts.

In the preparation and presentation of the financial statements for the year ended 30 June 2000, the value of the concession notes was estimated based on the assumption that Transurban will be successful in its dispute. As in prior financial years, this view is largely based on the fact that Transurban has obtained advice from Senior Council to the effect that the concession notes are deductible, the treatment of the concession notes in the financial statements of Transurban, and discussions with representatives of Transurban.

Full disclosure has been made by way of note to the financial statements (refer Note 12) as to the method of estimating the value of the concession notes, the existence and status of Transurban's dispute concerning the deductibility of the concession notes, and the possible financial effect on the financial statements of the Authority should Transurban be unsuccessful in its objection. This approach is consistent with that adopted in the prior financial year and was accepted by the Auditor-General.

In the view of the Authority, there is no further relevant information available today as to the likely outcome of Transurban's dispute than was available to the Auditor-General when the audit report was issued in relation to the prior financial year.

It is, therefore, a matter of regret that the Auditor-General has issued a qualified audit opinion on the financial statements of the Melbourne City Link Authority for the financial year ended 30 June 2000.

It is important to note that the difference in view between the Authority and the Auditor-General as to the value of the concession notes has no net impact on either the balance sheet or the revenue and expenditure statement of the Authority.

The issue of difference relates to a difference of view about the estimate of the value of an item, which is both an asset and a liability.

RESPONSE *provided by the Secretary, Department of Infrastructure*

Timeliness of reporting – local government

It should be emphasised that a major issue in terms of the performance of municipal councils with respect to the timeliness of their annual reports was the legislative requirements placed on councils to revalue all rateable properties and non-current assets within a very short period of time.

Asset revaluation

The issues of asset valuation, asset classification and reporting are subjects embodied under the Local Governments Division's emphasis on improved infrastructure asset management.

The Division has established the Asset Management Reference Group which will consider the topic. The Reference Group's objectives are as follows:

- *improved asset management culture throughout local government;*
- *sound asset management practices in the local government sector; and*
- *capacity to demonstrate the improvements made in asset management in the sector.*

The Reference Group is to be comprised of representatives from the sector peak bodies, VicRoads, Department of Treasury and Finance and will also include representation from the Victorian Auditor-General's Office.

The Reference Group is to have its first meeting in May 2001 and report to the Executive Director of the Local Government Division in December 2001. The sector as a whole will also have an opportunity to comment on the Reference Group's recommendations.

Accountability framework for local government companies

Section 193(11) of the Local Government Act requires the accounts of a company or undertaking approved under section 193 to be subject to audit as provided for local councils.

The legal opinion audit refers to did not dispute this requirement for audit – it referred solely to the form in which the company keeps its accounts. The company concerned has chosen to keep its accounts in a form required under Corporations Law, rather than normal local government practice. Local Government Division does not see that this affects the reporting requirements on section 193 entities – their accounts are still subject to audit in the usual way.

Audit also raises the issue of external reporting requirements, and expresses concern that some companies may not have such external reporting. The Local Government Division takes the view that the primary reporting for any local government entity is to its host council (or councils). Many section 193 approvals also require the entity to make regular reports to the Local Government Division on progress. These reports enable the Minister to note any problems – and to raise them with the council concerned. It is the responsibility of the council to decide what, if any, action is required.

Accounting for rail infrastructure assets

The Department has commenced a project to review transport infrastructure asset responsibilities between VicTrack and the Department. This review will take a strategic perspective to ensure that government objectives in relation to public transport service delivery are met.

LOCAL GOVERNMENT PERFORMANCE REPORTING

3.3.35 Since 1996, our Reports to the Parliament have commented on the external performance reporting arrangements operating within local government.

3.3.36 The existing external performance reporting arrangements within local government are evolving and are currently under review by the Department. The Department is being assisted in this task by a Committee, which comprises key industry representatives, whose role is to act as a facilitator and conduit of information on local government performance indicators.

3.3.37 Concurrently, the Department is planning to update the *Local Government Act* 1989 so that it:

- is logically structured, succinct and in plain English;
- corrects anomalies in the existing Act; and
- reflects the Government's partnership approach to local government.

3.3.38 The legislative provisions related to corporate planning and performance reporting arrangements are being considered as part of this update process. It is anticipated by the Department that the new legislation will be presented to the Parliament in the autumn session of 2002, at the conclusion of a wider consultation process.

3.3.39 The external performance reporting arrangements, which are a key component of the broader strategic corporate planning and management framework for local government, currently comprises 4 key elements as follows:

- publication of an audited performance statement in municipal council annual reports, including both actual and targeted results for the annual business plan performance measures, as required by the *Local Government Act* 1989;
- inclusion of other performance-related information in the annual report of municipal councils as required by the *Local Government Regulations* 2001, such as audited financial ratios and budget information;
- inclusion of unaudited "Best Value" performance indicators and actual results in municipal council annual reports, as required by the Ministerial Code issued pursuant to the *Local Government Act* 1989; and
- the inclusion of Statewide performance indicators in annual reports of municipal councils, from 1 July 2001 onward, as required by the Minister.

3.3.40 Key observations, related to the above 4 key elements of the existing external performance reporting arrangements within local government are set out later in this Report.

Audited performance statement

3.3.41 Most Victorian public sector agencies include some form of performance reporting in their annual reports as part of the accountability process. However, the Victorian local government sector is unique in that municipal councils are required, under the legislation, to prepare a performance statement for inclusion in their annual report which is required to be subject to audit by the Auditor-General.

3.3.42 Under the *Local Government Act* 1989, the performance statement must:

- outline the annual business plan performance targets and measures; and
- describe the extent to which the business plan was met in that year having regard to those targets and measures.

3.3.43 The introduction of an audited performance statement in the local government sector in the 1998-99 financial year was not surprisingly without problems with half of the performance statements receiving a qualified audit report. The key qualification issues related to:

- not all business plan performance measures and targets were included in the performance statement (24 instances);
- an annual business plan and related performance measures and targets had not been prepared (12 instances); and
- sufficient and appropriate records did not exist to support actual results included in the performance statement for certain performance measures (3 instances).

3.3.44 These issues arose despite the following comments made in our May 1998 *Report on Ministerial Portfolios:*

> *"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."*

3.3.45 While in certain key respects, the second audit round of municipal council performance statements produced significantly more favourable results (8 qualified audit opinions issued compared with 39 in the previous year), significant concerns continue over the effectiveness of performance statements at this early stage in their implementation including:

- concerns over the relevance, appropriateness and excessive number of business plan performance measures adopted by municipal councils; and
- deficiencies in municipal council business plans and corporate plans when compared with the requirements of the Act.

Audit approach to the audit of performance statements

3.3.46 My Office has adopted a limited scope audit for the purposes of forming an opinion on performance statements, during the first 2 audit cycles.

3.3.47 The audit opinion issued by the Auditor-General on municipal council performance statement indicates whether the performance statements were presented fairly in accordance with the requirements of the *Local Government Act* 1989 and states that the audit did not extend to an assessment of the relevance or appropriateness of the performance measures contained within the performance statements.

3.3.48 The above approach was adopted to allow the local government performance statement regime to sufficiently mature to the point where consideration of extending the audit scope to include the relevance and appropriateness of performance measures was deemed appropriate. Any observations in connection with the relevance and appropriateness of performance measures, identified during the course of the audit, are however referred in reports to municipal councils.

3.3.49 During the 1999-2000 audit cycle, a significant number of councils had taken action to enable the removal of prior year audit qualifications by ensuring that the performance statements contained the same performance measures as set out in their annual business plans, as required by the Act. Most municipal councils achieved this outcome by adopting a set of performance measures recommended by the Department during the early stages of the implementation of the performance statement regime.

3.3.50 The Department's recommended performance measures have the advantage that actual results achieved are generally capable of being verified, but in most instances are not the most relevant or appropriate in the context of the respective municipal council's business plan and corporate plan strategies and objectives. In some instances, councils simply listed the Department's recommended performance measures and targets in their business plan. They therefore did not set out, as required by the Act, the activities that council intends to pursue over the year under consideration. Consequently, the usefulness of performance statements, to inform readers of the annual reports of councils about the extent to which they have met their business plan objectives, a key requirement of the Act, is seriously impaired. Accordingly, the identification of relevant and appropriate performance measures remains a key challenge for the sector.

3.3.51 **Despite the substantial implementation challenges, I strongly support the inclusion of an audited performance statement in municipal council annual reports. The local government sector leads the Victorian public sector in this area. As other elements of the public sector seek to improve their performance reporting practices, the lessons learnt by the local government sector will provide a helpful guide to those that follow the path of comprehensive performance reporting.**

Financial ratios and budget information

3.3.52 Under the *Local Government Regulations* 2001, municipal councils are required to include the following performance-related information in their annual reports:

- the actual results for 3 financial years for 5 financial ratios;
- budgeted revenues and expenses compared with actual revenues and expenses; and
- a statement which reviews the performance of the council against the council's corporate and business plans, including comment on legislative, economic or other factors which have had an impact on the council's performance.

Best Value Victoria

3.3.53 The *Local Government (Best Value Principles) Act* 1999 introduced a Best Value regime for the delivery of services by the local government sector. The regime, known as "Best Value Victoria", is intended by the Government to act as a tool for change within the sector and creates additional external performance reporting obligations for municipal councils.

3.3.54 The Act sets out the following Best Value principles:

- all services provided by a council must meet quality and cost standards it has developed;
- all services provided by a council must be responsive to the needs of its community;
- each service provided by a council must be accessible to those members of the community for whom the service is intended;
- a council must achieve continuous improvement in the provision of services for its community;

- a council must develop a program of regular consultation with its community in relation to the services it provides; and
- a council must report regularly to its community on its achievements in relation to the principles set out above.

3.3.55 Further, the Act states that in applying the Best Value principles, councils may take into account, among other factors:

- the need to review services against the best on offer in both the public and private sectors;
- an assessment of value for money in service delivery;
- community expectations and values;
- the balance of affordability and accessibility of services to the community;
- opportunities for local employment growth or retention;
- the value of potential partnerships with other councils, and the State and Commonwealth Governments; and
- potential environmental advantages for the council's municipal district.

3.3.56 Under the Act, municipal councils must have developed a program for the application of Best Value by 31 December 2000 and ensure the Best Value principles are applied to all services by December 2005.

3.3.57 The Act also provides for the Minister to publish codes and guidelines in relation to how municipal councils are to give effect to the Best Value principles. The Minister has published 2 such codes pursuant to the Act: one relating to the Best Value Program and the other relating to reporting by municipal councils on the application of the Best Value principles.

3.3.58 Under the Ministerial Code on Reporting, commencing 2000-01, councils must report to the community at least once a year on what they have done to give effect to the Best Value principles. Such a report may be included as part of the report of operations in council’s annual reports or, alternatively, if the report of operations in the annual report contains a summary relating to Best Value activities a separate report may be published.

3.3.59 The information to be reported to the community at least annually, under the Ministerial Code, includes:

- progress made by the respective council in conducting the Best Value reviews scheduled for the relevant year in the council's Best Value program; and
- the council's application of the Best Value principles to the services for which it has completed reviews.

3.3.60 In addition, as Best Value reviews are completed, councils must include in their reports in respect of each reviewed service, the key quality and cost standards developed by the council in accordance with the Act, including:

- performance indicators for the key quality and cost standards;
- actual performance against the performance improvement target set for the year;
- trends in performance compared with standards and targets for the previous year or years;
- an explanation for any differences between targeted and actual performance, where appropriate;
- an outline of strategies proposed to improve performance, where appropriate;
- how certain factors listed in the Act were taken into account in developing the quality and cost standards; and
- what resources and arrangements apply for service delivery, where appropriate.

3.3.61 Thus, the Best Value initiative has introduced a further external performance reporting obligation for municipal councils, which is in addition to the performance statement and other performance related information required by the Regulations.

Statewide performance indicators

3.3.62 Since the 1997-98 financial year, municipal councils have provided the Department, on an annual basis, performance information for 76 prescribed performance indicators. This information is collated by the Department and made available to municipal councils as a means of facilitating best practice and encouraging performance benchmarking across like groups of councils.

3.3.63 In response to concerns expressed by the sector associated with the large number of performance indicators and their relevance and appropriateness, and in recognition of the Best Value reporting requirements, the Department has commenced work to develop, with the assistance of an industry-based reference group and in consultation with the sector, a small number of high level performance indicators to facilitate the State Government, the community and local government sector monitoring the "health" of the sector. These performance indicators, which replace the previous indicators, fall within 5 categories, with a total of 7 performance indicators already promulgated by the Department for inclusion in municipal council annual reports. Further performance indicators for 2 of the categories are currently under development with the Department's intention that they will be finalised in time for municipal councils to report, for the first time, on all of the Statewide performance indicators in their annual reports for the 2001-02 financial year.

Overall comment

3.3.64 **The existing external performance reporting arrangements within local government, including annual reporting by councils to their communities, includes the performance statement, performance-related information, reporting on Best Value and Statewide performance indicators.**

3.3.65 **Performance reporting has evolved over time, but is fragmented and has had some serious implementation challenges. I believe these arrangements will require some rationalisation as part of the overall local government planning, management and public accountability framework.**

3.3.66 **Public accountability now requires more than just audited financial outcomes and other general information on operations in annual reports. Externally reported performance-based information is an essential obligation of all public sector entities, including local government, to achieve an adequate level of accountability to the community. The value and credibility of such information is seriously diminished if that information is not subjected to a mandatory external audit by my Office, and consequential issue of an audit opinion for inclusion in councils' annual reports. Consequently, I strongly support the continuation of the current concept of the preparation of an annual performance statement, subject to my audit, by municipal councils and its subsequent reporting as part of the annual accountability reporting arrangements to the community by the council.**

3.3.67 **The external performance reporting arrangements are a key element of the strategic corporate planning and management framework and should not be considered in isolation. Consequently, the establishment of strong linkages between key elements of the strategic corporate planning and management framework under the Act, which includes the corporate plan, the 3 year financial plan, the annual business plan, the annual budget and the annual report (including performance-based information), within the context of Best Value regime, may need further reinforcement and clarification to ensure a consistent, coherent and effective framework. We understand these matters are under consideration as part of the current update of the *Local Government Act* 1989.**

RESPONSE *provided by the Secretary, Department of Infrastructure*

I share your belief in the value of performance reporting an as essential obligation for all public sector entities to ensure an adequate level of accountability to the community. Through the work of the Local Government Division, this Department has been active in promoting a number of initiatives to the local government sector to raise awareness and the standards of performance reporting by councils. The most significant of these are the Victorian Local Government Indicators and Best Value reporting.

The Victorian Local Government Indicators comprise a number of Statewide indicators designed to provide an overview of the health of the sector. A much larger number of comparative indicators, some 47 in all, enable councils to benchmark services between groups of like councils. Many of the indicators draw on the results of the annual Community Satisfaction Measurement Program, now in its fourth year. Representative sampling of some 30 000 members of the community produces a core measure of how individual councils are performing in the eyes of those most affected by, and interested in, the councils' performance.

Despite the fact that neither the Victorian Local Government Indicators nor the Community Satisfaction Measurement Program are prescribed in legislation, councils have supported both measures strongly. Many publish the annual community satisfaction results in their local newspapers although there is no requirement that they do so and the results are, in fact, supplied to them in confidence for their own use only.

RESPONSE *provided by the Secretary, Department of Infrastructure - continued*

The acceptance that these measures has attained is itself an indication of the growth of a culture of performance management and accountability in the sector. It will be further supported by the implementation of Best Value Victoria.

The Code of Best Value Reporting gazetted by the Minister for Local Government in November 2000 is mandatory - under section 208H of the Local Government Act 1989 - and requires a council to report, in respect of each service subjected to a Best Value review, on its performance against key quality and cost standards. The Code requirements are comprehensive and should result in each council giving its community a clear picture of its performance, progressively across the full range of services, by the end of the financial year 2005-06.

The Best Value program for service review and ongoing improvements must be incorporated into a council's normal corporate and business planning cycles, commencing with the corporate plan due by 30 June 2001. Accountability must then be reflected in the annual report in the "Best Value report" as part of the report of operations. Councils' Best Value reports will be studied by the Local Government Best Value Commission and the results returned to the sector to further improve performance reporting year-by-year.

While the report of operations is not audited, councils are nevertheless expected to report in a credible and reliable manner on their operations using annual (business) plan and Best Value indicators and measures. In other words, to use measures which are "auditable".

These developments are generally accepted as being in the direction that local government ought to head. The performance statement prescribed under section 153 of the Act has had the contrary effect, diverting councils back into a culture of compliance over recent years. As a result of this experience, the performance statement has acquired a poor "image" and its acceptance and usefulness into the future must now be regarded as problematic.

The update of the Local Government Act firmly addresses the issues you raise, namely, "the establishment of strong linkages between key elements of the strategic corporate planning and management framework under the Act". Furthermore, the Local Government Act update does address the issue of performance indicators being "auditable" and subject to independent scrutiny. However, whether this is done through mandatory external auditing by the Victorian Auditor-General's Office or by some other means is an issue that must be debated in the sector if the culture of performance management is to be progressed.

The work being done with the Local Government Act update, and the intention to provide best practice guidelines and training will, I believe, embed a culture of performance management and reporting. I strongly believe that this approach, reflected in the consultation paper for the Act update, will support the effective development of a performance management culture, owned by the sector.

PROPERTY VALUATIONS USED FOR RATING PURPOSES

3.3.68 Land Victoria, a division of the Department of Natural Resources and Environment, initiated a major review of procedures for undertaking property valuations for municipal rating purposes during 1996 and 1997. A key outcome of the Review was a new code of practice for property valuations known as *Valuation Best Practice*.

3.3.69 The new code of practice provides for a uniform approach to the collection of property data for valuations, including the specification of mandatory data fields to be collected when undertaking property valuations, and standard contracts for the engagement of valuers by municipal councils. A key intended outcome from the implementation of the new code is the preparation of high quality valuation data in a consistent format, for the State and municipal councils.

3.3.70 As part of the new code, councils are to conduct biennial property valuations enabling a Statewide picture of property values to be produced every 2 years. This property information is to assist strategic modelling and planning, and rate setting by municipal councils. This information would also satisfy the needs of other users, such as the State Revenue Office for land tax purposes.

3.3.71 The new code required valuers to inspect every property when undertaking valuations during 2000 and record up to 40 data elements or property details, as applicable. These details were designed to satisfy the needs of all the various users of the valuation information. The new code recommended that the valuation information be collected and stored electronically.

3.3.72 As recommended by the review undertaken by Land Victoria, an amendment was made in 1998 to the *Valuation of Land Act* 1960 to require all municipal councils to have undertaken a general valuation of all rateable properties after 1 January 2000, but before 30 June 2000. The amended Act also requires further valuations to be conducted every 2 years. The then Minister for Environment and Conservation subsequently determined, pursuant to the Act, that the valuation undertaken during 2000 was to be made as at 1 January 2000.

3.3.73 As a result of the above, all rateable properties, for municipal rating purposes, were required to be valued as at the same date for the first time, that is 1 January 2000. Prior to that date, most councils had property valuations for rating purposes between 5 to 9 years old while one council performed valuations on an annual basis.

Municipal rating processes

3.3.74 Municipal rates continue to be a major source of revenue for councils. Under the *Local Government Act* 1989, municipal councils must declare, by 31 August each year, the amount which the Council intends to raise by rates and charges. In addition, councils must declare whether the general rates revenue will be raised by the application of:

- a uniform rate;
- differential rates; or
- urban farm rates, farm rates or residential use rates.

3.3.75 Where a council declares that general rates will be raised by the application of a uniform rate, it must specify the percentage that will be applied against the value of the property to arrive at the general rate.

3.3.76 Under the Act, municipal councils can use one of 3 methods of valuing rateable properties for the purposes of setting rates, namely, site value, capital improved value (that is, the value of the land and any capital improvements, such as a house located on the land) or the net annual value (which, for example, is a set percentage of the capital improved value for residential and rural properties). The majority of councils base their rates on the capital improved value, with 6 councils utilising the net annual value method and only 2 metropolitan councils using the site value method.

3.3.77 Consequently, municipal councils determine the total amount to be raised by rates and charges and allocate that sum across ratepayers by determining the types of rates and charges to be used and the method of property valuation, depending on the types of rates to be raised. It should be noted that one consequence of this approach is that an increase in the valuation of a property may not necessarily result in an increase in municipal rates on that property.

Overview of the results of the valuations undertaken in 2000

3.3.78 The key outcome of the valuations undertaken during 2000, based on information collated by the Valuer-General, was:

- most residential properties in metropolitan areas have generally increased in value at a greater rate than non-residential properties, in particular several metropolitan areas had increases ranging between 50 to 200 per cent;
- residential values in regional centres have increased, some significantly, while non-residential property has remained stable or fallen in value;
- property values in some regional tourist destinations have increased significantly;
- residences with coast or bay views have increased dramatically in value; and
- values of grazing property have, generally, remained stable while the value of cropping land has generally increased.

Roles of the key participants in the valuation process

3.3.79 Key participants in the valuation process are the councils, the Valuer-General and the valuers (which may be independent contractors or council staff, however, the majority were independent contractors).

3.3.80 The functions of the Valuer-General under the Act are:

- to collect and collate such evidence as he thinks necessary or desirable to assist valuers in the making of valuations;
- to make available to valuers any evidence that may be of assistance in the making of valuations; and
- to investigate and report to the Minister for Environment and Conservation on any matter he considers likely to improve the standard of valuing in Victoria.

3.3.81 Chart 3.3E overviews the responsibilities of the key participants in the conduct of a general valuation of properties for municipal rating purposes.

CHART 3.3E
OVERVIEW OF THE RESPONSIBILITIES OF THE KEY PARTICIPANTS IN A GENERAL PROPERTY VALUATION *(a)*

Valuer-General	Council	Valuer
• Sets valuation best practice and supervises and assists valuers. • Reviews valuation reports, issues certificates of satisfactory valuation to councils and certifies valuations as true and correct. (The Minister can, in turn, declare the valuation suitable for adoption.)	• Contracts with Valuer and manages contract, including timeliness of valuation. • Verifies valuation data prepared by valuers. • Requests certificates of satisfactory valuation from the Valuer-General. • Pays valuers and issues rate notices.	• Collects and verifies property details. • Undertakes property valuation. • Provides evidence of work undertaken for which payment is sought from councils. • Forwards valuation report to Valuer-General.

(a) Based on the requirements of the *Valuation of Land Act* 1960 and *Valuation Best Practice* promulgated by Land Victoria.

3.3.82 A council must not, under the Act, pay any valuer who is not a full-time member of the council's staff for any work in respect of a general valuation unless the Valuer-General has issued a certificate of satisfactory valuation or valuation progress in respect of the valuation work. The Act, nevertheless, provides that a council may make such a payment if it notifies the Valuer-General in writing that it intends to do so and the Valuer-General fails to give the council, within 30 days after the notification, either:

- a certificate of satisfactory valuation or valuation progress; or
- a written notice setting out the matters that need to be rectified before he or she will issue such a certificate.

Supervision and management of the valuation process

3.3.83 Chart 3.3E, summarises the different responsibilities of the Valuer-General and councils for the conduct of valuations. My Office’s survey of all municipal councils identified a number of issues in connection with the supervision and management of the 2000 property valuation process. Some of these issues appear to stem from some apparent misunderstandings over the responsibilities of the Valuer-General and councils within the existing framework. It is acknowledged, however, that the conduct of a Statewide property valuation program for the first time using a common framework represented a significant challenge for councils, valuers and the Valuer-General.

3.3.84 Nevertheless, 2 of the key issues that arose during the review concerned who had primary responsibility for monitoring the timeliness of the conduct of the valuation by valuers and verifying or checking the valuation results, and in particular checking the underlying property data and details, prior to the issue of rate notices.

3.3.85 **Many councils responded to my Office’s survey that they had relied on the Valuer-General to monitor the timeliness and results of the valuation, and had not conducted any checks, or had only undertaken limited checking procedures prior to the issue of rate notices due to:**

- **delays in the preparation of the valuation, which had meant that sufficient time was not available for councils to undertake adequate verification work within the legislative deadlines; and/or**
- **councils had relied on their contracted valuers to undertake sufficient quality control procedures together with the supervision of the valuers’ work by the Valuer-General.**

3.3.86 In a number of councils where delays occurred in the valuation process, the councils indicated their belief that supervision of the valuers' progress was the responsibility of the Valuer-General. However, the code of practice (*Valuation Best Practice*) places the responsibility with council to manage the timeliness of the completion of the valuation by their valuer and it is council who has a legal obligation under the *Valuation of Land Act* 1960 to undertake the valuation, not the Valuer-General. Audit was advised that the Valuer-General reported on the status of the valuation exercise to the relevant council every month.

3.3.87 **The delays in the conduct of the valuation, as outlined later in this Report, seriously impacted on the ability of both councils and the Valuer-General to verify the valuers' information in a timely fashion and in a number of instances resulted in rate notices being issued without sufficient verification of the accuracy of property valuations, including underlying property details. Consequently, not all errors were corrected prior to the issue of rate notices and substantial ratepayer concerns resulted from the valuation process.**

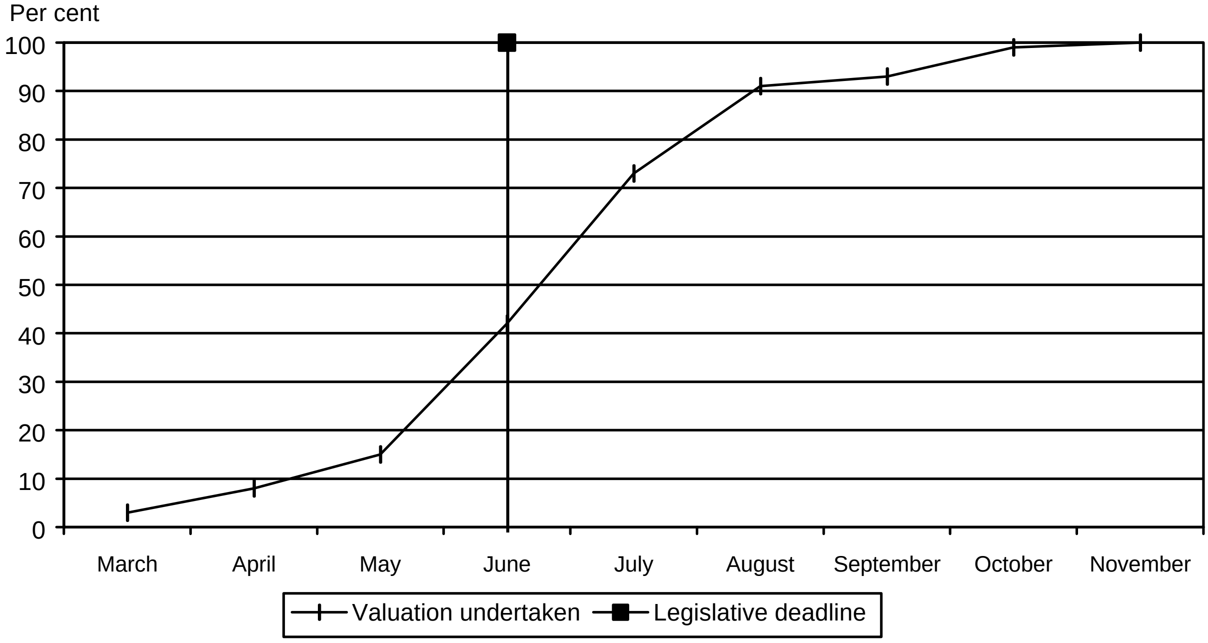
3.3.88 The code of practice covering the valuations undertaken during 2000 provided that the completion dates for each stage of the valuation process should be determined by the contracted valuer within 30 days of the acceptance of the contract, subject to the approval of councils. However, the Valuer-General has prepared more detailed guidelines for the next round of valuations which aims to better define the relationship between councils, valuers and the Valuer-General by including greater specification of the tasks required to be undertaken during each stage of the valuation. Further, these guidelines also include recommended completion dates for each stage of the valuation process within the recommended proforma contract with valuers.

Timeliness of the valuations undertaken in 2000

3.3.89 The *Valuation of Land Act* 1960 required municipal councils to have undertaken the 2000 valuations by 30 June 2000. The valuation timetable under the Act significantly shortened the period of time between the effective date of the valuation and the date by which the valuer was to have prepared his report to council from some 27 months (general valuation for metropolitan councils undertaken in 1996) to 6 months (general valuation for all councils in 2000).

3.3.90 Chart 3.3F, sets out the timeliness of the conduct of valuations undertaken in 2000, based on the date of preparation of the valuation report by the valuer, compared with the legislative deadline.

CHART 3.3F
TIMELINESS OF THE VALUATIONS UNDERTAKEN DURING 2000 *(a)*



(a) Based on the legislative deadline of 30 June 2000 and the date the valuation report was provided to council by the valuer (that is the "return" date as recorded by the Valuer-General).

3.3.91 Chart 3.3F highlights that only 42 per cent of councils met the legislative deadline for the conduct of valuations. Further, it was not until mid-November that the last valuation report was prepared.

Finalisation of the valuation process

3.3.92 While this analysis sets out the extent of delay in meeting the legislative deadline for the preparation of the valuation report, it does not reflect the full extent of delays leading up to the finalisation of the valuation process.

3.3.93 The *Valuation of Land Act* 1960 requires that the valuer's report be presented to the Valuer-General for his determination as to whether it is generally true and correct. The Valuer-General, once satisfied with the valuation, can make a certification to this effect to the Minister for Environment and Conservation who may then make a declaration under the Act that the valuation is suitable to be adopted and used for the intended purpose. The Act provides certain responsibilities and powers to the Valuer-General in the event that a general valuation, or a part or parts of a valuation are found not to be generally true and correct. In addition, during the preparation of the valuation, the Valuer-General can issue certifications of satisfactory valuation or valuation progress in respect of a valuation or parts of a valuation under the Act to enable councils to pay contracted valuers.

3.3.94 **Audit was advised by the Valuer-General's Office during the preparation of this Report, that a certification of satisfactory valuation or valuation progress for the final stages of the valuations undertaken during 2000 had not been issued at that time in respect of approximately 26 out of a total of 78 municipalities. Audit was further advised that there was concern over the ability of a number of municipalities to achieve a final certification of satisfactory valuation given inadequacies in supporting evidence for the relevant valuations and that at least 5 of those municipalities had terminated their contract with their valuers.**

3.3.95 **Further, our audit disclosed that the Valuer-General had not prepared, in respect of the 2000 valuation, any certifications under the Act as to the truth and correctness of any municipality valuations, and that the Minister for Environment and Conservation had not declared any municipality valuations pursuant to the Act as being suitable for adoption and able to be used for the intended purpose.**

3.3.96 Nevertheless, municipalities have used the valuations undertaken during 2000 for rating purposes by issuing rate notices and have made the related declarations under the *Local Government Act* 1989.

3.3.97 I have sought legal advice from the Victorian Government Solicitor on the impact of the absence of the Valuer-General's certification and the Minister's declaration, pursuant to section 7 of the *Valuation of Land Act* 1960, on the validity and legality of the rate notices issued by councils during 2000. That advice concluded that:

> *"Even if s7 of the Act [Valuation of Land Act 1960] provided for a regime which had to be completed before a rate could be struck on the basis of the valuation, assuming that a valuation was in fact true and correct, and the Valuer-General had declared it as such even after a rate was set, it is my view that it would more likely than not be upheld as a valid rate and would not be struck down on the basis that such certification or declaration was not made at that time. It is probable that a court, taking an outcomes based approach when asked to consider the issue, would find the provisions of s7 procedural or directory rather than mandatory vis a vis the striking of rates and therefore find that there had been substantive compliance with such provisions, because of the inconvenience which it would cause to hold otherwise. A court would be heartened by the fact that there are other remedies available to ratepayers to object to a valuation and to challenge a rate set on that basis.*
>
> *This is not to say that, if a rate has been set on the basis of a valuation which has not been subject to the supervision of the Valuer General as provided by the Act, it might not be challenged on an administrative law review ground, for example on the basis that a relevant consideration has not been taken into account (eg. that the valuation had not been certified true and correct).*
>
> *Ultimately however, neither the LGA [Local Government Act 1989] nor the Act mandate or prohibit council or other rating authorities setting rates based on valuations which have not achieved s7 certification…*

The second reading speeches to the Act and subsequent amending Acts indicate Parliament's intention to avoid going as far as to dictate that councils (and probably other rating authorities) can only set rates based upon valuations in respect of which the generally true and correct process had been strictly adhered to. Therefore, although it might be considered to be imprudent of council (or another rating authority) to base its rates on a valuation which was not declared to be generally true and correct I do not consider that it was Parliament's intention to go as far as prohibiting it from doing so. …"

3.3.98 The legal advice also observes that:

"… At the end of the day however, failure to achieve a s7 certification or declaration does not undermine the rates that are set in accordance with them although it may have a negative impact on their credibility and the rating authority setting them and may thus make them more susceptible to challenge. …"

3.3.99 **As a matter of best practice and in order to ensure ratepayers have the benefits of independent review and certification of the property valuations which underpin certain municipal rates, it is my opinion that the adoption and use of a general valuation by municipal councils prior to the Valuer-General's certification and the Minister's declaration was imprudent.**

Cost of the valuation process in 2000

3.3.100 The total cost of the valuation process in 2000 varied from council to council and, in part, depended upon the number of assessments within the relevant municipality. Some 14 councils advised audit that the cost of the valuation process for each council ranged between \$500 000 and \$1 million, while a further 8 municipalities claimed that they each incurred costs under \$100 000. The average cost of each property valuation for country councils was generally twice the cost for metropolitan councils, based on the information provided by municipalities in response to my Office's survey.

3.3.101 The Valuer-General's analysis of the change in valuation contract costs per assessment from the valuations conducted in 2000 compared with that projected for the 2002 indicates that an average overall net reduction of some 15 per cent might be achieved in 2002, however, the estimated change in costs varies significantly between municipalities. This expected net reduction appears to flow from a combination of better property data and systems, and reduced property inspection requirements.

Ratepayer concerns about the 2000 property valuation process

3.3.102 Municipal council responses to my Office's survey indicated that two-thirds of councils, mainly those in the metropolitan area of Melbourne, were satisfied with the completeness and accuracy of the valuation process undertaken during 2000. Conversely, one-third of councils, generally from country areas, recognised that deficiencies arose mainly from:

- the untimely conduct of the valuation process;
- implementation problems with specialist information technology systems;
- errors in existing property details maintained by councils; and
- valuation errors.

3.3.103 **Based our survey results and visits to certain councils, we estimated that approximately 4 per cent, which equates to some 93 000 rate notices issued by municipal councils, resulted in a query by ratepayers.** The level of queries raised by ratepayers varied significantly between municipalities, ranging up to 6 000 for one municipality (or 11 per cent). Over half of the councils that responded to my Office's survey had between 1 000 and 6 000 queries from ratepayers. However, it should be noted that several municipalities did not record the level of queries raised by ratepayers and that not all queries raised by ratepayers indicate that an error existed in the property valuation or rate notice.

3.3.104 Ratepayer queries in relation to the 2000 property valuation process were either:

- Resolved in discussion with council officers and/or the valuer;
- Resulted in supplementary valuations by councils**. It is estimated that approximately 2 per cent, which equates to some 44 000 rate notices, have been subject to a supplementary valuation to correct deficiencies in the 2000 valuation process,** based on the results of my Office's survey which were tested by audit visits to certain councils. The level of supplementary valuations undertaken varied significantly between municipalities, ranging up to approximately 7 000 for one municipality; or
- Resulted in formal objections being lodged to the valuations by ratepayers under the *Valuation of Land Act* 1960. **Overall, less than one per cent of valuations were subject to a formal objection (after excluding those objections which were subsequently withdrawn following meetings with valuers and/or council officers),** based on the results of my Office's survey and data provided by the Valuer-General at the time of preparation of this Report. This represents some 18 900 objections**. However, the level of objections varied significantly between municipalities, with 8 councils recording objections at between 4 to 13.3 per cent. In absolute number terms, 3 councils received between 1 400 to 2 280 objections.**

3.3.105 At the date of preparation of this Report, many of the formal objections were yet to be finalised. In most instances, objections have been successful, mainly due to data errors in the valuation process, which have led to valuations being adjusted.

Supervision of the conduct of the valuations

3.3.106 The Valuer-General appointed supervisors on contract to assist his Office to monitor the work undertaken by councils' valuers and to ascertain the consistency and accuracy of the 2000 valuation process. As indicated earlier in this Report, based on my Office's survey of councils there was an expectation gap between the role played by the Valuer-General's supervisors and that anticipated by councils. In particular, council respondents to my Office's survey indicated that they required a greater level of advice from the Valuer-General's supervisor on the valuers' performance as well as the progress being made by the valuers compared with the required timelines. This is despite the obligations and responsibilities imposed upon councils by the *Valuation of Land Act* 1960 and the code of practice (*Valuation Best Practice*).

3.3.107 Councils advised audit of a number of other issues in respect of the role played by supervisors appointed by the Valuer-General, which highlighted, among other things, a need for:

- more training of supervisors and relevant council staff, particularly in respect of the new valuation methodology and software packages used in undertaking valuations;
- greater consistency in the sample sizes of valuations checked by the Valuer-General's staff or contractors; and
- more comprehensive checking of valuations undertaken by valuers before they are provided to councils, including more visits by supervisors to property sites to determine the accuracy of data sets.

3.3.108 These matters have been considered by the Valuer-General's Office as part of the development of procedures for the valuation process to be undertaken in 2002. **The Valuer-General's Office has drawn on comments from industry groups and an industry-based reference group in reviewing the valuation process and has sought to better define the relationship between councils, valuers and the Valuer-General (including his supervisors) by including clearer specification of the tasks to be undertaken during each stage of the valuation process within the recommended proforma contract for valuers.**

Availability of suitably qualified and experienced valuers

3.3.109 **The substantial challenges posed by the valuation process undertaken in 2000, including conducting a general valuation across the State, together with significantly shorter timeframes for undertaking the valuation and the introduction of a new valuation methodology, which included the use of computerised systems, compounded the difficulties faced by councils in engaging suitably qualified valuers.**

3.3.110 **All councils, in responding to my Office's survey, commented on the difficulties in attracting suitably qualified valuers. This remains a key challenge for the valuation process to be undertaken in 2002. Rural areas in particular had greater difficulty in appointing a valuer.**

3.3.111 Other related concerns raised by councils and/or the Valuer-General included:

- valuers accepting work from a number of councils that was beyond their capacity to handle;
- valuers encountering difficulty in meeting the tight legislative timelines;
- inconsistencies in the information collected by valuers during site inspections;
- valuers using inexperienced and/or unqualified people in the valuation process;
- adequate on-site inspections were not undertaken for all properties as required by the code of practice known as *Valuation Best Practice*; and
- shortage of valuers was also perceived to have added to the cost of the valuation process, particularly in rural areas.

3.3.112 For the next round of valuations to be undertaken in 2002, the Valuer-General has indicated that councils will be provided assistance with:

- appointment of suitable contract valuers;
- management of contracts with valuers; and
- training of council staff and assistance to further improve the accuracy of property data for 14 rural councils.

3.3.113 In addition, the Valuer-General has conducted a national recruitment campaign to supplement the number of available valuers.

Data and system deficiencies

3.3.114 The code of practice (*Valuation Best Practice*) recommended that councils and their valuers use computerised systems to assist with the 2000 valuation process in order to achieve efficiencies for all stakeholders.

3.3.115 Of the councils that responded to my Office's survey, 6 councils indicated that they continue to utilise manual or part manual card systems to record property information. Further, council respondents indicated that attempts to use computer software packages had, due to inexperience, implementation issues and compatibility problems, added to the difficulties in meeting legislative deadlines and ensuring the accuracy of recorded property information.

3.3.116 Industry groups have moved to review the existing software packages suitable to assist in the valuation process which are on the market as a service to the industry while the Valuer-General intends to conduct training programs and workshops to demonstrate the application of certain computer assisted quality assurance techniques available in preparation for the 2002 valuation process. These workshops are intended to include advice on the operation of these software packages and how they may be adapted to provide the necessary information for statutory and exception reporting purposes. This action should place councils in a better position for the 2002 valuation process.

Lessons for the next general valuation

3.3.117 The valuation process undertaken in 2000 was a massive and ambitious undertaking for all key stakeholders. Contract and time management, together with a shortage of appropriately skilled valuers, emerged as key issues during the 2000 valuation process. Further, certain legislative requirements were not met as referred to earlier.

3.3.118 The Valuer-General has also designed a recommended timetable and approach for the 2002 valuation, which is now built into the recommended proforma contract for valuers, that requires valuers to undertake certain valuation work at an earlier point in the valuation cycle in order to allow more time for review and checking. However, the recommended finishing date for the valuers' work, and the legislative completion date for the valuation, are unchanged from the previous valuation cycle.

3.3.119 In accordance with the Valuer-General's recommended timetable, councils were required to engage valuers in time to commence the 2002 valuation process on or before 1 March 2001. It is of concern that 8 councils have been unable to meet this first key date of the Valuer-General's timetable, particularly in light of the experiences encountered in 2000, and it acts as an alert to all key stakeholders to ensure the delays experienced in the 2000 valuation are not repeated.

3.3.120 The Valuer-General's strategy for the 2002 valuation process does not involve an external inspection of all properties, as was the case in 2000, rather it includes a rolling inspection program over more than one general valuation. This has enabled the Valuer-General to recommend a later starting date for the 2002 valuation process, than for the 2000 revaluation. Consequently, the period over which the 2002 valuation process will be undertaken is significantly shorter than the 2000 valuation process.

3.3.121 Council valuers are required under the *Valuation of Land Act* 1960 to have submitted their report on the next general valuation for 2002 to the relevant council by 30 June of that year. Valuers have a further 2 months to provide a copy of their valuation report to the Valuer-General, that is by 31 August. **However, under the *Local Government Act* 1989 municipal councils must declare by the same date the amount which council intends to raise by rates and charges and its related rating strategy. Consequently, unless councils and valuers meet their obligations under the *Valuation of Land Act* 1960 prior to the legislative deadlines, the Valuer-General and Minister will not have sufficient time to undertake the necessary procedures to enable them to be in a position to issue the required certifications and declarations before councils are required to make the necessary declarations in respect of rates and charges under the *Local Government Act* 1989.**

3.3.122 **It will be important that appropriate provision is made in the 2002 plans to ensure that all certificates of satisfactory valuation or valuation progress, as necessary, are issued by the Valuer-General prior to the use and adoption of the 2002 valuation by councils. Further, the strategy should also ensure that valuations are not adopted or used by municipal councils and other rating or taxing bodies, such as the State Revenue Office, until the Valuer-General has prepared his certification under the *Valuation of Land Act* 1960 as to the general truth and correctness of the relevant municipality's valuations and the Minister has declared, pursuant to the Act, that the valuation is suitable for adoption and can be used for rating purposes.**

RESPONSE *provided by Secretary, Department of Natural Resources and Environment*

The issues addressed in this response have been discussed with representatives from both the Department of Infrastructure and the Department of Treasury and Finance who support the comments.

Supervision and management of the valuation process

It is acknowledged by the valuation industry and the Valuer-General that errors can occur in the making of mass rating valuations. It is for this reason that the objection provisions are included in the Act to enable ratepayers to rectify any error.

Supervisors appointed by the Valuer-General monitored the progress of the valuation against council/valuer agreed time lines and a copy of the supervisor's monthly report was sent to both the council's Contract Manager and the council valuer identifying instances where the valuer's progress was significantly behind schedule. However, as the valuers are contracted to the council, the supervisors were limited in the action available to compel the valuer to complete the valuation in a proper and timely manner.

The Valuer-General will undertake a consultation campaign with councils throughout the 2002 valuation. This campaign will stress the need for regular and comprehensive provision of data to enable supervisors to adequately monitor the valuation throughout its progress and verify the completed valuation on its return.

Finalisation of the valuation process

The Valuer-General issues Section 7A certificates certifying various stages of the valuation upon request from a council following a claim for payment from the council's contract valuer. If the valuer does not request payment the Valuer-General has no powers under the Valuation of Land Act to require a council to submit a 7A request. Further, if a valuer does not provide data to support the claim from the council, the Valuer-General will issue a notice of non-compliance. In some cases, despite persistent requests, the complete data and valuation were only provided to the Valuer-General after the valuations were returned and implemented.

Traditionally, the Valuer-General has waited for the completion of the initial objection process before certifying to the Minister that the valuation is generally true and correct. This approach is considered to be an appropriate and reasonable interpretation of the intention of the Act. It should be noted that for the 2000 revaluation, the objection process has only just been completed in many councils.

The Valuer-General advises that he believes it desirable that certification in the Generally True and Correct format be issued prior to the use of the general valuation by a council or other rating authorities. However, the ability of the Valuer-General to provide such certification is dependant on a council's valuer providing the valuation and supporting data in a timely manner to enable a proper review. At present, there is no legislative power to demand such information until two months after the valuation return.

The Valuer-General will investigate the practicality of a strategy including legislative options to address this issue in the future.

RESPONSE *provided by Secretary, Department of Natural Resources and Environment - continued*

Ratepayer concerns about the 2000 property valuation process

In the first year of a Statewide general revaluation return it is to be expected that there would be a high level of ratepayer queries for a variety of reasons. This has been the case with the 2000 revaluation. However, ratepayer objections are often rate driven and not necessarily a result of poor valuation practice, i.e. the number of objections is not necessarily an indicator of the general truth and correctness of a valuation.

It must also be taken into consideration that this was the first general valuation undertaken after a number of years and large shifts in value had occurred in many regions. In addition, the relative movement in values for different areas within individual councils reflected a shift in the incidence of the rate burden and further contributed to ratepayer concerns.

Availability of suitably qualified and experienced valuers

In reviewing the progress and outcomes of the 2000 revaluation, the Valuer-General noted a shortage of qualified valuers in the rural areas and instigated a national recruitment campaign that resulted in the identification of 15 suitable valuers available for recruitment from interstate. At this stage, 6 valuers have been placed and a further 9 are still available for recruitment.

Lessons for the next general valuation

As part of the 2002 Valuation Best Practice Guidelines, valuers contracted by councils are required to provide the valuation and the supporting data to the Valuer-General's supervisors according to preset guidelines. This should enable the progressive review and certification of the valuation process to be completed in a more timely fashion. If the council valuers comply with these requirements the Valuer-General will be better able to certify the valuation prior to adoption by a council.

It is critical, within the current legislative framework, that individual councils closely monitor and maintain the necessary timeframes and ensure that their valuers complete the valuation and provide the suitable data within the timeframe set out in the 2002 Valuation Best Practice Guidelines. This will enable the Valuer-General to complete his final review and make his certification to the Minister prior to the return of the valuation.

It is likely that not all councils will be able to comply in 2002 but the Valuer-General will undertake an ongoing communication program fully outlining the benefits in improved public confidence in the valuation outcomes for councils able to comply with valuation program timelines.

The Valuer-General will investigate the practicality of a strategy including legislative options to address this issue in the future.

I am confident that as the biennial valuations progress and councils and their valuers become increasingly familiar with the process, the quality, timeliness and ratepayer acceptance of the valuation program will improve considerably.

SCHEDULE A
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS

Report	*Subject*	*Status at date of preparation of this Report*
	MATTERS RESOLVED OR ACTION COMMENCED	
PUBLIC TRANSPORT		
Ministerial Portfolios, May 1997, p. 121.	The Department of Infrastructure has not performed a post-implementation review of the contracting-out of the Melbourne to Warrnambool and Melbourne to Cobram public transport services and, accordingly, there is a possibility that the experiences gained from these arrangements may not be factored into future privatisation proposals.	Although the Department of Infrastructure has not conducted a post-implementation review of the contracting-out of these services, the relevant contracts are currently being reviewed in order to determine an appropriate course of action to ensure the continuation of these services after the expiry date of the existing arrangements of 30 June 2001.
PORTS		
Ministerial Portfolios, June 2000, p. 323-5.	The balance sheet of the Victorian Channels Authority does not reflect the value of its shipping channels. Accordingly, the true value of all assets available to the Authority are not reported and the true cost of the services provided by the Authority are not transparent.	During the 1999-2000 financial year, all channel assets previously managed by the former Port of Melbourne Authority were recognised by the Victorian Channels Authority.
LOCAL GOVERNMENT		
Ministerial Portfolios, May 1998, pp. 110-13.	The use of audit committees and internal audit had not been universally adopted across the local government sector and, as a consequence, corporate governance within the sector had been diminished.	The Local Government Division of the Department of Infrastructure in conjunction with the local government sector has developed and issued *best practice* guidelines for the operation of audit committees and internal audit in local government entities.
Ministerial Portfolios, May 1998, pp. 114-20.	A survey in the 1996-97 financial year of the management of municipal business undertakings indicated that 12 councils which had contract expenditure in excess of $68 million were unable to identify surpluses or losses generated from their business unit operations.	The Department's Local Government Division in conjunction with the local government sector has developed a *best practice* guideline for internal and external financial reporting by councils on the financial performance of business units and major contracts.
Ministerial Portfolios, May 1999, pp. 158-60.	Legislative amendments should be considered for local government entities requiring annual reporting to the responsible Minister and the Auditor-General of all instances of theft, arson, irregularity and fraud.	The *Local Government Act* 1989 is to be amended during 2002. The Department of Infrastructure previously advised that amendments to the Act requiring annual reporting to the responsible Minister and the Auditor-General of all instances of theft, arson, irregularity and frauds similar to those required of other public sector agencies will be considered as part of the update.

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

Report	*Subject*	*Status at date of preparation of this Report*
	MATTERS RESOLVED OR ACTION COMMENCED - *continued*	
LOCAL GOVERNMENT		
Ministerial Portfolios, June 2000, pp. 157-8.	A government study released in January 2000 identified the need for most councils to take action within the next 7 years to fund required infrastructure asset renewals.	In May 1999, the Local Government Division of the Department of Infrastructure advised my Office that following consultation with councils on the findings of the Government's study of local government infrastructure, the Local Government Division intends to recommend to the responsible Minister strategies to improve infrastructure management in councils. As indicated earlier in this Part of the Report the Division created a reference group in May 2001 which will consider asset management practices in the sector.

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS			
FINANCIAL YEAR ENDED 30 JUNE 2000			
Department of Infrastructure	27 Oct. 2000	30 Oct. 2000	✓
TRANSPORT			
Melbourne City Link Authority	27 Oct. 2000	27 Oct. 2000	✗
Roads Corporation	19 Oct. 2000	19 Oct. 2000	✓
Public Transport Corporation	7 Sept. 2000	8 Sept. 2000	✓
Victorian Rail Track	26 Oct. 2000	31 Oct. 2000	✓
PORTS			
Marine Board of Victoria	6 Oct. 2000	10 Oct. 2000	✓
Hastings Port (Holding) Corporation	21 Sept. 2000	26 Sept. 2000	✓
Melbourne Port Corporation	15 Sept. 2000	22 Sept. 2000	✓
Victorian Channels Authority	15 Sept. 2000	28 Sept. 2000	✓
PLANNING			
Architects Registration Board of Victoria	12 Sept. 2000	14 Sept. 2000	✓
Building Control Commission	11 Aug. 2000	28 Aug. 2000	✓
Heritage Council	5 Oct. 2000	10 Oct. 2000	✓
Plumbing Industry Commission	3 Oct. 2000	4 Oct. 2000	✓
ULC Real Estate Services Pty Ltd	30 Aug. 2000	5 Sept. 2000	✓
Urban Land Corporation	30 Aug. 2000	5 Sept. 2000	✓

✓ Clear audit opinion issued.

✗ Qualified audit opinion issued.

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

			Clear opinion issued	
Entity	*Statements signed by entity*	*Auditor-General's reports signed*	*Financial Statement*	*Performance Statement*

COMPLETED AUDITS - *continued*

FINANCIAL YEAR ENDED 30 JUNE 2000 - *continued*

LOCAL GOVERNMENT

Alpine Shire Council	27 Oct. 2000	9 Nov. 2000	✗	✓
Ararat Rural City Council	25 Sept. 2000	9 Oct. 2000	✓	✓
Ballarat City Council	26 Sept. 2000	29 Sept. 2000	✓	✓
Banyule City Council	19 Sept. 2000	20 Sept. 2000	✓	✓
Bass Coast Shire Council	17 Oct. 2000	26 Oct. 2000	✗	✓
Baw Baw Shire Council	18 Sept. 2000	20 Sept. 2000	✓	✓
Bayside City Council	29 Sept. 2000	29 Sept. 2000	✓	✓
Boroondara City Council	13 Oct. 2000	16 Oct. 2000	✓	✓
Brimbank City Council	30 Sept. 2000	12 Oct. 2000	✓	✓
Buloke Shire Council	12 Jan. 2001	23 Jan. 2001	✓	✓
Campaspe Shire Council	27 Sept. 2000	5 Oct. 2000	✓	✗
Cardinia Shire Council	26 Oct. 2000	14 Nov. 2000	✓	✓
Casey City Council	19 Sept. 2000	20 Sept. 2000	✓	✓
Casey - Cardinia Regional Library Corporation	20 Sept. 2000	26 Sept. 2000	✓	n.a.
Central Highlands Regional Library Corporation	12 Sept. 2000	15 Sept. 2000	✓	n.a.
Central Goldfields Shire Council	15 Nov. 2000	17 Nov. 2000	✓	✓
CityWide Service Solutions Pty Ltd	4 Oct. 2000	5 Oct. 2000	✓	n.a.
Colac-Otway Shire Council	13 Sept. 2000	28 Sept. 2000	✓	✗
Corangamite Shire Council	5 Oct. 2000	11 Oct. 2000	✓	✓
Corangamite Regional Library Corporation	28 Sept. 2000	2 Oct. 2000	✓	n.a.
Darebin City Council	21 Dec. 2000	22 Dec. 2000	✗	✓
Delatite Shire Council	25 Sept. 2000	29 Sept. 2000	✓	✓
East Gippsland Shire Council	22 Sept. 2000	20 Oct. 2000	✓	✓
Eastern Regional Library Corporation	26 Sept. 2000	28 Sept. 2000	✓	n.a.
Frankston City Council	26 Sept. 2000	28 Sept. 2000	✓	✓
Gannawarra Shire Council	26 Sept. 2000	29 Sept. 2000	✓	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

Entity	*Statements signed by entity*	*Auditor-General's reports signed*	*Clear opinion issued*	
			Financial Statement	*Performance Statement*

COMPLETED AUDITS - *continued*

FINANCIAL YEAR ENDED 30 JUNE 2000 - *continued*

LOCAL GOVERNMENT- *continued*

Geelong Regional Library Corporation	7 Sept. 2000	13 Sept. 2000	✓	n.a.
Glen Eira City Council	27 Sept. 2000	29 Sept. 2000	✓	✗
Glenelg Shire Council	12 Sept. 2000	30 Sept. 2000	✓	✗
Glenelg Regional Library Corporation	18 Sept. 2000	26 Sept. 2000	✓	n.a.
Golden Plains Shire Council	21 Nov. 2000	22 Jan. 2001	✗	✓
Goulburn Valley Regional Library Corporation	23 Sept. 2000	29 Sept. 2000	✓	n.a.
Greater Bendigo City Council	3 Nov. 2000	3 Nov. 2000	✓	✓
Greater Dandenong City Council	9 Oct. 2000	9 Oct. 2000	✓	✓
Greater Geelong City Council	13 Sept. 2000	27 Sept. 2000	✓	✓
Greater Shepparton City Council	25 Sept. 2000	27 Sept. 2000	✓	✓
Hepburn Shire Council	28 Sept. 2000	10 Oct. 2000	✓	✓
High Country Regional Library Corporation	28 Sept. 2000	29 Sept. 2000	✓	n.a.
Hindmarsh Shire Council	24 Oct. 2000	29 Oct. 2000	✓	✓
Hobsons Bay City Council	16 Oct. 2000	17 Oct. 2000	✓	✓
Horsham Rural City Council	9 Nov. 2000	10 Nov. 2000	✗	✓
Hume City Council	10 Oct. 2000	12 Oct. 2000	✓	✓
Hume-Moonee Valley Regional Library Corporation	26 Oct. 2000	31 Oct. 2000	✗	n.a.
Indigo Shire Council	25 Oct. 2000	13 Nov. 2000	✗	✗
Kingston City Council	26 Sept. 2000	10 Oct. 2000	✓	✓
Knox City Council	28 Sept. 2000	28 Sept. 2000	✓	✓
La Trobe Shire Council	26 Oct. 2000	27 Oct. 2000	✓	✓
Loddon Shire Council	12 Dec. 2000	18 Dec. 2000	✓	✓
Macedon Ranges Shire Council	13 Sept. 2000	19 Sept. 2000	✓	✓
Manningham City Council	26 Sept. 2000	10 Oct. 2000	✓	✓
Maribyrnong City Council	28 Sept. 2000	6 Oct. 2000	✓	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

Entity	*Statements signed by entity*	*Auditor-General's reports signed*	*Clear opinion issued: Financial Statement*	*Clear opinion issued: Performance Statement*
COMPLETED AUDITS - *continued*				
FINANCIAL YEAR ENDED 30 JUNE 2000 - *continued*				
LOCAL GOVERNMENT- *continued*				
Maroondah City Council	25 Sept. 2000	27 Sept. 2000	✓	✓
Melbourne City Council	5 Oct. 2000	13 Oct. 2000	✓	✓
Melbourne Wholesale Fish Market Pty Ltd	13 Sept. 2000	13 Sept. 2000	✓	n.a.
Melton Shire Council	15 Nov. 2000	16 Nov. 2000	✗	✓
Mildura Rural City Council	12 Jan. 2001	15 Jan. 2001	✓	✓
Mitchell Shire Council	21 Sept. 2000	3 Oct. 2000	✓	✓
Moira Shire Council	22 Jan. 2001	23 Jan. 2001	✓	✓
Monash City Council	25 Sept. 2000	29 Sept. 2000	✓	✓
Moonee Valley City Council	18 Sept. 2000	25 Sept. 2000	✓	✓
Moorabool Shire Council	27 Sept. 2000	29 Sept. 2000	✓	✓
Moreland City Council	26 Sept. 2000	27 Sept. 2000	✓	✓
Mornington Peninsula Shire Council	30 Oct. 2000	1 Nov. 2000	✗	✓
Mount Alexander Shire Council	17 Nov. 2000	23 Nov. 2000	✓	✓
Moyne Shire Council	29 Sept. 2000	10 Oct. 2000	✓	✓
Murrundindi Shire Council	5 Dec. 2000	7 Dec. 2000	✓	✓
Nillumbik Shire Council	28 Nov. 2000	30 Nov. 2000	✗	✓
North Central Goldfields Regional Library Corporation	5 Oct. 2000	11 Oct. 2000	✓	n.a.
Northern Grampians Shire Council	24 Oct. 2000	26 Oct. 2000	✓	✓
Port Phillip City Council	16 Oct. 2000	19 Oct. 2000	✓	✓
Prahran Market Pty Ltd	29 Sept. 2000	16 Oct. 2000	✓	n.a.
Pyrenees Shire Council	19 Dec. 2000	19 Dec. 2000	✓	✓
Queenscliffe Borough Council	21 Sept. 2000	28 Sept. 2000	✓	✓
Queen Victoria Market Pty Ltd	13 Sept. 2000	13 Sept. 2000	✓	n.a.
Regent Management Company Pty Ltd	26 Feb. 2001	27 Feb. 2001	✓	n.a.
South Gippsland Shire Council	6 Oct. 2000	6 Oct. 2000	✓	✓
Southern Grampians Shire Council	6 Sept. 2000	26 Sept. 2000	✗	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

Entity	*Statements signed by entity*	*Auditor-General's reports signed*	*Clear opinion issued* *Financial Statement*	*Clear opinion issued* *Performance Statement*
COMPLETED AUDITS - *continued*				
FINANCIAL YEAR ENDED 30 JUNE 2000 - *continued*				
LOCAL GOVERNMENT - *continued*				
Stonnington City Council	20 Oct. 2000	24 Oct. 2000	✓	✓
Strathbogie Shire Council	28 Sept. 2000	4 Oct. 2000	✓	✓
Streetsahead Cleaning Services	30 Nov. 2000	5 Dec. 2000	✓	n.a.
Surf Coast Shire Council	15 Sept. 2000	3 Oct. 2000	✗	✓
Swan Hill Rural City Council	16 Nov. 2000	22 Nov. 2000	✗	✓
Swan Hill Regional Library Corporation	21 Nov. 2000	30 Nov. 2000	✓	n.a.
Towong Shire Council	16 Nov. 2000	21 Nov. 2000	✗	✓
Wangaratta Rural City Council	29 Sept. 2000	6 Oct. 2000	✓	✗
Warrnambool City Council	20 Sept. 2000	27 Sept. 2000	✓	✓
Wellington Shire Council	22 Sept. 2000	28 Sept. 2000	✓	✓
West Wimmera Shire Council	26 Sept. 2000	9 Oct. 2000	✓	✗
West Gippsland Regional Library Corporation	21 Sept. 2000	3 Oct. 2000	✓	n.a.
Whitehorse City Council	26 Sept. 2000	26 Sept. 2000	✓	✓
Whitehorse Manningham Regional Library Corporation	30 Oct. 2000	31 Oct. 2000	✗	n.a.
Whittlesea City Council	29 Sept. 2000	5 Oct. 2000	✓	✓
Wimmera Regional Library Corporation	10 Nov. 2000	15 Nov. 2000	✓	n.a.
Wodonga Rural City Council	29 Nov. 2000	1 Dec. 2000	✗	✗
Wyndham City Council	17 Nov. 2000	23 Nov. 2000	✗	✓
Yarra City Council	3 Oct. 2000	3 Oct. 2000	✓	✓
Yarra Ranges Shire Council	27 Sept. 2000	27 Sept. 2000	✓	✓
Yarra Melbourne Regional Library Corporation	29 Sept. 2000	2 Oct. 2000	✓	n.a.
Yarra Plenty Regional Library Corporation	26 Sept. 2000	29 Sept. 2000	✓	n.a.
Yarriambiack Shire Council	12 Dec. 2000	18 Dec. 2000	✓	✓

✓ Clear audit opinion issued.

✗ Qualified audit opinion issued.

n.a. Agency not required by legislation to produce a performance statement.

Part 3.4

Justice

KEY FINDINGS

Management of the Metropolitan Women's Correctional Centre

- In November 2000, the Government reached an agreement with the contractor to transfer the ownership and management of the Metropolitan Women's Correctional Centre at Deer Park to the public sector as the defaults under the contract were persistent and continuing in nature, and the operator could not ensure the safety and wellbeing of prisoners, staff and visitors.

  Paras 3.4.47 to 3.4.55

- The settlement amount was $20.2 million, consisting of $17.8 million to purchase the Centre's buildings, infrastructure and chattels, and $2.4 million to finance the costs associated with terminating the loan facility.

  Paras 3.4.47 to 3.4.55

- The weaknesses in the Centre's contractual arrangement, especially in respect of the lack of clarity regarding the rights and obligations of the respective parties and the dispute resolution process, left the Department of Justice exposed to risk. Despite this situation, the Government was able to terminate the contract on favourable terms to itself, while at the same time avoiding a prolonged legal dispute with the contractor through negotiating a commercial settlement amicable to both parties.

  Paras 3.4.78 to 3.4.84

- In response to the Government's drive for significant cost savings from outsourcing, the Department in selecting the original service provider for the Centre, placed considerable emphasis on the financial evaluation criteria used to ensure cost savings and less emphasis on the capacity of the contractor to effectively manage and operate the facility. This emphasis on cost savings was one of the factors contributing to the problems encountered at the Centre.

  Paras 3.4.61 to 3.4.70

KEY FINDINGS *- continued*

Management of the Metropolitan Women's Correctional Centre *- continued*

- An economic appraisal was not undertaken at the time of outsourcing the Centre which resulted in insufficient information being available, to enable the Government to make an informed decision on whether this form of service provision provided the most cost-effective outcome for the State or to enable the Department to properly assess the adequacy of private sector tenders.

Paras 3.4.73 to 3.4.75

Estate Agents Guarantee Fund

- Approximately $8.4 million is anticipated to be expended from the Estate Agents Guarantee Fund during the year. This is significantly less than the $28.4 million in revenue expected to be generated by the Fund, resulting in a budgeted surplus of almost $20 million for the 2000-01 financial year.

Paras 3.4.110 to 3.4.118

- The net assets held in the Fund as at 30 June 2000 totalled $99.9 million. In these circumstances, the Parliament could consider amendments to the Act in order to broaden the criteria for grant payments.

Paras 3.4.110 to 3.4.118

- Payments have been made from the Fund on a number of occasions to meet the costs associated with professional training of real estate agents, however, funding has not been provided for the training and development of other professionals working in the real estate industry such as solicitors, conveyancing agents and financial advisors.

Paras 3.4.126 to 3.4.130

- In order to improve the level of accountability over trust funds separate annual financial reports should be produced for each of the major funds administered by the Department.

Paras 3.4.107 to 3.4.109

SUMMARY OF AUDIT RESULTS

3.4.1 The Justice portfolio comprises the Department of Justice, as the central coordinating agency for the portfolio, Victoria Police and a number of public sector agencies, statutory offices, and judicial and quasi-judicial bodies. Broadly, the portfolio consists of the following areas of government activity.

Attorney-General

3.4.2 The area within the portfolio under the responsibility of the Attorney-General encompasses a broad range of services provided directly by various business units within the Department of Justice including:

- legal services which involves developing legislation and providing legal advice to government;
- enforcement of fines, civil judgements and court orders;
- confiscation of assets held by convicted offenders; and
- support for victims of crime

3.4.3 In addition, court and tribunal services are provided by judicial and quasi-judicial bodies including:

- The Supreme Court;
- The County Court;
- The Magistrates' Court (including the Children's Court, Coroner's Court and the Victims of Crime Assistance Tribunal); and
- The Victorian Civil and Administrative Tribunal (VCAT).

3.4.4 Furthermore, the following public sector agencies are ultimately accountable to the Attorney-General.

- Office of Public Prosecutions;
- Victoria Legal Aid;
- Victorian Electoral Commission;
- Office of the Legal Ombudsman;
- Legal Practise Board; and
- Victoria Police (for its support to the judicial process and custody and transportation of persons in police custody).

Police and Emergency Services

3.4.5 In relation to Police and Emergency Services, the Department plays a co-ordination role in respect of community safety, with Victoria Police, Country Fire Authority and Metropolitan Fire and Emergency Services Board providing the associated essential services. In relation to the Corrections function, the Department is involved in the provision of prison services and the management of community-based orders issued by the courts.

Consumer Affairs

3.4.6 The Consumer Affairs function involves the Department providing:

- consumer protection; and
- registration and issue of births, deaths, marriages and change of name certificates.

3.4.7 In relation to this function, Victoria Police provides information and licensing services which involves processing Freedom of Information (FOI) applications and probity checks.

3.4.8 Furthermore, the following public sector agencies form part of the Consumer Affairs function:

- Equal Opportunity Commission - deals with matters involving equal opportunity and discrimination; and
- Office of the Public Advocate - advocates, promotes and supports the rights and interests of the disadvantaged.

3.4.9 The Attorney-General, the Minister for Consumer Affairs, and the Minister for Police and Emergency Services and the Minister for Corrections have responsibility for operations within the Justice sector. These Ministers have collective responsibility for the Department of Justice.

3.4.10 Details of the specific ministerial responsibilities for public sector bodies within the portfolio are provided in Table 3.4A. These public bodies, together with the Department of Justice, were subject to audit during the 1999-2000 financial year.

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

Ministerial portfolio	*Entities subject to audit*
Attorney-General	Equal Opportunity Commission Legal Practice Board Legal Practitioners Liability Committee Office of Public Prosecutions Office of the Legal Ombudsman Office of the Public Advocate Queen Victoria Women's Centre Trust Senior Master of the Supreme Court Victoria Legal Aid Victorian Electoral Commission Victorian Institute of Forensic Medicine
Consumer Affairs	Residential Tenancies Bond Authority
Corrections	-
Police and Emergency Services	Country Fire Authority Metropolitan Fire and Emergency Services Board National Institute for Forensic Science National Police Ethnic Advisory Bureau Office of the Chief Commissioner of Police (Victoria Police)

Audit opinions issued

3.4.11 The Auditor-General is responsible for the audit of 18 agencies (including the Department of Justice and Victoria Police) within the Justice portfolio. All of these audits have 30 June balance dates and 16 are required to report to the Parliament by 31 October in accordance with the *Financial Management Act* 1994. With the exception of the Senior Master of the Supreme Court and the National Institute for Forensic Science, all agencies within the Justice portfolio report to the Parliament under section 46 of the Act.

3.4.12 At the date of preparation of this Report, 16 audit opinions were issued on financial reports of public sector agencies within the Justice portfolio. Details of audits completed and those outstanding are contained in Schedule B of this Part of the Report.

3.4.13 Of the financial reports finalised, only one was subject to a qualified audit report. The audit opinion issued on the Melbourne Fire and Emergency Services Board's financial report was qualified as all the revenue controlled by the Board was not disclosed in its operating statement in accordance with Australian Accounting Standard AAS15.

Timeliness of financial reporting process

3.4.14 The *Financial Management Act* 1994 requires government agencies to prepare their financial reports within 8 weeks of balance date and for these reports to be audited within 4 weeks of their receipt by the Auditor-General. Table 3.4B provides details of the timeliness of the financial reporting process within the Justice portfolio.

TABLE 3.4B
TIMELINESS OF FINALISATION OF AUDITED FINANCIAL STATEMENTS, JUSTICE PORTFOLIO

	Entities	
Number of weeks after end of financial period	*Number*	*Per cent (cumulative)*
Less than 8 weeks	-	-
8 to 10 weeks	3	17
10 to 12 weeks	2	28
12 to 14 weeks	3	45
14 to 16 weeks	2	56
Over 16 weeks *(a)*	8	100

(a) Includes 2 entities whose financial reports are yet to be finalised.

3.4.15 The above table shows that **there is scope for improvement in the timeliness of audited financial report completion by portfolio entities, with only 28 per cent of entities able to meet the 12 week legislated completion timeframe**. The audited financial statements of 56 per cent of the entities were available within 4 weeks of the legislated completion timeline (i.e. within 16 weeks of year-end). However, at the date of preparation of this Report, 2 entities had not produced their financial statements for the financial year ended 30 June 2000.

3.4.16 **Timeliness of reporting is an essential characteristic of quality information and the effectiveness of the accountability process. Accordingly, it is important that avenues are identified and pursued to improve the timeliness of the financial reporting process.**

MANAGEMENT OF THE METROPOLITAN WOMEN'S CORRECTIONAL CENTRE

3.4.17 When the former State Government was elected in 1992, Victoria's corrections system was based on the traditional public sector model where all prisons were owned and operated by the Government. At that time, the Government identified a number of serious, long-standing problems with the adult prison system, such as:

- poor productivity levels and high operating costs;
- declining and inadequate infrastructure;
- inflexible workforce; and
- low levels of accountability.

3.4.18 The Government at that time considered that cost-efficiencies and improved service delivery could be achieved by limiting its role to setting policy, standards and outcomes, and leaving the service delivery to contracted private sector providers. This policy position was outlined in the Government's *Infrastructure Investment Policy for Victoria,* which sought to encourage private sector involvement in the investment of both new and existing public sector infrastructure and related services. In accordance with this policy, the Department of Justice encouraged private sector firms to bid, in a competitive environment, for the right to manage and operate the State's private prisons. The policy document provided guidance on undertaking outsourcing projects and, in order to ensure that cost savings were generated, set a financial benchmark, which the tenderers had to exceed before they were eligible to provide services to the Government.

3.4.19 In December 1993, the New Prisons Project was established. This initiative sought private sector provision of 3 new prison facilities in Victoria to replace several outdated facilities, namely, the Coburg Complex, (incorporating Pentridge Prison and the Metropolitan Reception Prison), Fairlea Women's Prison at Fairfield and the Rural Men's Prison located at Sale.

3.4.20 In order for the Department to outsource prison services, the *Corrections Act* 1986 was amended to enable the Minister for Corrections to enter into service agreements with the private sector. The required amendments, which were made in late 1994, became operative in January 1995. The amendments to the Act also provided for the creation of a Commissioner for Correctional Services whose responsibilities included "monitoring performance in the provision of all correctional services to achieve the safe custody and welfare of prisoners and offenders".

3.4.21 One of the 3 new prisons proposed was the Metropolitan Women's Correctional Centre at Deer Park on the west side of Melbourne, which provided a 125 bed prison capable of accommodating approximately 75 per cent of State's female prisoner population. In response to increases in Victoria's women prisoner population, the Centre now provides accommodation for around 174 prisoners. The additional accommodation needed for the increased number of prisoners has been primarily provided in portable accommodation units located on the site.

3.4.22 Under the new private sector arrangements, cost savings of $225 million were expected to be generated by the Department from the 3 new prisons over the term of the respective service agreements ($16 million of which was related to the Centre at Deer Park).

Metropolitan Women's Correctional Centre at Deer Park.

Tender process

3.4.23 The key objectives of the New Prisons Project were to:

- *"reduce the costs to Government to below established benchmark recurrent costs of service delivery;*
- *ensure the scope and quality of services to prisoners is maintained and/or enhanced without compromising security and safety;*
- *meet government policy objectives of risk transfer to the private sector;*
- *replace inadequate and ageing prisons with new facilities and increase the capacity of correctional facilities to meet projected demand; and*
- *introduce private sector investment funds (equity) into the Victorian prison infrastructure".*

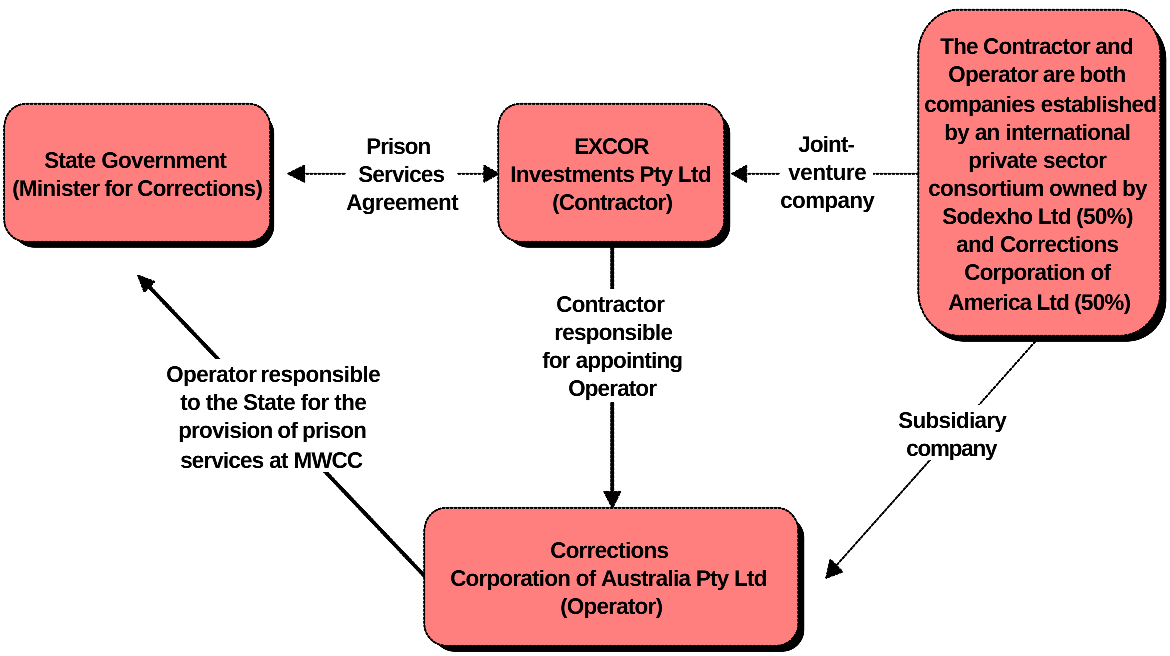
3.4.24 In late 1993, the Department publicly invited potential bidders to submit a "registration of capacity" for the provision of a new women's prison at Deer Park. Following an evaluation of the submissions received, a short list of 3 bidders was developed in January 1994. A project brief for the design, construction and operation of the Centre was then developed and issued to the short-listed bidders in July 1994 as the basis upon which tenders were to be submitted.

3.4.25 Tender submissions prepared by 2 of the 3 bidders were eliminated, as they did not meet the financial requirements of the tender. One bid was eliminated because the price submitted did not generate the cost savings required by the Government's financial benchmark. The other bid was eliminated as the tenderer was not willing to accept the transfer of certain financial risks, was unable to demonstrate the existence of a suitable financier and did not provide an acceptable financial structure.

3.4.26 In December 1994, Excor Investments Pty Ltd (the contractor), a joint venture company of an international consortium owned by Sodexho Ltd (a large international management and construction company) and Corrections Corporation of America Ltd (a major local and international private provider of correctional services), was selected as the preferred tenderer. The tender price submitted by the contractor was 15 per cent below the State Government's financial benchmark.

3.4.27 In June 1995, the contractor appointed Corrections Corporation of Australia Pty Ltd (the operator), a subsidiary company of the international consortium mentioned above, as the operator of the Centre. Chart 3.4C sets out the relationship between the Government, the contractor and the operator.

CHART 3.4C
CONTRACTUAL RELATIONSHIP BETWEEN THE GOVERNMENT, CONTRACTOR AND OPERATOR FOR THE METROPOLITAN WOMEN'S CORRECTIONAL CENTRE



3.4.28 The Centre, which was commissioned in August 1996, cost $21 million to construct, $17 million of which was funded by debt financing and $4 million by an equity contribution from the private sector consortium.

3.4.29 In our 1995-96 *Report of the Auditor-General on the Statement of Financial Operations*, we concluded that the bidding and selection process for the private prison contract was undertaken in a manner consistent with the Government's *Infrastructure Investment Policy for Victoria*. **Furthermore, the probity auditor engaged by the Department to review the bid evaluation processes concluded that the methodology and criteria used for the evaluation of the tenders was fair and reasonable.**

Financial and operating arrangements

3.4.30 The financial and operating arrangements for the Centre were outlined in a series of complex agreements between the former Minister for Corrections on behalf of the State, the contractor and the project's financier. There were 3 principal agreements: a Ground Lease Agreement, a Prison Services Agreement (PSA) and a Tripartite Agreement, the key terms of which included:

- The Centre was to be constructed on Crown land leased by the contractor for a period of 40 years;
- Specified prison accommodation services were to be provided by the contractor to the Department over a 20 year period, with allowance for a further 10 year extension;
- Specified correctional services and programs were to be provided by the contractor over an initial 5 year period, with correctional services fees to be payable by the State for the delivery of these services. The PSA was renewable at the Government's option for 5 further terms of 3 years or under certain circumstances could be put to tender by the Government at the end of the initial term or on expiry of each term thereafter;
- Ownership of the facilities was to remain with the contractor; and
- The project’s financier was to hold a security interest in the new facilities, with the contractor and the Government liable for the payment of *“Break-Costs”* (compensation) to the financier, in the event that the loan provided by the financier to fund the construction of the Centre was prematurely terminated.

3.4.31 The PSA allowed the Department to influence the contractor’s performance through performance-based payments and penalties for non-performance.

3.4.32 There were approximately 20 service delivery outcomes included in the Agreement, broken into 5 broad categories, namely, prison operation, education and training, prison industries, prisoner health, and other programs. Annual performance payments were based on the contractor’s achievement of these service delivery outcomes.

3.4.33 The PSA also provided the Government with a number of avenues to address poor performance. For example, the Department had the power to issue a certificate reducing the accommodation services charge or the correctional services fee, where the operator failed to deliver services to the required standard. Alternatively, the agreement provided for a default notice to be issued by the Minister requiring the contractor to take action to address the default within a specified timeframe.

Problems at the Metropolitan Women's Correctional Centre

3.4.34 As indicated earlier in this Report, the Commissioner has responsibility for monitoring the operations of all prison services, which is performed by the Monitoring and Assessment Unit, within the Office of Correctional Services Commissioner. The functions of this Unit included reviewing the operator's performance against the Service Delivery Outcomes (SDOs) and targets included in the PSA.

3.4.35 The results of the Unit's review process indicated that the operator's performance was not meeting the standards specified in the contract and was deteriorating over time, particularly in relation to outcomes dealing with drug use, assaults and self-harm. Table 3.4D illustrates the operator's performance against SDOs for the period 1997-98 to 2000-01.

TABLE 3.4D
CONTRACTOR'S PERFORMANCE AGAINST SDOs

		Actual results for year			
Service delivery outcome	*Standard required*	*1997-98*	*1998-99*	*1999-00*	*2000-01*
Self-mutilation/attempted suicide	3.8 per 100 receptions	4.5	5.4	7.8	9.4
Assaults on prisoners by other prisoners	30.0 per 100 prisoner year	35.3	30	37.4	45.3
Assaults on staff or other persons	10.0 per 100 prisoner year	16.7	10	9.3	19.7
Drug testing	8.26%	8.1%	7.5%	5.7%	8.6%
Medical screenings performed within 24 hours of reception	100%	Not recorded	98.9%	99.8%	97.7%

3.4.36 The ongoing decline in the operator's performance was further illustrated by the high number of prison incidents, serious security breaches and prisoner management issues which the operator failed to adequately prevent, including:

- two serious prisoner disturbances in late 1999;
- a prisoner accessing confidential prisoner information;
- prisoners entering restricted areas;
- lack of procedural checks and monitoring of the visitors centre;
- loss of control over the high security unit;
- a major fire in the high security unit;

- a large number of prisoners starting fires and assaulting staff during April and May 2000; and
- an inadequate response to a bomb threat.

3.4.37 In mid-1999, the Commissioner formally advised the operator of her concerns with the Centre's performance. In particular, the Commissioner identified the operator's inability to deliver the outcomes outlined in the correctional services agreement, and the lack of remedial action taken by the operator to address the significant security, prisoner management and safety issues identified at the prison.

3.4.38 Although strategies introduced by the operator to address these deficiencies were initially successful, within several months the performance of the operator had again deteriorated.

3.4.39 The seriousness and continuing nature of the problems resulted in the Minister of Corrections, under clause 57.1 of the Prison Services Agreement, issuing the operator with a Correctional Services Default Notice on 10 May 2000. The Default Notice raised a number of material contractual default's including:

- the failure of the gatehouse officer to process and record details of visitors to the Centre;
- firearms carried by 2 police officers were not surrendered to prison staff and stored in the gatehouse before the officers entered the maximum-security prison, and this incident was not immediately reported;
- an ex-prisoner had access to a confidential incident report; and
- a medical bag was left in a prisoner's cell, resulting in the loss of needles and syringes.

3.4.40 On 19 May 2000, a second Default Notice was issued by the Minister as a result of:

- staff leaving the officer's station entrance door in the management unit unsecured, allowing 5 high security prisoners access to an exercise yard used by protected prisoners; and
- a set of keys to the Centre's most secure unit going missing for 33 hours, with the incident not declared at the earliest opportunity.

3.4.41 A third Default Notice was issued on 18 July 2000, which included the following material defaults:

- failure to contain and supervise prisoners;
- lack of appropriate staffing levels;
- failure to manage non-conforming prisoners, leading to a number of incidents involving prisoners lighting fires and assaults on staff;
- excessive periods of prisoner "lock downs" in cells;
- use of unauthorised staff members to transport prisoners between prisons;
- ineffective management of programs and security procedures for illicit drugs;

- failure to comply with emergency management procedures;
- inadequate provision of security systems to ensure the safety and security of prisoners and staff; and
- failure to medically assess prisoners on their admittance to the Centre.

3.4.42 In addition to the reviews undertaken by the Commissioner, the operations of the prison were also subject to a number of other independent reviews, including:

- A review by the Office of Post Compulsory Education, Training and Employment in January 2000, which led to the suspension, for one month, of the operator's status as a Registered Training Organisation;
- A health service audit by the Department of Human Services in March 2000, which identified significant issues with the delivery of health services at the Centre that could potentially compromise the health of women at the prison;
- An investigation by the Victorian WorkCover Authority in May 2000, which resulted in the sanctioning of the operator for regulatory breaches associated with the exposure of staff to an unsafe environment caused by under-staffing at the Centre; and
- A security audit conducted by the Department of Justices' Security and Emergency Services Group in June 2000, which found that the operator had breached several of its own operating procedures. This review also identified the absence of appropriate policies and procedures to guide and assist staff in undertaking their duties and to ensure the adoption of a consistent approach to prisoner management within the Centre.

3.4.43 The ongoing problems at the Center were documented, by the Commissioner, in her 13 September 2000 *Metropolitan Women's Correctional Centre's Compliance with its Contractual Obligations and Prison Service Agreement* report, which was tabled in the Parliament.

3.4.44 That report indicated that despite repeated notice being provided of specific issues of non-compliance, the operator failed to remedy the underlying service deficiencies outlined in the default notices and, as a consequence, the operator had not fulfilled its contractual obligations in a range of specific areas, including:

- prevention and management of self-harm;
- management of non-conforming prisoners;
- provision of adequate staffing to ensure close prisoner surveillance and maintenance of security and safety of staff and prisoners;
- management of illicit drugs;
- provision of sufficient security systems to ensure the safety of prisoners and staff; and
- management of emergency responses and compliance with emergency management procedures.

3.4.45 **In that Report, the Commissioner indicated that the difficulties experienced at the Centre appeared to be the collective result of:**

- **inconsistent management practices and poor leadership at the Centre, since the resignation of the then General Manager in July 1999;**
- **lack of operational procedures, guidelines and on-job support and staff training;**
- **budget constraints and shortages of experienced staff; and**
- **poor prison design, restricting the overall functionality of the prison, which was compounded by the increase in the prisoner population which exceeded its original capacity.**

3.4.46 Following publication of the State Coroner's findings into the significant number of deaths in private prisons during the late 1990s, an independent review of Victoria's prison system was established by the Government. The findings of that review were outlined in a report titled *Report of the Independent Investigation into the Management and Operations of Victoria's Private Prisons,* October 2000. The key findings and recommendations outlined in the report included:

- there is little scope to increase the flexibility of contracts;
- performance measures specified in the current prison contracts are inadequate in gauging performance;
- recruitment, selection and training of custodial staff needed strengthening;
- prisoner health services are particularly fragmented; and
- programs such as rehabilitation of prisoners should be improved.

Decision taken by the Government to step-in

3.4.47 **The Report by the Commissioner on 13 September 2000 indicated that the defaults were persistent and continuing in nature, and that the operator could not ensure the safety and wellbeing of prisoners, staff and visitors.** On receiving that Report, the State Government sought advice on its legal position from the Government Solicitor and other legal consultants. The advice provided indicated that in dealing with performance issues, due process had been followed by the Department and that the operator had been provided with sufficient opportunity to remedy the contractual breaches.

3.4.48 Following receipt of the advice, the Minister concluded that the situation at the Centre represented an emergency. After consultation with the Premier and Treasurer, the Minister then proceeded to appoint an administrator to take over the Centre's operation in accordance with section 8F of the *Corrections Act* 1986, and section 27B of the PSA.

3.4.49 On 3 October 2000, *Step-In Notices* were served, advising the contractor that an administrator from the Public Correctional Enterprise (CORE), within the Department of Justice, had been appointed to manage the Centre in place of the existing operator.

3.4.50 Immediately after *Step-In Notices* were issued, the Government commenced negotiations with the contractor to achieve a mutually agreed termination of the contractual arrangements. The contractor, having acknowledged the performance failures raised by the Commissioner, requested a negotiated settlement of the contractual arrangements. The Government favoured this proposition as it ensured a commercial settlement was reached with the contractor and avoided a prolonged legal dispute that could have exposed the Government to litigation.

3.4.51 Prior to the commencement of negotiations, the Premier, the Treasurer and the Minister endorsed Terms of Reference for the negotiations and the establishment of a Steering Committee (comprising senior representatives from the Departments of Justice, Premier and Cabinet, and Treasury and Finance) and a negotiation team (comprising senior officers from the Departments of Justice, and Treasury and Finance).

3.4.52 **On 2 November 2000, the Government reached an agreement with the contractor to transfer the ownership and management of the Centre to the public sector. The settlement amount was $20.2 million, consisting of $17.8 million to purchase the Centre's buildings, infrastructure and chattels and $2.4 million to finance the costs associated with terminating the loan facility. This amount was $1.3 million below the market value of the Centre, estimated by 2 independent valuers commissioned by the Valuer-General.**

3.4.53 The agreed settlement included a $14.8 million payment to the project financier to pay-out the contractor's existing loan facility and relinquish a performance bond of $125 000 held by the Department.

3.4.54 The settlement package also recognised an amount of $1.2 million in direct costs incurred by the State as part of the step-in and administration of the facility. These costs included:

- $740 000 for consultants to provide advice on legal, financial and accommodation matters;
- $184 000 for the security services prior to the step-in; and
- $275 000 for urgent maintenance required at the Centre.

3.4.55 The settlement package did not contain compensation to the contractor for loss of business, profits or damage to its reputation.

Causes of the problems facing the Centre

3.4.56 This section of the Report provides an outline of what audit considers were the major causes of the problems experienced by the Department in outsourcing the construction and operation of the Centre. It is hoped that the provision of this information will provide other government agencies contemplating the outsourcing of public goods and services in the future with a number of valuable lessons.

Contracting-out the provision of social services

3.4.57 Our May 1999 *Report on Ministerial portfolios* indicated that although the Government has the right to determine how government services are to be provided, the ultimate responsibility for the provision of these services remains with the Government. In the case of prison services, the operation of the prison system and the duty of care to prisoners remains with the Government regardless of how the services are provided. These sentiments were also expressed by the Commissioner in a paper presented to the State Government Business Symposium 2000 titled *Managing Commercial Contracts: A Practitioners View*. The paper commented:

> *"The Government of the day, regardless of its political persuasion or policy position, retains a basic non-negotiable duty of care responsibility on behalf of the community which cannot be transferred to a private operator, in order to ensure that prisoners are treated humanely and decently and given every opportunity to return to that society after release from custody better able to reintegrate successfully into the community, no matter what the contractual arrangements may be."*

3.4.58 In these circumstances, it is imperative that considerable effort is made in selecting a contractor who understands the nature and standard of services required, is willing to deliver on the spirit and intent of the agreement (rather than the detail outlined in the contract), and will promptly and appropriately respond where services provided fall short of the Department's expectations. The only arrangement that can be effective in this environment is a partnership where both parties have a mutual understanding and respect for one another.

3.4.59 Audit acknowledges that once the Department had decided to use a private sector provider, the complexities, multi-service requirements and variable nature of the correctional services tendered made it difficult to construct an agreement which would ensure the effective provision of these services. Furthermore, audit agrees with the Department's view that an overly prescriptive contract and tender specification, detailing exactly how services are to be delivered, would have stifled the tenderers' use of innovative service delivery options. However, audit considers that the contract and tender specifications should have specified the broad services required and the objectives or expectations of the Department in respect of these services.

3.4.60 It is now evident that the contractor and operator failed to deliver on some basic correctional services which were not specifically outlined in the contract such as prison and rehabilitation programs, and in other circumstances the services they provided were clearly inadequate, such as in the areas of supervision of prisoners, health services and maintenance of prison facilities.

Inadequate contract price

3.4.61 Due to the long-term nature of the outsourcing arrangement and the significant infrastructure investment by the contractor, it was imperative that the amount paid by the Department to the contractor for the provision of accommodation and correctional services was sufficient to provide both the quality and quantity of services required, and provide an adequate return on investment for the service provider.

3.4.62 However, from the numerous internal and external reviews of the prison, it is evident that the price negotiated for the provision of prison services was too low. The ongoing staff shortages, lack of adequate maintenance work carried out on the facilities and absence of staff training programs at the Centre may be indicative of an inadequate purchase price.

3.4.63 In contracting-out prison services, the then Government had an agenda to fast-track private sector involvement in the delivery of prison services and to reduce the costs of these services to the government. This initiative to reduce costs, through the outsourcing of government services, was driven centrally by the Department of Treasury and Finance, which established the Statewide financial benchmark which all outsourcing arrangements were required to meet in order to obtain government approval. **In response to the Government's drive for significant cost savings from outsourcing, the Department of Justice, in selecting a service provider, placed considerable emphasis on the financial evaluation criteria used to ensure cost savings and less emphasis on the capacity of the contractors to effectively manage and operate the facility.**

3.4.64 As indicated earlier in this Report, one of the 3 tenderers was eliminated because that tenderer's bid exceeded the Government's financial benchmark and a major reason for the elimination of a second tenderer was due to that tenderer's unwillingness to accept the transfer of risks proposed by the Department without further monetary reward.

3.4.65 The successful tender was 15 per cent less than the financial benchmark price set by the Department, with the benchmark approximating the costs incurred to provide the services internally.

3.4.66 In addition, these arrangements transferred a significant amount of the financial risk to the private sector, for which the contractor would need to be compensated and the payments made to the contractor needed to include an amount to provide a return on the contractor's investment.

3.4.67 Although there were likely to be inefficiencies in the internally provided services, the fact that the contractor was willing to provide these services at a discount (compared with the costs of internally providing the services) should have made the Department question the adequacy of the price tendered. However, there is no evidence of any such questioning of the tender price.

3.4.68 From a tender evaluation perspective, given that the majority of the operators costs related to staff payments, it would have been prudent to specify or at least request details of staff-to-prisoner ratios in the tender negotiations. The Department chose not to do this, as it considered that such an action might stifle more innovative approaches to prison management. The danger of not requiring indicative staff-to-prisoner ratio is that the contractor's tender price may be set at an unsustainably low price in order to win the contract.

3.4.69 Where a generic product is purchased on a short-term contract, in a market with multiple service providers and where no significant infrastructure investment is involved, obtaining the lowest possible purchase price is likely to be prudent. However, as indicated earlier in this Report, given the unique nature of prison operations, it was imperative that the contract price accepted was sufficient to enable the contractor to provide the quantum and quality of services required by the Department. **Where the contract price has been set too low, and given that one of the objectives of the contractor was to generate a profit, it is not surprising that the standard of service provided by the contractor was adversely affected.**

3.4.70 Recognising that the Centre's contractual arrangements lacked sufficient detail to ensure an adequate standard of service, the subsequent contracts for the 2 private male prisons (Port Phillip Prison at Laverton and Fulham Correctional Centre at West Sale), were more explicit in terms of prisoner management requirements including issues such as staff selection and training, and staff deployment.

Inadequate knowledge and experience

3.4.71 A major cause of the problems impacting on the prison was the absence of sound management and leadership within the senior administration of the prison, and a general lack of experience among prison staff.

3.4.72 At the time of tendering, the Department knew the successful tenderer's recruitment policy did not provide for the engagement of staff currently working in the corrections system. As a result, many staff employed by the contractor lacked experience in the corrections industry. To what extent the Department took this knowledge into account in selecting the successful tenderer is unclear.

Assessment of service delivery options

3.4.73 A basic function of most, if not all correctional services is to provide facilities and programs for the containment and rehabilitation of prisoners. Any decision on how these services should be provided would normally be based on an economic appraisal of the various service provision options. This would involve a systematic weighing up of the costs and benefits (both financial and non-financial) of alternatives, including the internal and external provision of these services.

3.4.74 However, as a result, the government's desire to have private sector involvement in the delivery of prison services, no economic appraisal of alternative options was undertaken.

3.4.75 **Audit acknowledges the Government's right to determine how public goods and services are delivered. However, in the absence of an economic appraisal there was insufficient information at the time of outsourcing, to enable the Government to make an informed decision on whether this form of service provision provided the most cost-effective outcome for the State or to enable the Department to properly assess the adequacy of private sector tenders.**

Flexibility of contractual arrangements

3.4.76 Correctional services are not only a complex area, but also one that is continually changing. For example, in the last few years there has been an unforeseen increase in the number of women prisoners and the profile of these prisoners has changed significantly, which has, in turn, impacted on the proportion of maximum security, protection prisoners and drug-related offenders accommodated in special units.

3.4.77 The contractual arrangements for the provision of accommodation and correctional services are also extremely detailed and complex in nature, making it very difficult for the Department to initiate changes quickly in response to changing circumstances. A number of the problems faced by the Department resulted from its inability to initiate action to quickly address these changed circumstances.

Enforcing the contract

3.4.78 In any contractual arrangement, the extent to which disputes over performance can be resolved will depend on the nature and quality of the contractual arrangements and on how well the contract is managed while in dispute.

3.4.79 Once the Centre's contract was in default, the absence of dispute resolution process definition within the Agreement and the lack of legal precedent in respect of similar contracts, led to considerable uncertainty regarding the process by which the Government could issue default notices and ultimately remove the operator. As a result, the Government did not have sufficient assurance that the processes followed to seek remedial action from the contractor and the subsequent step-in, were appropriate and did not expose the Government to other risks.

3.4.80 In respect of the lack of guidance in the contract, the PSA did not provide:

- A definition of what constituted a default;
- Guidance on the format of the default notices, including the language used and detail required;
- Details of the process required to be followed to terminate the contract, which forced the Government to tolerate a period of poor performance (in order to provide a basis for terminating the contract and enable the Government to demonstrate that due process had been followed) before action was taken to remove the operator; and

- The PSA did not provide sufficient clarity regarding the power of the Secretary of the Department, in the selection of a private prison's General Manager. (Although the Secretary is required to approve the employment of any perspective employee by a private prison, and therefore has a right to veto an appointment, there is no clear right for the Secretary to be involved in the selection process for a new General Manager.)

3.4.81 In recognition of the shortcomings of the Centre's PSA, the agreements subsequently developed for the other private prisons offered more specificity about defaults and performance arrangements in the contract. These agreements provided greater detail and definition regarding default regimes and the default cure arrangements.

3.4.82 It is also worth noting the different approaches taken by the Victorian and Western Australian Governments in developing contractual arrangements for private prisons. Specifically, Western Australia's contractual arrangements:

- make termination available for any default under the contract, whereas in the Centre's PSA the range of defaults enabling termination was narrower;
- allow the State to issue a default notice where there has been a degradation in performance even though it does not constitute a default;
- provide that, any failure to comply with the agreement would constitute a default, whereas, in the Centre's PSA there were certain situations where such a failure would not constitute a default; and
- more broadly define defaults to cover all non-compliance with the contract and the law.

3.4.83 **The weaknesses in the Centre's contractual arrangement, especially in respect of the lack of clarity regarding the rights and obligations of the respective parties and the dispute resolution process, left the Department exposed to risk. Despite this situation, the Government was able to terminate the contract on favourable terms to itself, while at the same time avoiding a prolonged legal dispute with the contractor through negotiating a commercial settlement amicable to both parties.**

3.4.84 Audit considers that the contractor's decision not to contest the termination of the arrangement or to pursue litigation in the courts, was likely to have been influenced by:

- the evidence indicating poor management of the Centre was overwhelming;
- the delicate and difficult task of dealing with a non-performing contract was soundly managed by the Department; and
- the contractor, as a significant supplier of private prisons worldwide, was motivated by the desire to protect its reputation.

Performance-linked payments

3.4.85 In order for the performance-linked payments included in the contract to be effective in influencing the contractor's behaviour, there needed to be a rigorous evaluation of the contractor's performance against well-defined outcomes built into the contractual arrangements.

3.4.86 As indicated in our May 1999 *Report on Ministerial Portfolios*, the service delivery outcomes used as a basis for paying the contractor's performance-linked fees, were deficient in that they were:

- Based on outcomes achieved in outdated prisons identified for replacement. For example, the service delivery outcomes for self-mutilations, assaults and positive drug test results were based on the highest rates recorded in the existing prison system at that time. As a result, the outcomes did not place any expectation on the contractors to improve on minimum standards or adopt best practice;
- Essentially quantitative in nature. There are no qualitative indicators in place to measure the effectiveness of many prison programs, such as drug treatment programs for prisoners;
- Focused on short-term achievements. For example, service delivery outcomes did not include the quality or effectiveness of staff recruitment and training; and
- Did not address some key areas of prison operations. Areas such as rehabilitation and visit arrangements and activities to strengthen family links were not included in service delivery outcomes.

3.4.87 In addition, if performance-linked payments are to be effective in influencing the contractor's performance, these payments should also be of significant value to provide the operator with an incentive to achieve the stipulated outcomes, and only be paid for good performance.

3.4.88 Unfortunately the annual performance-linked payments, representing less than 5 per cent of the total aggregate annual payments payable to the contractor, were not large enough (relative to the costs associated with rectifying the problems facing the Centre) to influence the contractor's behaviour.

3.4.89 This situation was compounded by the structure of the arrangements, which allowed a contractor who was not performing to a high standard or was performing badly in a number of key areas, to still receive the full, or a substantial proportion of the annual performance-linked payments.

3.4.90 **In these circumstances the performance-linked payments were never likely to be a suitable mechanism for encouraging effective service delivery.**

Ongoing operational costs of the Centre

3.4.91 Since the commencement of the contract in August 1996, the State has paid the contractor a total of $39.7 million in fees and charges for managing and operating the Centre as specified in the contractual arrangements. Details of these costs are provided in Table 3.4E

TABLE 3.4E
TOTAL PAYMENTS MADE TO THE CONTRACTOR BETWEEN 1996-97 AND 2000-01
($'000)

Fee/charge	*1996-97*	*1997-98*	*1998-99*	*1999-00*	*(a) 2000-01*	***Total***
Correctional services fee	4 408	5 638	5 887	6 968	2 741	**25 642**
Accommodation services charge	2 291	3 003	2 930	2 915	939	**12 078**
Performance-linked fee	-	551	620	551	301	**2 023**
Total *(b)*	**6 699**	**9 192**	**9 437**	**10 434**	**3 981**	**39 743**

(a) Represents the period July-October 2000.
(b) In addition to the above, the Centre was allocated approximately $380 000 per annum for government-sponsored programs (e.g. under the Turning the Tide initiative the Centre was allocated $320 000 from the Community Support Fund to address drug issues, while $60 000 was allocated for therapeutic care programs).

3.4.92 The Department's total base budgeted expenditure for the contractor during the 2000-01 financial year was $10.9 million. However, following the Government take-over of the Centre, this budget required adjustment, and an additional $2.4 million to finance the costs associated with terminating the loan facility with the Centre's financier.

3.4.93 As the full transition of the Centre to the Government had not occurred at the date of preparation of this Report, the anticipated total costs to government for the 2000-01 financial year had not been fully determined. However, a number of additional costs have resulted from the new arrangement including:

- higher staffing costs of around $3 million per annum, stemming from an increase in staffing levels at the Centre and transferring the majority of the operator's custodial and administration staff to government employee awards;
- additional costs for the provision of health services, estimated to increase by $1.5 million per annum; and
- around $600 000 increase per annum in the Centre's WorkCover premium, as a result of its recent poor performance.

3.4.94 **The total costs incurred by the Government between 1 July 2000 and 28 February 2001 in respect to the Centre were $33.6 million, some $22.7 million higher than that provided in the State Government's 2000-01 budget. This additional amount includes capital costs of $17.8 million for the acquisition of the Centre's physical assets, and $4.9 million representing costs associated with assuming responsibility for management of the Centre and rectifying problems identified.**

Current status of prison arrangements

3.4.95 Since taking over the operations of the Centre, the Department has conducted a series of reviews and developed strategies to address a wide range of deficiencies including security, health services, prisoner programs, accommodation, prisoner industries, IT systems, and staff recruitment and training. The Commissioner is of the view that the prison has stabilised and the performance is consolidating, despite the prison continuing to experience a number of serious incidents. This view was outlined in the Commissioner's quarterly prison performance report, which stated:

> *"CORE's [the Public Correctional Enterprise] responsiveness, professionalism and commitment demonstrated in the intervention is to be commended. The subsequent feedback from shareholders in relation to the operation of the Centre has been positive, especially in respect of the increased participation of prisoners in programs and improved health services. However, notwithstanding the achievements made in the short period of time, there have been a significant number of incidents at the prison since step-in. The Commissioner is of the opinion that the frequency and nature of these incidents suggests that they are in part indicative of anxieties created by the changeover. However, they are also a feature of the dynamics of a maximum security reception prison."*

3.4.96 The Commissioner has indicated to audit that strategies introduced by the Department represent a major undertaking that should result in a considerable improvement in the delivery of prison services at the Centre over a number of years.

3.4.97 Based on discussions with the Department, the Government is satisfied that the remaining 2 private prisons, the Rural Men's Prison at Fulham near the City of Sale and the Metropolitan Men's Prison at Laverton North, are operating in compliance with legislative and contractual requirements.

3.4.98 In respect of the 2 remaining private prisons, the Government is entitled to review the respective contracts, with a view to improving their effectiveness and has the opportunity to re-tender for the operation of the private prisons. If tenders are to be called, the review process provides for a 2 month period in which the incumbent contractor may submit an offer to the Minister for the provision of correctional services for a further term of 3 years. This process provides the contractor with the right to exclusive negotiations with the Minister during that period.

3.4.99 If the Minister accepts the contractor's offer, the contract does not require the Department to go through a tender process. Alternatively, if he rejects the offer he can initiate the new tender process at his discretion. The initial term of the remaining PSAs for these 2 prisons will expire between mid to late 2002, at which time the Government expects to review the respective agreements.

3.4.100 **As part of this review process, the Department should endeavor to provide better guidance, within the PSAs, on the form of Default Notices and the processes that should be followed, in the event that the Government may need to terminate the agreement and assume control of a prison.**

RESPONSE *provided by Secretary, Department of Justice*

In general, the Report provides a balanced review of the financial and operating arrangements that were in place between the contractor and the Government for the management of the Centre. The review of the process on the decision taken by the Government to return the Centre to public ownership and management is also considered to be accurate and a true reflection of the processes undertaken.

ESTATE AGENTS GUARANTEE FUND

3.4.101 Following a review of the real estate industry in the 1978-79 financial year, the former Estate Agents Board was established under the *Estate Agents Act* 1980, with responsibility for:

- licensing all sub-agents, estate agents and corporations operating in Victoria which deal in the real estate industry;
- promoting the interests of the public and the real estate industry by encouraging high standards of estate agency practice; and
- providing housing assistance in accordance with section 76 of the *Estate Agents Act* 1980.

3.4.102 The Board was a self-funding body, which generated income from licence fees paid by estate agents, interest received from financial institutions on balances held on behalf of estate agent's trust accounts and interest on investments. This income was paid into the Estate Agents Guarantee Fund.

3.4.103 Income generated by the Board was used to:

- meet its operating costs;
- compensate members of the public who had suffered financial loss by reason of misappropriation or defalcation of their moneys while held on trust by estate agents;
- assist in housing programs which encourage home ownership; and
- assist in the education of the public and the industry in real estate practice and procedures.

3.4.104 The Board operated until it was dissolved on 1 February 1995, following amendments to the Act in October 1994. Those amendments also established the following 3 new regulatory bodies within the former Office of Fair Trading and Business Affairs (now Consumer and Business Affairs Victoria) within the Department of Justice:

- Estate Agents Licensing Authority, which acquired the administrative and licensing functions of the former Board, including the management of the Fund;
- Estate Agents Disciplinary and Licensing Appeals Tribunal, which acquired the quasi-judicial functions of the former Board; and
- Estate Agents Council, which has responsibility for policy and advisory matters.

3.4.105 Following the change in legislation, responsibility for reporting on the operation of the Fund was transferred to the Secretary of the Department of Justice and details of the operations and financial position of the Fund were incorporated into the Department's annual financial report.

3.4.106 With the passing of the *Tribunals and Licensing Authorities (Miscellaneous Amendments) Act* 1998, the Estate Agents Licensing Authority was abolished and its responsibilities were absorbed by the newly formed Business Licensing Authority. That Act also abolished the Estate Agents Disciplinary Tribunal and Licensing Appeals Tribunal, with their responsibilities transferred to the Victorian Civil and Administration Tribunal (VCAT).

Trust funds administered by Consumer and Business Affairs Victoria

3.4.107 In addition to the Estate Agents Guarantee Fund, Consumer and Business Affairs Victoria (CBAV) administers 6 other trust funds. The combined assets of these funds at 30 June 2000 amounted to some $318 million. Details of the respective fund balances, the legislation establishing them, the source of trust income and purposes for which trust funds can be expended are outlined in Table 3.4F.

TABLE 3.4F
DETAILS OF TRUST FUNDS ADMINISTERED BY CBAV

Fund	*Act of Parliament*	*Balance at 30 June 2000 ($'000s)*	*Source of income*	*Expenditure purposes*
Residential Tenancies Bond Account and Investment Income Account	*Residential Tenancies Act* 1997	196 351	• Interest on investments	• Administration of the Fund • Transfers to Residential Tenancies Fund
Estate Agents Guarantee Fund	*Estate* Agents Act 1980	100 078	• Interest on estate agent's trust accounts • Interest on investments • Licensing fees • Fines	• Operation of the Estate Agents Council • Tribunal grants • Guarantee claims • Administration of the requirements of the Act
Residential Tenancies Fund	*Residential Tenancies Act* 1997	19 696	• Transfers from Residential Bonds Investment Income Account • Interests on investments • Tribunal fees • Interest on individual bond trust accounts	• Tribunal costs • Payments for Research and education permitted by s.495 of the Act • Administration of the requirements of the Act
Domestic Building Fund	*Domestic Building Contracts and Tribunal Act* 1995	1 467	• Building registration fees collected by the Building Control Commission • Income on investments • Tribunal fees • Fines	• Tribunal costs • Grants permitted by s.124(3)(d) of the Act • Administration of the requirements of the Act

TABLE 3.4F
DETAILS OF TRUST FUNDS ADMINISTERED BY CBAV *- continued*

Fund	*Act of Parliament*	*Balance at 30 June 2000 ($'000s)*	*Source of income*	*Expenditure purposes*
Motor Car Traders Guarantee Fund	*Motor Car Traders Act* 1986	907	• Interest on investments • Licensing fees • Fines • Recovery of claims paid	• Guarantee claims • Administration of the requirements of the Act
Consumer Credit Fund	*Credit (Administration) Act* 1984	824	• Credit provider contributions • Interest on investments	• Grants permitted by s.86AB of the Act • Administration of the requirements of the Act
Prostitution Control Board Fund	*Prostitution Control Act* 1994	265	• Licensing fees • Fines	• Administration of the requirements of the Act

3.4.108 With the exception of the Residential Tenancies Bond Authority, which produces annual financial reports that are subject to audit and tabled in the Parliament, the financial operation and position of the other trust funds outlined by the above table are included within the Department of Justice's annual financial report. However, due to the size and diversity of the Department's financial operations there is a lack of transparency over the other trust funds' activities.

3.4.109 **In order to improve the level of accountability over trust fund moneys, it is recommended that separate annual financial reports be produced for each of the major trust funds administered by the Department.**

Operations of the Estate Agents Guarantee Fund

3.4.110 The Estate Agents Guarantee Fund's income in the 2000-01 financial year was derived from the same sources as the predecessor Board, that is from:

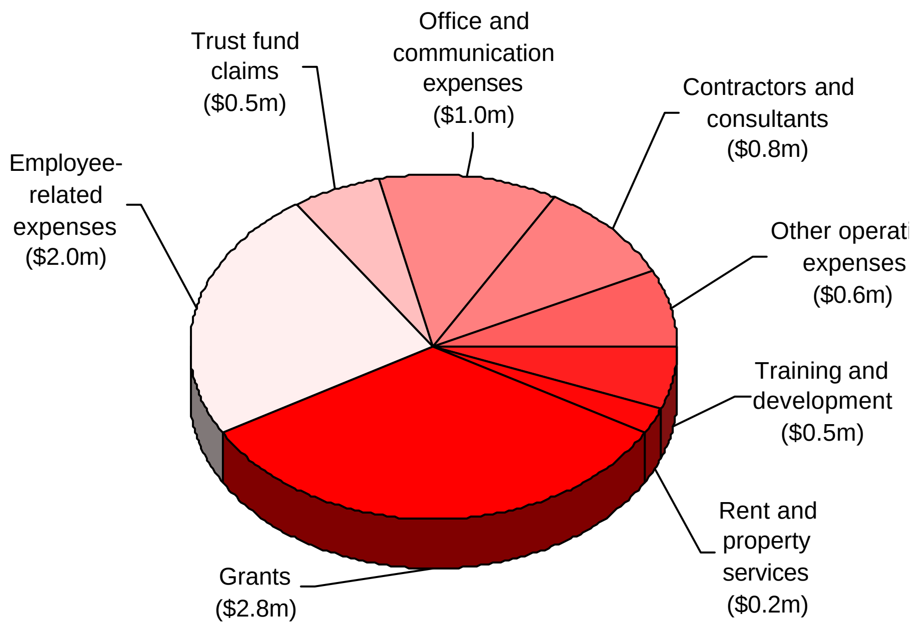
- licence fees ($1 million);
- interest received from financial institutions on balances held by them on behalf of estate agent's trust accounts ($20 million); and
- interest on investments ($7 million).

3.4.111 All interest generated from real estate agent trust accounts (which is primarily generated on deposit moneys paid to agents in respect of the purchase of real estate) is paid into the Fund. However, in many of the larger property sales, deposits are paid by the purchaser into a joint trust account in the names of both the purchaser and seller. In these circumstances, the interest on these deposits is not paid into the Fund.

3.4.112 The income generated by the Fund is used for the same purposes as it was by the previous Board, with the exception of assistance to housing programs that encourage home ownership, the funding of which was removed following the 1994 amendments to the Act. In the 1999-2000 financial year, 143 claims for compensation totalling $300 000, were paid from the Fund. Of these claims, 87 were in respect of security deposits, 52 related to rental moneys, 2 involved sales deposits and 2 were concerned with other matters.

3.4.113 Chart 3.4G outlines how the Fund's income is expected to be distributed in the 2000-01 financial year.

CHART 3.4G
ESTATE AGENTS GUARANTEE FUND BUDGETED EXPENDITURE, 2000-01
($million)



3.4.114 **As illustrated by the chart, approximately $8.4 million is anticipated to be expended from the Fund during the year. This is significantly less than the $28.4 million in revenue expected to be generated by the Fund, resulting in a budgeted surplus of almost $20 million for the 2000-01 financial year. Similar surpluses have been recorded by the Fund over a number of years, with the net assets held in the Fund increasing from $46.6 million as at 30 June 1997 to $99.9 million as at 30 June 2000, an increase of $53 million or on average $17.7 million per annum.**

3.4.115 Looking at the future operating performance of the Fund, with the value of real estate increasing over time, deposits and Fund income are likely to continue to increase into the future. The size of this increase in income will be even greater if interest rates rise in the future.

3.4.116 On the expenditure side there is little scope for the Fund surplus to be significantly reduced through grant payments, with the Fund making around 8 payments per annum over the last 3 years, with payments averaging $300 000 in each of those years. Other major costs, such as those associated with administrating the Fund and compensation payments are also expected to remain at their current levels in the foreseeable future. The combination of these factors is likely to result in a continuation of the increase in the balance of moneys held in the Fund.

3.4.117 Initiatives undertaken by the Department, such as publicly advertising the availability of funds and the criteria for grant approval does not seem to have encouraged an increase in grant applications. It would appear that the criteria established in the Act for grant payments may be set too narrowly to enable the Department to increase the number of grant payments and accordingly reduce the Fund's surplus.

3.4.118 **In these circumstances, the Parliament could consider amendments to the Act in order to broaden the criteria for grant payments.**

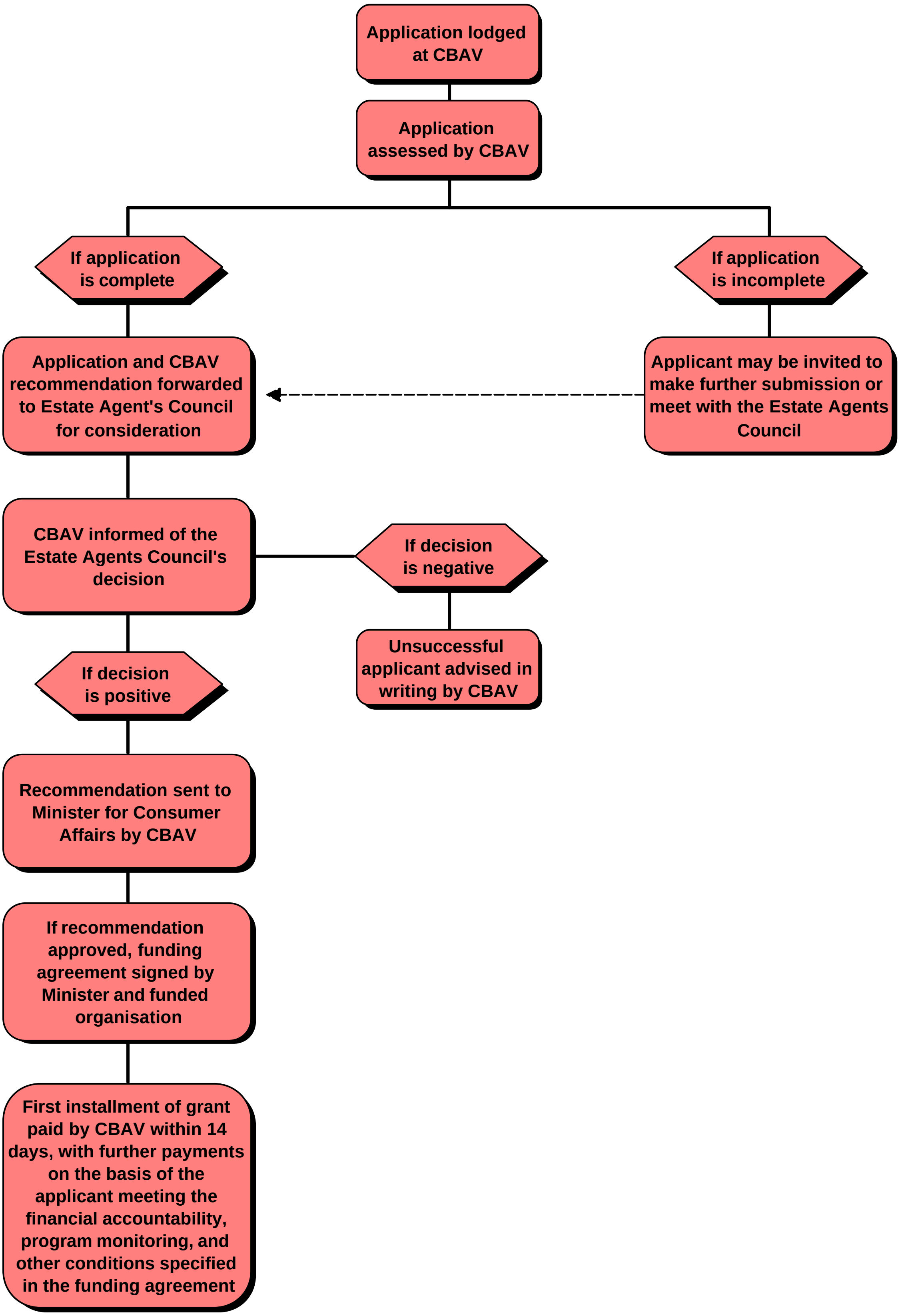
Grant payments

3.4.119 Under section 76(3) of the Act, the Minister, after consultation with the CBAV and the Estate Agents Council, may approve grants from operating surpluses held by the Trust for one or more of the following purposes:

- community education programs relating to the sale, purchase or lease of real estate or businesses;
- programs that promote the ownership of real estate;
- training of estate agents and agents' representatives;
- promoting the mediation or conciliation of disputes between estate agents and the public;
- reviewing or reforming the law and procedures concerning the lease or transfer of interests in land and;
- projects facilitating the registration of interests in land or compilation of other information relating to the ownership of land.

3.4.120 The process for applying for, and approval of, grants is outlined in Chart 3.4H.

CHART 3.4H
ESTATE AGENTS GUARANTEE FUND,
GRANT APPLICATION AND APPROVAL PROCESS



3.4.121 The timing of the grant payments is dependent on the amount of the grant. CBAV guidelines provided to grant applicants indicate that grants of up to $20 000 will usually be paid in full and in advance, while payments of grants in excess of $20 000 will be made in 2 parts.

3.4.122 Table 3.4I below summarises grants made from the Fund over the 3 years from 1997-98 to 1999-2000.

TABLE 3.4I
SUMMARY OF GRANTS FROM THE ESTATE AGENTS GUARANTEE FUND, 1997-98 to 1999-2000

Recipient	*Number of grants*	*Total value of grants ($)*	*Purpose of grants*
The Real Estate Institute of Victoria (REIV)	15	2 114 603	Provision of professional education programs for real estate agents and representatives, and free homebuyers seminars and investment seminars to the public.
Land Victoria, Department of Natural Resources and Environment	2	4 871 000	Improving the accessibility and quality of land valuation data and information held on real estate in Victoria.
Credit Helpline	2	98 470	Establishment of a telephone advisory service providing information on the type and availability of credit available for the purchase of property.
Paraplegic and Quadriplegic Association of Victoria	1	54 980	Development and part-funding of the delivery of a short course designed to educate real estate agents on the special accommodation requirements of people with disabilities.
Victorian Stock Agents' Association	1	20 390	Development and presentation of a course for real estate agents and representatives involved in selling and managing rural real estate.
Office of Housing, Department of Human Services	1	50 100	Support to Group Self-Build and Shared Equity Programs.
Ecumenical Housing	1	30 640	Development of a community housing training program.
Total	**23**	**7 201 083**	

3.4.123 As disclosed in the above table, the recipients of the 2 largest quantum of grants were the REIV and Land Victoria. The grants provided to the REIV included an amount of $69 000 for the gathering and analysis of property sales data to prepare profiles on selected Victorian municipalities. This grant formed part of a larger $568 000 grant to the REIV under an omnibus funding agreement. The first half of the funding provided under this agreement ($284 000) was paid to the REIV in November 1997, with the remainder provided in May 1998. In April 1999, the REIV realised it did not have the resources to proceed with the property sales data program and returned $69 000 to CBAV.

3.4.124 CBAV has advised that separate funding agreements are now used to fund individual projects. In addition, although not formally stated in the guidelines for grant applications, the payment of large grants (generally in excess of $100 000) is now made progressively, based on the cash flow requirements of the project. CBAV is also considering the payment of smaller grants, in excess of $20 000, in 4 parts as opposed to 2 parts as currently is required by the guidelines.

3.4.125 **It is recommended that CBAV guidelines be updated to reflect current grant payment practises. In addition, projects for which grants have been approved must continue to be actively monitored and assessed to ensure that the grant money is either used for its intended purpose or refunded on a timely basis.**

Grants provided for training

3.4.126 One of the areas outlined in the Act as appropriate for the use of the Trust money is the training of real estate agents. Although the Act does not draw any distinction, there are basically 2 types of real estate agent training:

- training that directly benefits the clients of real estate agents; and
- training that would normally be undertaken by the real estate profession, to improve the skills and knowledge of its staff.

3.4.127 Our review disclosed that real estate training, funded by grants from the Fund included training in:

- conduct of auctions;
- property management;
- quality assurance;
- business risk management;
- sales; and
- other specialised workshops.

3.4.128 From the above list it can be seen that the Trust moneys have been used to provide training that any professional organisation would be required to provide to its staff.

3.4.129 Although not explicitly outlined in the Act, the intention of Parliament when drafting the criteria for grant payments was more likely to fund real estate agent training which directly benefited the clients of real estate agents, rather than the general professional development activities of agents.

3.4.130 **It also seems unusual that the Trust moneys have been utilised on a number of occasions to meet the costs associated with professional training of real estate agents, while funding has not been provided for the training and development of other professionals working in the real estate industry such as solicitors, conveyancing agents and financial advisors.**

Natural Resources and Environment-funded projects

3.4.131 In late 2000, the CBAV received an application from the Department of Natural Resources and Environment (NRE) for a grant of $30 million (over 3 years) to implement some key aspects of the government's property online initiative. Funding was requested for 6 separate projects, the details of which are disclosed in Table 3.4J.

TABLE 3.4J
PROPOSED NRE PROJECT FUNDING

Project	*Purpose of funding*	*Funding ($million)*
Streamlined planning through electronic applications and referrals (SPEAR)	An e-commerce system that will facilitate processing of planning, building and subdivision applications using the electronic transfer of information via the internet.	10
E-Conveyancing (ECV)	Allowing solicitors and others involved in conveyancing to obtain their land information requirements and complete their conveyancing contracts via the internet. This project will also enable electronic lodgment of titles information and immediate registration of interests in land.	5
Land Information Management System	Provide access to information on the status of Crown land and enable transactions involving the use of Crown land to be completed electronically.	5
Crown Land Status Online	An authoritative database of Crown land parcels, accessible on-line.	2
Survey	Facilitate changes to the survey function and surveyor registration, and provision of continuing education programs to surveyors.	6
Standard parcel identifier	Providing a link between disparate land parcel datasets, which will enable Vicmap to be used as a complete and unambiguous map based entry point for land information or transactions.	2
Total		**30**

3.4.132 In its proposal, NRE contends that each of these projects fall within the approved purposes outlined in section 76 of the Act, that is the projects are concerned with *"reviewing or reforming the law and procedures concerning the lease or transfer of interests in land"* and *"facilitating the registration of interest in land or compilation of other information relation to the ownership of land"*.

3.4.133 The NRE submission indicated that the projects would provide significant benefits to the Government, industry and consumers, including:

- reduction in the time taken to transact land dealings;
- generation of efficiencies within government, such as the provision of automated information on the status of Crown land for Native Title claims;
- provision of on-line access to integrated property data and simplification of property transactions;

- lower statutory charges for property transactions reflecting reduced costs to government, electronic lodgement of property transactions and subdivision plans; and
- increased professional competency of land surveyors and greater certainty in respect of title boundaries, resulting from reforms to the surveying profession.

3.4.134 At the date of preparation of this Report a decision on the approval of the proposed $30 million in funding had not been made. As indicated earlier in this Report, NRE received 2 grants from the Fund in the last 3 years for projects associated with the automation of the Titles Office records, totalling $4.87 million.

3.4.135 **The projects included in the NRE application will clearly benefit the community and are likely to meet the criteria for approval under the Act. However, the Government, through NRE, has responsibility for the provision of accurate, reliable and accessible information to the public and the real estate industry, regarding land boundaries, interests, valuations and other land related data. Therefore, the use of grant moneys to fund the provision of basic government services could be seen as an inappropriate use of Trust Fund moneys.**

***RESPONSE** by the Secretary, Department of Justice*

Trust funds administered by Consumer and Business Affairs Victoria

It is agreed that the level of accountability over trust funds be increased by greater transparency in the annual reporting on the funds. This would be achieved by the inclusion in future CBAV annual reports tabled in Parliament of key financial information on revenue, expenditure, assets and liabilities.

Grants payments

The Government is considering proposing amendments to the Act to broaden the criteria for grant payments.

Guidelines for disbursement of EAGF grants will be updated, and approved grants will continue to be actively monitored and assessed to ensure that grant money is either used for its intended purpose or refunded on a timely basis.

Grants provided for training

Section 76(3) of the Estate Agents Act 1980 specifically provides for the making of grants for projects relating to the training of estate agents and agents' representatives. Specific provision for the training of other professional groups is not made in the Act, but applications of the training of other professional groups would be considered against the various criteria for the approval of grants that are set out in s.76(3) of the Act.

Natural Resources and Environment-funded projects

Grants from the EAGF have been approved to government bodies where the purpose of the grant complies with the provisions of the Act, and there is clear public benefit in the project proposed for funding. In relevant cases, the Minister for Consumer Affairs would consult with other relevant Ministers before approving grants to other government departments. The particular application referred to will now not be funded in 2001-02.

RESPONSE *by the Secretary, Department of Natural Resources and Environment*

Natural Resources and Environment funded projects

The automation of freehold titles has been fully funded by the Government, with an additional $30 million provided in the 2001-02 State budget to bring total government funding of the Titles Automation Project to over $90 million.

Successive Governments have funded the establishment of the State's land information infrastructure and the State's fundamental datasets. Land Victoria's current $30M EAGF application mainly concerns projects which leverage-off this government investment in basic services.

Land Victoria's current EAGF application identifies the major beneficiaries of the projects as the property industry and consumers. An independent appraisal of these projects identified benefits to industry of over $220 million per annum, which will in turn be passed on to consumers through lower prices and more timely services. As these benefits accrue to the property industry and consumers, it is seen as appropriate for the EAGF to be used for these projects.

SCHEDULE A
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS

Report	*Subject*	*Status at date of preparation of this Report*
	MATTERS RESOLVED OR ACTION COMMENCED	
DEPARTMENT OF JUSTICE		
Infants Investment Trust Accounts		
Ministerial portfolios, May 1998, pp. 150-1.	Enhancements to the infant investment trust accounts system should be implemented at the County Court and the Victims of Crime Assistance Tribunal to enable the regular production and issue of transaction statements to trust fund beneficiaries.	In late 1999 the County Court's infant investment database was upgraded. However, the upgraded system did not allow for significantly increased functionality such as the ability to issue transaction statements. The County Court is also awaiting the outcome of a consultant's report on the Court's administration of funds held on behalf of persons with a disability. It is anticipated that the report will recommend the transfer of investment funds to another agency.
Victoria Legal Aid – Funding changes		
Ministerial portfolios, May 1999, pp. 186-207.	There is a need for Victoria Legal Aid (VLA) to undertake an assessment of the need for legal aid within the Victorian community to assist it in allocating scarce legal aid funding in the most effective and equitable manner, and to determine the impact of changes to legal aid guidelines on the provision of legal aid services in Victoria.	VLA is awaiting the findings of the Parliamentary Law Reform Committee's review of legal services in rural and regional Victoria. Audit was advised that a small survey of criminal law practitioners is being undertaken by VLA to help determine the need for legal aid in Victoria.
Need for enhanced public accountability covering non-judicial functions of Victorian courts		
Ministerial portfolios, May 1999, pp. 208-16.	No audits have been undertaken by the Auditor-General of administrative functions within judicial bodies since June 1996 because of legal advice obtained by the Department of Justice. This situation is totally unsatisfactory in terms of the public accountability implications to the Parliament and the community. Urgent action by way of legislative change is necessary to redress the position.	This important but complex issue is still under consideration by the Government.

SCHEDULE A
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS

Report	*Subject*	*Status at date of preparation of this Report*
	MATTERS RESOLVED OR ACTION COMMENCED	
TRAFFIC CAMERA OFFICE AND FINE COLLECTION SERVICES		
Ministerial portfolios, May 1996, pp. 152-9. *June 2000, p. 195.*	The long outstanding fines, totalling some $169 million, which were not allocated to LMT Australia (the successful tenderer the outsourcing of the operation of traffic cameras and fine collection and management services) for recovery action, are unlikely to be recovered given the rationalisation of internal resources.	At the time LMT was awarded the contract, $217 million of fines were outstanding for extensive periods. Under the contract LMT was required to recover at least $48 million of this amount. If LMT recovers more than $48 million it will receive bonuses under the contract.
	In addition, LMT's performance in relation to the Traffic Camera Office and Fixed Penalties Payments Office debt collection was below that specified in the contract, resulting in a possible reduction in payments to the service provider of $475 000.	LMT's performance has been below that specified in the contract in relation to the collection of debt incurred since the commencement of the contract and penalties have accumulated for this under performance.
TENANCY BOND AUTHORITY		
Ministerial Portfolios, June 2000, p.201.	Audit questioned whether the price submitted by the successful tenderer for the provision of tenancy bond collection, repayment and maintenance processing, was too low to adequately provide the services required.	In late 2000, the Department negotiated a revised contract with National Registry Services Pty Ltd, which required the Department to pay an additional $1.9 million to the company over the remaining period of the contract.

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS

Entity	Financial statements signed by entity	Auditor-General's report signed	Clear opinion issued
COMPLETED AUDITS			
FINANCIAL YEAR ENDED 30 JUNE 2000			
Department of Justice	9 Oct. 2000	16 Oct. 2000	✓
ATTORNEY-GENERAL			
Equal Opportunity Commission	25 Oct. 2000	26 Oct. 2000	✓
Legal Practice Board	29 Aug. 2000	31 Aug. 2000	✓
Office of Public Prosecutions	14 Sept. 2000	20 Sept. 2000	✓
Office of the Legal Ombudsman	21 Sept. 2000	21 Sept. 2000	✓
Office of the Public Advocate	20 Oct. 2000	25 Oct. 2000	✓
Queen Victoria Women's Centre Trust	26 Sept. 2000	27 Sept. 2000	✓
Victoria Legal Aid	25 Aug. 2000	28 Aug. 2000	✓
Victorian Electoral Commission	28 Sept. 2000	28 Sept. 2000	✓
Victorian Institute of Forensic Medicine	24 Oct. 2000	24 Oct. 2000	✓
POLICE AND EMERGENCY SERVICES			
Country Fire Authority	28 Aug. 2000	6 Sept. 2000	✓
Metropolitan Fire and Emergency Services Board	25 Sept. 2000	25 Sept. 2000	Qualified opinion
(Reason for Qualification: *Controlled revenue not recognised in operating statement)*			
National Institute of Forensic Science *(a)*	25 Oct. 2000	2 Nov. 2000	✓
National Police Ethnic Advisory Bureau	24 Oct. 2000	2 Nov. 2000	✓
Office of the Chief Commissioner of Police	31 Aug. 2000	19 Oct. 2000	✓
CONSUMER AFFAIRS			
Residential Tenancies Bond Authority	15 Feb. 2001	16 Feb. 2001	✓
INCOMPLETED AUDITS			
FINANCIAL YEAR ENDED 30 JUNE 2000			
Senior Master of the Supreme Court *(a)*			Financial statements not received
Legal Practitioners Liability Committee			" "

(a) In the absence of a statutory requirement for the audit of these financial statements they are audited by arrangement.

Part 3.5

Natural Resources and Environment

KEY FINDINGS

Automation of the Land Titles Register

- The current titles automation project at the Land Registry was initially scheduled for completion in March 2000. However, this target was subsequently revised to April 2002.

  Paras 3.5.39 to 3.5.44

- The project is expected to cost $91.6 million, an increase of $29.4 million or 47 per cent from the original cost estimate.

  Paras 3.5.45 to 3.5.51

- The total cost of major information technology developments, such as the titles automation project, are often difficult to estimate until detailed specifications are developed and the scope of the project is clearly defined. The large increase in the cost of the project to date and the potential for further costs is indicative of the risks associated with a project of this scale. The remaining stages of the project require careful management to minimise any further escalation of costs.

  Paras 3.5.45 to 3.5.51

- The revised management framework established in March 2001 should improve the overall management of the titles automation project and the level of accountability provided to senior management. However, it will be vital that the ongoing effectiveness of this framework and associated management processes are continually reassessed to ensure that adequate control is maintained over the progress and emerging costs of the project.

  Paras 3.5.52 to 3.5.56

KEY FINDINGS *- continued*

Wind-up of the Victorian Dairy Industry Authority

- The Victorian Dairy Industry Authority (VDIA) ceased operating in October 2000, at which time its net assets were distributed to Dairy Food Safety Victoria and a private company known as the Geoffrey Gardiner Dairy Foundation.

  Paras 3.5.81 to 3.5.83

- Net assets transferred from the VDIA to the Geoffrey Gardiner Dairy Foundation amounted to $62.6 million. The majority of the net assets transferred to this private company for use in accordance with the *Dairy Act* 2000 related to proceeds from the sale of the VDIA's fixed assets and intellectual property.

  Paras 3.5.87 to 3.5.94

- Although the Foundation is required to table audited annual financial reports in the Parliament, no independent review mechanism has been established to ensure that the funds transferred to the company are spent in accordance with the intentions of Parliament as outlined in the *Dairy Act* 2000.

  Paras 3.5.87 to 3.5.94

- In October 1999, the VDIA sold Food Quality Services Ltd, a wholly-owned subsidiary for $25 000. The sale process incurred costs of $72 000. Although the company was originally intended to be self-funding, the VDIA provided it with a total of $1.2 million to fund its operations since it commenced trading in July 1997.

  Paras 3.5.107 to 3.5.108

- In April 2000, the VDIA sold its interest in a joint venture arrangement involving the manufacture and marketing of Big M milk products in China to the Tianjin Dairy Corporation, a division of the Tianjin Farm Bureau which was the VDIA's original Chinese partner in the joint venture. The VDIA received $50 000 from the sale which was $342 000 less than the value of the VDIA's share of the net assets of the joint venture. Expenses related to the sale of the joint venture totalled $91 300.

  Paras 3.5.100 to 3.5.106

- At the time of the sale of the joint venture, the VDIA's share of its accumulated losses totalled $1.2 million and its initial investment of $730 000 in the joint venture had been written-down to zero. When the VDIA's direct costs associated with the management of the joint venture are included, the overall cost to the VDIA as a result of its involvement in the joint venture was in excess of $2 million.

  Paras 3.5.100 to 3.5.106

KEY FINDINGS *–continued*

Wind-up of the Victorian Dairy Industry Authority *- continued*

- In September 2000, the Big M brand was sold to National Foods and the REV, Skinny Milk and Farmhouse brands were sold to Parmalat Foods. The sale of the brands generated $57.2 million for the VDIA, with costs associated with the sale process amounting to $686 000.

Paras 3.5.95 to 3.5.99

Buy-out of bay and inlet commercial fishing access licences

- The Department of Natural Resources and Environment initiated a licence buy-out scheme which resulted in the removal of more than half of the commercial fishing licences for Victorian bays and inlets for an average purchase price of $74 000. The voluntary buy-back scheme, which cost $8 million, will be ultimately funded by the $20 recreational licence for anglers.

Paras 3.5.130 to 3.5.142

- The primary objective of the buy-out was to obtain the voluntary surrender of the maximum number of licences without affecting commercially caught fish supplies. With the voluntary nature of the buy-out scheme, and the remaining licensees having the ability to increase their fish take, commercial fishers stood to benefit from the buy-out.

Paras 3.5.159 to 3.5.161

- The buy-out is expected to have negligible impact on the commercial fish catch in bays and inlets, with the exception of Shallow and Anderson's Inlets, and has not directly concerns with net fishing.

Paras 3.5.162 to 3.5.165

- The method chosen for the buy-out has created significant differences in the benefits received by fishers in different locations.

Paras 3.5.166 to 3.5.170

- The Fisheries Co-Management Council's 1997 Review indicated that the sustainable future of bay and inlet fisheries were more seriously threatened by habitat and environmental degradation than by current recreational or commercial fishing activities.

Paras 3.5.171 to 3.5.174

KEY FINDINGS *–continued*

Alpine resorts land stability

- The Government, through the Department of Natural Resources and Environment, initiated a comprehensive review of land stability at all 6 of Victoria's alpine resorts during 1997-98.

  Paras 3.5.179 to 3.5.198

- Of the 660 sites assessed, 76 were rated as either a high or very high hazard, with many sites at risk of more than one type of instability.

  Paras 3.5.179 to 3.5.198

- High and very high hazard sites requiring urgent attention were managed at acceptable levels by the June 2000 snow season following the undertaking of remedial work, and it is anticipated that the remaining remedial work will be completed by mid-2002.

  Paras 3.5.199 to 3.5.203

- The importance of, and need for, ongoing monitoring of not only hazardous but also potentially hazardous sites is illustrated by the collapse, in January 2001, of a significant section of the fill supporting the resort access road at Mt Baw Baw.

  Paras 3.5.204 to 3.5.207

- The Alpine Resorts Planning Scheme has not been amended as concerns exist as to how to incorporate the findings of the review undertaken by the Department into the Scheme without explicitly exposing the State to liability should any land stability issues arise. In addition, it was felt that by publicly disclosing the hazard ratings of individual sites, it was possible that the value of the developments on the high hazard sites may be negatively impacted.

  Paras 3.5.228 to 3.5.232

- It was quite clear that the Thredbo disaster was the catalyst for the action taken to identify the significant hazards at the Victorian alpine resorts and the subsequent action taken to mitigate those risks.

  Paras 3.5.233 to 3.5.236

SUMMARY OF AUDIT RESULTS

3.5.1 The Natural Resources and Environment portfolio encompasses a number of areas of government activity as set out in the following paragraphs:

Environment and Conservation

3.5.2 The Environment and Conservation function encompasses a broad range of services provided directly by the Department of Natural Resources and Environment and other services provided by a diverse group of public sector bodies, which include:

- catchment management and provision of water and sewerage services;
- waste management;
- environment protection; and
- other conservation activities.

3.5.3 The major functions undertaken directly by the Department include:

- **Forest management** - which facilitates the provision of timber and other products from State forests on a sustainable basis, and the conservation of flora and fauna within those forests;
- **Fire management** - which involves the provision of fire protection and suppression services on public land and assistance in response to other emergency situations on private land;
- **Land management and information -** which involves:
  - management of public land in Victoria;
  - maintenance of land definitional information;
  - provision of title registration, valuation and other information services; and
  - maintenance of the State's digital map base system (Vicmap Digital); and
- **Conservation and Recreation** - which involves the provision of:
  - coastal planning and management services;
  - maintenance and enhancement of the State's biological diversity; and
  - management and regulation of Victoria’s parks and reserves.

Catchment management and water and sewerage services

3.5.4 The Department has overall responsibility for the co-ordination and management of the Victorian water sector, which comprises the metropolitan, non-metropolitan urban and rural water sectors and the activities of the State’s catchment management authorities.

Metropolitan water sector

3.5.5 The metropolitan water sector consists of a wholesale water authority, Melbourne Water Corporation and 3 retail water distribution companies, namely, Yarra Valley Water Limited, South East Water Limited and City West Water Limited.

3.5.6 The retail water companies operate under licences to provide water and sewerage services to 3.1 million people in metropolitan Melbourne.

3.5.7 Melbourne Water supplies bulk water to the retail water companies and is responsible for the treatment and disposal of sewage and provision of drainage services.

Non-metropolitan urban water sector

3.5.8 The non-metropolitan urban water sector, which consists of 15 water authorities, provides water and sewerage services to approximately 1.1 million people living in country Victoria.

3.5.9 The authorities access their water from various sources, including purchases from rural water authorities, internal storage facilities and through direct extraction from rivers, streams and the ground.

Rural water sector

3.5.10 The rural water sector is responsible for supplying Victoria's agricultural community with water for irrigation, stock and domestic purposes, and supplying bulk water to urban water authorities and industry.

Catchment management

3.5.11 Victoria's 9 catchment management authorities were established on 1 July 1997 to undertake the statutory functions established by the *Water Act* 1989 of catchment and land protection, waterway and floodplain management, and regional drainage.

Waste management

3.5.12 The waste management sector consists of 16 regional waste management groups. The role of these groups is to work with local government, the private sector, the community and the Environment Protection Authority to achieve sustained reductions in waste, and improvements in the management of residual waste streams.

Environment protection

3.5.13 The Environment Protection Authority is a statutory body established under the *Environment Protection Act* 1970. The primary responsibility of the Authority is to ensure the protection of Victoria's air, water and land from the adverse impacts of pollution, wastes and unwanted noise.

Other conservation activities

3.5.14 Other activities of a conservation nature which are undertaken by various public sector agencies include:

- management of Victoria's alpine resorts;
- management of the State's metropolitan parks and gardens; and

- provision of tourist attractions such as the Melbourne Zoo and Phillip Island Nature Park.

Aboriginal Affairs

3.5.15 The Aboriginal Affairs function involves the provision by the Department of services and programs to help Aboriginals protect, manage and improve community awareness of Aboriginal cultural heritage.

Agriculture

3.5.16 The Agriculture function involves the Department undertaking research and development activities, supporting the agricultural sector through extension and market development services, and provision of policy, regulatory and quality assurance services for the dairy, grain, horticulture, meat and wood agricultural industries.

3.5.17 Other entities who assist in the provision of this activity include:

- 3 public bodies involved in agricultural research, in addition to the Department's 16 research institutes; and
- 5 development committees and one marketing board.

Energy and Resources

3.5.18 The Energy and Resources function encompasses a range of activities including:

- **Minerals and Petroleum** – which involves the regulation of the extractive, exploration and mining industries and pipelines in Victoria, provision of industry-specific facilitation, development and marketing services, and maintenance of the State's historical geological database; and
- **Fisheries** – which involves industry regulation, economic development, resource management and provision of information services in the Victorian commercial fishing and aquaculture industries.

3.5.19 The Minister for Agriculture, the Minister for Aboriginal Affairs, the Minister for Energy and Resources, and the Minister for Environment and Conservation have responsibility for operations within the Natural Resources and Environment sector. These Ministers have collective responsibility for the Department of Natural Resources and Environment.

3.5.20 Details of the specific ministerial responsibilities for public sector bodies within the portfolio are provided in Table 3.5A. These public bodies, together with the Department of Natural Resources and Environment, were subject my audit during the 1999-2000 financial year.

TABLE 3.5A
MINISTERIAL RESPONSIBILITY FOR PUBLIC BODIES WITHIN THE NATURAL RESOURCES AND ENVIRONMENT SECTOR

Ministerial portfolio	*Entities subject to audit*
Aboriginal Affairs	-
Agriculture	Agriculture Victoria Services Pty Ltd
	Australian Food Industry Science Centre
	Emu Industry Development Committee
	Food Quality Services Pty Ltd
	Food Science Australia
	Melbourne Market Authority
	Murray Valley Citrus Marketing Board
	Murray Valley Wine Grape Industry Development Committee
	Northern Victorian Fresh Tomato Industry Development Committee
	Veterinary Practitioners Registration Board of Victoria
	Victorian Dairy Industry Authority
	Victorian Meat Authority
	Victorian Strawberry Industry Development Committee
Energy and Resources	Renewable Energy Authority of Victoria
Environment and Conservation	Alpine Resorts Co-ordinating Council
	Casey's Weir and Major Creek Rural Water Authority
	Catchment management authorities (9)
	Central Highlands Region Timber Pty Ltd
	City West Water Ltd
	Eco Recycle Victoria
	Environment Protection Authority
	Falls Creek Alpine Resort Management Board
	First Mildura Irrigation Trust
	Gippsland and Southern Rural Water Authority
	Goulburn Murray Rural Water Authority
	Lake Mountain Alpine Resort Management Board
	Marine and Fresh Water Resources Institute
	Melbourne Parks and Waterways
	Melbourne Water Corporation
	Mount Baw Baw Alpine Resort Management Board
	Mount Buller Alpine Resort Management Board
	Mount Stirling Alpine Resort Management Board
	Non-metropolitan water authorities (15)
	Phillip Island Nature Park Board of Management
	Regional waste management groups (16)
	Royal Botanic Gardens Board
	Shrine of Remembrance Trustees
	South East Water Limited
	Sunraysia Rural Water Authority
	Surveyors Board of Victoria

TABLE 3.5A
MINISTERIAL RESPONSIBILITY FOR PUBLIC BODIES
WITHIN THE NATURAL RESOURCES AND ENVIRONMENT SECTOR - *continued*

Ministerial portfolio	*Entities subject to audit*
Environment and Conservation - *continued*	Sustainable Energy Victoria
	Trust for Nature (Victoria)
	Victorian Plantations Corporation
	Water Training Centre
	Wimmera Mallee Rural Water Authority
	Yarra Bend Park Trust
	Yarra Valley Water Limited
	Zoological Parks and Gardens Board

Audit opinions issued

3.5.21 The Auditor-General is responsible for 86 financial audits within the Natural Resources and Environment portfolio. Seventy-nine of these audits have 30 June balance dates and are required to report to the Parliament by 31 October in accordance with the *Financial Management Act* 1994. All of these agencies report under section 46 of the Act, except for 5 companies which report under section 53A.

3.5.22 At the date of preparation of this Report, 84 audit opinions were issued on financial reports of public sector agencies within the Natural Resources and Environment portfolio. Details of audits completed and those outstanding are contained in Schedule B.

3.5.23 Of the financial reports finalised, 82 received clear audit opinions and 2 received qualified audit opinions. Details of qualified audit opinions and the reasons for the qualifications are outlined in Table 3.5B

TABLE 3.5B
QUALIFIED AUDIT OPINIONS
NATURAL RESOURCES AND ENVIRONMENT PORTFOLIO

Name of entity	*Nature of audit qualification.*
Murray Valley Citrus Marketing Board	Limitation of scope qualification. Due to inadequacy of the Board’s internal control mechanisms, audit was unable to attest to the completeness of levy revenue recorded in the Board’s financial report.
Tungamah Shire Water Board	The lack of adequate accounting records precluded audit from verifying the validity of information contained in the Board’s financial reports for 1994-95, 1995-96, 1996-97 and 1997-98 financial years.

Timeliness of financial reporting process

3.5.24 The *Financial Management Act* 1994 requires government agencies to prepare their financial reports within 8 weeks of balance date and for these reports to be audited within 4 weeks of their receipt by the Auditor-General. Table 3.5C provides details of the timeliness of the financial reporting process within the Natural Resources and Environment portfolio.

TABLE 3.5C
TIMELINESS OF FINALISATION OF AUDITED FINANCIAL STATEMENTS, NATURAL RESOURCES AND ENVIRONMENT PORTFOLIO

	Entities	
Number of weeks after end of financial period	*Number*	*Per cent (cumulative)*
Less than 8 weeks	3	3
8 to 10 weeks	9	14
10 to 12 weeks	9	24
12 to 14 weeks	11	37
14 to 16 weeks	17	57
16 to 18 weeks	4	62
More than 18 weeks *(b)*	33	100

(a) The table does not include financial statements for the 1998-99 financial year.

(b) Includes 3 entities where the audited financial reports are yet to be finalised.

3.5.25 The table demonstrates that **there is scope for improvement in the timeliness of audited financial report completion by portfolio entities, with only 24 per cent of entities able to meet the 12 week legislated completion timeframe**. The audited financial statements of 57 per cent of the entities were available within 4 weeks of the legislated completion timeline (i.e. within 16 weeks of year-end). However, at the date of preparation of this Report, 3 entities had not finalised their financial statements.

3.5.26 **Timeliness of reporting is an essential characteristic of quality information and the effectiveness of the accountability process. Accordingly, it is important that avenues are identified and pursued to improve the timeliness of the financial reporting process.**

AUTOMATION OF THE LAND TITLES REGISTER

3.5.27 Land Registry, a division of Land Victoria within the Department of Natural Resources and Environment, is responsible for:

- maintaining and updating the State's Land Titles Register, which is the main repository for land information;
- creating titles for new parcels of land;
- providing access to information from the register and associated documents to a range of interested parties, including banks, solicitors, real estate agents and individuals; and
- storing registered documents that are required for inspection.

3.5.28 In its current form, the Land Titles Register comprises a collection of mainly paper-based land titles and supporting documentation including:

- 3.9 million land titles of which 2.5 million are current and 1.4 million have been cancelled;
- 300 000 plans which define the boundaries of new land parcels created through subdivisions;
- 270 000 survey reports which contain documents prepared by land surveyors in support of plans of property subdivision; and
- 13 million instruments which are source documents for new details registered on land titles including mortgage amendments, transfers of land titles to a new proprietor, caveats and creation of multiple land titles from existing land titles.

3.5.29 Land Registry operations cover a significant area of activity with over 800 000 title searches and 700 000 dealing transactions undertaken each year. Annual revenue collections from this area of activity approximates $130 million. Land titles, dating back to the 1850s, occupy over 9 043 linear metres of storage space within the Land Registry premises.

History of automation of land titles

3.5.30 The majority of land queries and transactions, including title searches and land registration are undertaken by reference to paper-based documents. However, a number of computerised systems, introduced before 1990, are in use to support the functioning of the Land Titles Register. These systems, for which facilities management is undertaken by external contractors, are:

- Unregistered Dealings System (URDS), which is used to track the status of land dealings documentation;
- Automated Land Titles System (ALTS), which is used for storage and update of the 28 per cent of total land titles that are available in an electronic format; and
- Imaging System, which records images of 66 per cent of total registered plans of subdivision, survey reports and instruments.

3.5.31 The Land Registry has, over many years, recognised the need to automate all major aspects of its operations to ensure that an effective and efficient registry service is maintained. Table 3.5D outlines steps taken to automate the Land Titles Register since initial automation was commenced in 1989.

TABLE 3.5D
STEPS TAKEN TO AUTOMATE THE LAND REGISTRY, 1989 TO PRESENT

Year	*Steps taken*
1989	The Automated Land Titles System (ALTS) was introduced to enable the initial automation of the land titles register involving the conversion of paper titles to computer titles.
1991	Approximately 28 per cent of paper titles were converted to electronic format by in-house staff.
1992	ALTS was expanded to enable the on-line update of computer folios by Land Registry and facilitate remote title search by interested parties.
1993	Conversion of paper titles to an electronic format within the ALTS system was suspended due to a lack of resources with only 28 per cent of titles converted.
1994	A Department of Premier and Cabinet report on the business operations of the Land Titles Office (now Land Registry) recommended automation of all paper titles.
1995-97	A proposal to attract private sector funding for the titles automation process was unsuccessful.
1997	In August 1997, approval was obtained from the Treasurer for the automation of all land titles (known as the Titles Automation Project or "TAP") with initial funding of up to $62 million and the final funding allocation to be determined once tenders were received. New tenders for titles automation services were called with the cost of automation to be funded from excess fees generated from the former Land Titles Office operations.
1998	Tender evaluation completed and 3 contracts entered into for project management services, land titles data conversion and development of new Victorian On-line Titles System (VOTS). (Refer to Table 3.5H for the estimated cost of the VOTS project.)
1999	Implementation of TAP commenced
2000	Revised cost estimate of $91.6 million and revised completion date for initial implementation of VOTS by November 2001. Minor enhancements to VOTS to be finalised by April 2002.

3.5.32 As outlined in the preceding table, **the automation of land titles has been slow, with little progress made between the suspension of the initial automation project in 1993 and the commencement of the current Titles Automation Project in 1997. This lack of progress was mainly due to insufficient resources being available to pursue automation until approval was received for the current project.**

3.5.33 Comments on aspects of the current Titles Automation Project are contained in the following paragraphs of this Report.

Overview of the current Titles Automation Project

3.5.34 The Titles Automation Project (TAP) is a major initiative aimed at introducing new and improved business processes and systems to facilitate the automation of land titles operations. The implementation of TAP, which will result in the creation of an electronic land titles register and the replacement of the outdated paper-based and electronic systems currently in use, is expected to significantly enhance the delivery of land titles registration services by:

- assisting Land Victoria in achieving its objectives of providing an authoritative, comprehensive and easily accessible system of land information and management;
- maintaining an electronic security copy of all land titles;
- increasing productivity within the Land Registry;
- allowing immediate and remote access to land titles;
- providing a platform for electronic conveyancing; and
- significantly reducing the time taken to process land titles transactions.

3.5.35 Table 3.5E sets out the expected processing efficiency sought following the successful implementation of TAP.

TABLE 3.5E
EXPECTED REDUCTION IN PROCESSING TIMES FOR LAND TITLE TRANSACTIONS

Transaction	*Current service times*	*Automated service times*
Computerised titles	1 hour	Less than 2 seconds
Paper titles	24 hours	Not applicable
Instruments	24 hours	1-10 seconds
Registration of documents lodged	3 weeks for 80 per cent of dealings	Less than 15 minutes for simple dealings 1 to 5 days for complex dealings

3.5.36 Land Registry has entered into 3 contracts for the implementation of TAP, namely:

- *Project Management*, entered into in April 1998 with TCS Management Pty Ltd, involving the provision of project management services for the implementation and delivery of TAP, including managing all tasks associated with:
  - the tendering of the other 2 contracts;
  - overseeing the development of the Victorian Online Titles System (VOTS);
  - controlling and co-ordinating the activities of a TAP project team and external contractors;
  - providing regular reports of progress against milestones;
  - advising on all matters relevant to the achievement of key outcomes; and
  - providing a training program to enable Land Registry staff to utilise the VOTS system.
- *Land Titles Data Conversion,* entered into in December 1998 with Hermes Precisa Pty Ltd, which requires delivery of 7 key services comprising:
  - *Land Titles Security Copy*, which involves the creation of a scanned image of all titles;
  - *Land Titles Data Conversion* (Text and Diagram), which requires the capture of text from both current and cancelled titles in an electronic format and the provision of a separate title diagram for current titles on the document imaging system;
  - *Plans of Subdivision Conversion*, which requires the preparation and loading to the document imaging system of approximately 43 000 plans of subdivision and approximately 270 000 survey reports;
  - *Instrument Conversion*, which involves the preparation and loading to the document imaging system of approximately 500 000 instruments;
  - *Implementation of a Document Imaging System and Provision of Facilities Management Services*, relating to transfer of the existing imaging system to a new software platform, and the provision and facilities management of a new document imaging system;
  - *Image and Data Migration*, which requires the transfer of image and index data from the existing systems to the new document imaging system; and
  - *Ongoing Document Load*, which involves the loading to the document imaging system of all new registered instruments, plans of subdivision and survey reports.

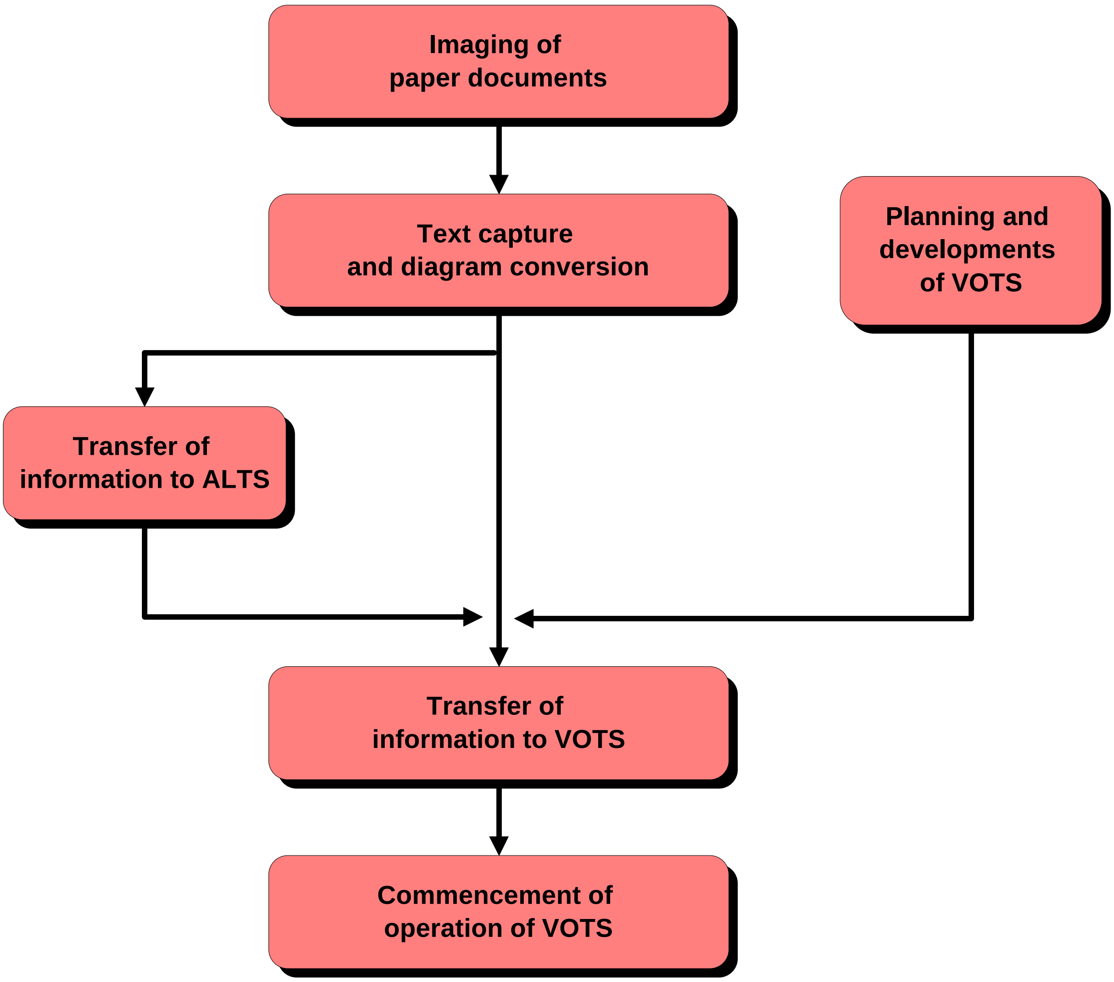
- *Land Titles Re-engineered Business System,* entered into in April 1999 with Fujitsu Australia Limited, involving the construction of a new IT system, the Victorian Online Titles System (VOTS), and encompassing:
    - software development and maintenance;
    - facilities management of equipment, software and the network required to operate the VOTS system;
    - the transfer of data from existing systems to the new VOTS system; and
    - the provision of services for enhancements to the VOTS application software.

3.5.37 The contracts for data conversion and the new information technology system involved not only the conversion of existing data and the development of the system but also ongoing data conversion of new land titles and system management for a period up to April 2004. While prices for the provision of services were included in the contracts, these prices were established on broad-based service specifications. Consequently, the ultimate cost of these services was dependent on subsequent decisions related to the detailed scope and specifications of the project, the ongoing volume of data to be converted and the resultant impact on contract prices.

3.5.38 Key processes involved under the contracts for data conversion and the development and implementation of the VOTS system, (as summarised in Table 3.5F), involve the following steps:

- *Data conversion*, which requires the scanning of each paper title and associated documents for subsequent input into a computer database. The text from the paper titles and associated documents have been transferred to the existing automated system ALTS as an interim data storage medium until such time that the VOTS system is fully operational. More complex documentation, which cannot be stored on ALTS due to certain limitations within the system, will be directly transferred to the VOTS system; and
- *Development and implementation of VOTS,* which covers the initial preparation of the customer functional specifications and, ultimately, the development of the system based on the specifications. The implementation of the 7 core functional modules is currently in progress covering systems administration, search and retrieval, a land index database (LANDATA), data migration, revenue receipting, off-line management and register management.

TABLE 3.5F
DATA CONVERSION AND VOTS DEVELOPMENT PROCESSES



Status of the Titles Automation Project

3.5.39 **The Titles Automation Project was initially scheduled for completion in March 2000, as set out in a *Project Definition Report* prepared in February 1998. However, this target was subsequently revised to:**

- **a "go live" target date for the implementation of VOTS by November 2001; and**
- **final completion, including minor software enhancements and post-implementation reviews by April 2002.**

3.5.40 The extensions to the initial TAP completion dates have resulted from a number of factors including:

- delays in the commencement of tendering and contracting;
- complexities that have arisen during data conversion due to the poor condition of many paper documents;

- the need for extensive expert interpretation of certain documents prior to data conversion; and
- a change in project scope arising from the development of detailed functional service specifications.

3.5.41 Table 3.5G outlines the status and expected date of completion, at the time of the preparation of this Report, for each of the key services required under the contractual arrangements.

TABLE 3.5G
PROGRESS AGAINST KEY DELIVERY MILESTONES

Task	*Status*	*Date completed/due date for completion*
Data conversion		
Migration of image data from the existing system to the new imaging system	Completed	28/01/00
Instrument Conversion	Completed	2/08/00
Land Titles Security Copy	Completed	13/10/00
Data Conversion – Text	Completed	8/11/00 (Text capture excludes 230 000 titles by virtue of their complexity. These titles will be captured as and when transactions on the respective titles are recorded.)
Data Conversion – Diagram	Completed	22/12/00
Plan of subdivision – Survey Reports	78 per cent complete	29/06/01
Plan of subdivision – Plans	75 per cent complete	30/4/02 (The remaining plans are large plans which require breaking down into several parts before imaging.)
VOTS		
Business Process	Completed	9/03/00
Software Development	96 per cent complete	11/07/01
User Acceptance Testing	80 per cent complete	1/08/01
Release Acceptance	Not commenced	28/09/01
Ongoing services		
Document Load	Ongoing	30/04/04
Document Imaging	Ongoing	30/04/04
Facilities Management	Ongoing	30/04/04
Support Service	Not commenced	30/04/04
Systems Integration	Ongoing	30/04/04

3.5.42 **All 7 modules relating to the VOTS system have been constructed and handed over to Land Registry for formal user acceptance testing. However, at the date of the preparation of this Report, only 4 modules have been fully tested and accepted by Land Registry.**

3.5.43 While TAP is currently on track to meet the revised delivery milestones, there are a number of outstanding factors that may have a significant impact on whether these milestones will be achieved, including:

- The outcome of system testing for the remaining VOTS modules;
- The relocation of Land Victoria, including the Land Registry, to new premises from November 2001; and
- A business decision by the Department of Natural Resources and Environment and Land Victoria to adopt the Department's standardised desktop operating environment. **This factor was not accounted for in the 1998 contract specifications and has implications for the architecture of the system and the system's ongoing performance.** The implications of this matter are currently under consideration by the Land Registry and its contractors.

3.5.44 While a risk management framework has been in place since 1998, action has recently been taken to strengthen this aspect of the project to ensure that the outstanding factors outlined above and any other emerging risks associated with the project are comprehensively managed. Specific actions have included the establishment of a risk management committee with broad representation and appointment of an Information Technology Risk Manager.

Project costs

3.5.45 In August 1997, the Treasurer's approval was obtained for funding of the project up to $62 million with a final allocation for the project to be determined on the receipt of tenders. At the time, it was envisaged that the total cost of the project may increase following development of the detailed project scope and specifications with any additional funding requirements to be subject to a separate submission to the Department of Treasury and Finance.

3.5.46 Land Registry included only broad specifications in its initial project proposals and adopted an approach of relying on contractors to develop more detailed specifications during the development phase of the project. This approach was also aimed at providing scope for tenderers to offer off-the-shelf solutions. While this approach may be adopted for major information technology projects, clearly a risk exists that the scope, timing and cost of the project will be under-estimated during the initial proposal and planning phases.

3.5.47 A comparison of the original cost estimate to the most recent revised estimate is outlined in Table 3.5H.

TABLE 3.5H
SUMMARY OF TAP COSTS
($'000)

Contract	*Original cost estimate*	*Revised cost estimate*	*Increase in costs*
Project management	2 595	5 785	3 190
Data conversion	40 876	48 064	7 188
VOTS	18 745	26 266	7 521
Expert advice obtained and overtime worked by in-house staff on the project *(a)*	-	8 517	8 517
Contingency	-	3 000	3 000
Total	**62 216**	**91 632**	**29 416**

(a) Both the initial and revised cost estimates are understated to the extent that they do not incorporate the salary costs of in-house staff for the extensive time devoted to the project during normal working hours. These costs have been absorbed within the normal operating costs of Land Registry.

3.5.48 The revised cost estimate of $91.6 million, of which $53 million has been expended to date, is based on a business case review and financial analysis undertaken by external consultants and the project management team in October 2000. This review was commissioned to clearly determine the total funding requirements for the project. The review encompassed consideration of a number of options, including estimating the cost of each option, abandonment of the project, limiting the project scope, or completing the project in line with its established scope. The review recommended continuation of the project in line with its established scope. Land Registry accepted this recommendation.

3.5.49 **Based on this revised estimate, the cost of the project has increased by $29.4 million or 47 per cent from the cost outlined in the initial project proposals.** The major reasons for this increase include:

- Difficulties in accurately estimating total costs of automation during the initial stages of the project in the absence of detailed project specifications;
- Cost variation claims made by contractors due to factors such as changes to the project scope and system specifications, and various difficulties experienced in the conversion of data not anticipated at the commencement of the project. To date, variations totalling $11 million have been approved by the Land Registry;
- A $1.9 million compensation claim by the contractor resulting from a decision by the Land Registry not to proceed with the automation of 230 000 of the more complex land titles;
- Additional costs of $3.2 million related to the extension of contract project management services to March 2002; and
- The cost of expert advice and staff overtime that was not provided for in the initial cost estimates.

3.5.50 **The final cost of the project may escalate beyond the current estimate of $91.7 million** if the contingency provision allowed for in the estimate is exceeded in relation to:

- the additional costs that may arise from the outcome of current negotiations for an extension of project management services to March 2002;
- additional costs for expert advice and staff overtime associated with the provision of TAP services;
- costs associated with commissioning VOTS within the new premises; and
- contract variations and the outcomes of VOTS testing associated with the remaining VOTS modules.

3.5.51 **The total cost of major information technology developments, such as the Titles Automation Project, are often difficult to estimate until detailed specifications are developed and the scope of the project is clearly defined. However, the large increase in the cost of the project to date and the potential for further costs is indicative of the risks associated with a project of this scale. The remaining stages of the project require careful management to minimise any further escalation of costs.**

Adequacy of project management

3.5.52 Land Victoria has commissioned a number of independent reviews of the project, the latest being the December 2000 review of the effectiveness of project management services.

3.5.53 That review identified a number of deficiencies in the management of the project including:

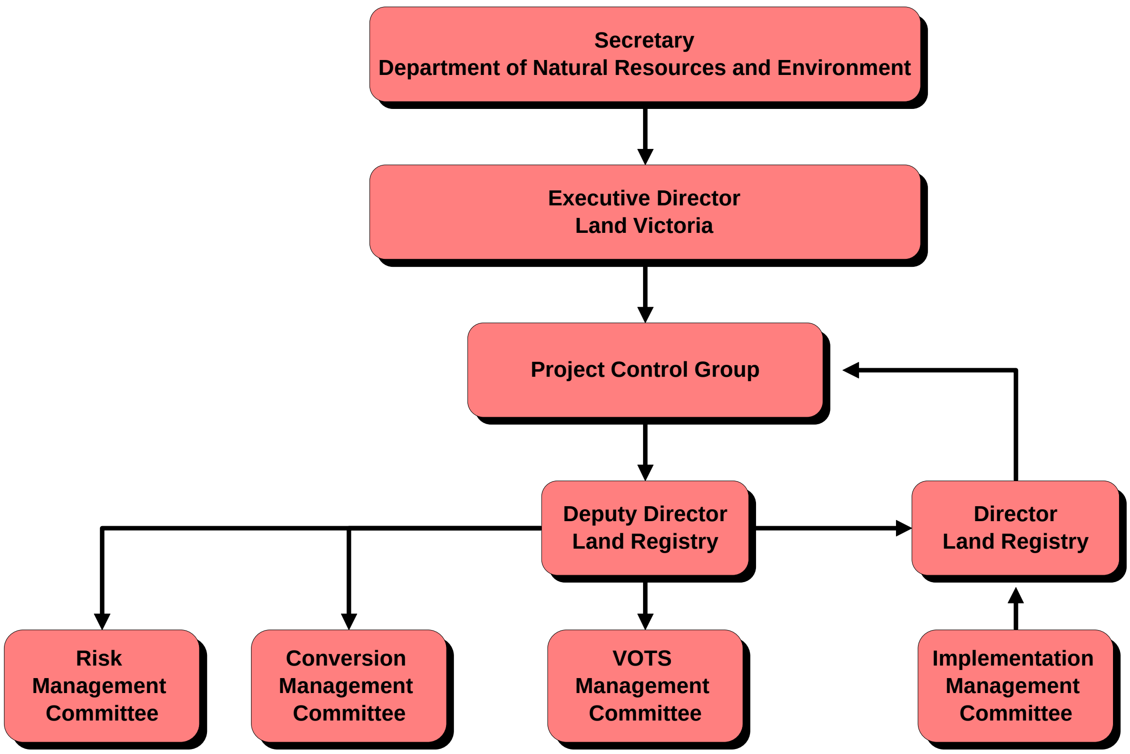
- insufficient controls and approvals relating to the significant additional costs arising from the use of Land Registry resources, the extension of project management services and unforeseen data conversion issues;
- inadequate consideration of contract variations on project costs or timeframes; and
- a lack of detail in ongoing financial reporting.

3.5.54 These concerns over project management were further compounded by **changes within the Land Registry's internal project management structure, due to a number of key staff departures since 1998, which have adversely impacted upon the continuity of knowledge and expertise in relation to the Titles Automation Project.**

3.5.55 Recent action has been taken to address some of the issues highlighted by the December 2000 review of project management arrangements and to implement other required improvements identified by Land Registry including:

- establishment in March 2001 of a revised management framework with ultimate accountability for the project resting with the Secretary of the Department of Natural Resources and Environment, as outlined in Chart 3.5I;
- enhancement of the role and accountability of the Project Control Group which was first established in 1997 to oversee the management and development of the project;
- appointments to vacant positions within the project management structure;
- development of an integrated project plan;
- improved controls over the monitoring and approval of changes and variations to project scope and contractual arrangements; and
- enhancement to financial and progress reporting of the project.

CHART 3.5I
CURRENT TAP MANAGEMENT FRAMEWORK



3.5.56 **The revised management framework should improve the overall management of the Titles Automation Project and the level of accountability provided to senior management. However, it will be vital that the ongoing effectiveness of this framework and associated management processes are continually reassessed to ensure that adequate control is maintained over the progress and emerging costs of the project.**

RESPONSE *provided by Secretary, Department of Natural Resources and Environment*

Overall comment

The Titles Automation Project (TAP) is on schedule for implementation later in the year. As the project nears finalisation, the Department has taken a number of actions to ensure that the costs to complete the automation project do not exceed the current estimate of $91.7 million.

The Department commissioned an independent review of forecast costs to completion of TAP. This review found that the forecast project costs were sound. As an extra precaution, the independent review suggested that funding estimates should include a provision for additional project contingency. A $3 million contingency sum is included in the $91.7 million total project cost.

In addition, as audit's Report acknowledges, the Department has put in place a number of measures to control any escalation of project costs. These include measures to improve project governance and control, a review of project management and implementation of the recommendations arising from that review. The Department has also strengthened the risk management arrangements for the project and appointed an independent external IT adviser to the Project Control Group. The appointment of an IT Risk Manager for the project is also imminent.

Status of the project

Land Registry has completed acceptance testing of 4 modules and the acceptance testing program is on schedule to complete module testing on 7 June 2001. This program provides 5 months for integrated testing of VOTS before the planned "go live" date. The integrated testing program has been revised recently to provide extra days of time contingency in the schedule.

Project costs

As noted by audit in Table 3.5H of the Report, the initial funding approved by the Treasurer was up to $62 million with final funding to be determined once tenders were received. The initial funding was for project planning and start-up and it was always anticipated that further funding would be required once firm project costs were established.

Of the $35.6 million funds remaining in the TAP budget as at 30 April 2001, $23.6 million is for facilities management and ongoing conversion of new documents. These costs are fixed in contracts with major suppliers. The balance of $11.9 million is for final software payments, remaining conversion tasks, testing, data migration, training and project management. At this stage in the implementation of TAP, the costs of the above activities can be established with a high degree of confidence. In addition, TAP has a $3 million contingency included in the $91.7 million in the total project cost. This contingency has not been allocated to any activity.

RESPONSE *provided by Secretary, Department of Natural Resources and Environment - continued*

Project costs *- continued*

As anticipated in the initial project funding request, once detailed specifications and project scoping were completed for TAP it was necessary to seek additional funding to complete the project. Now that the costs of completing the Titles Automation Project have been accurately established, the Department has taken action to closely manage the final stages of the project to ensure that there is no escalation of costs. These actions include:

- *An independent review of project costs. The review concluded that the forecast costs to completion were sound;*
- *An independent project management review. The Department has implemented all the major recommendations arising from that review;*
- *Strengthened project governance and reporting arrangements within Land Victoria and to the NRE Executive;*
- *Appointment of an independent IT professional to the Project Control Group;*
- *Establishment of a risk management committee with broad representation covering both the project and associated activities such as the relocation to new accommodation; and*
- *Appointment of an IT Risk Manager.*

Adequacy of project management

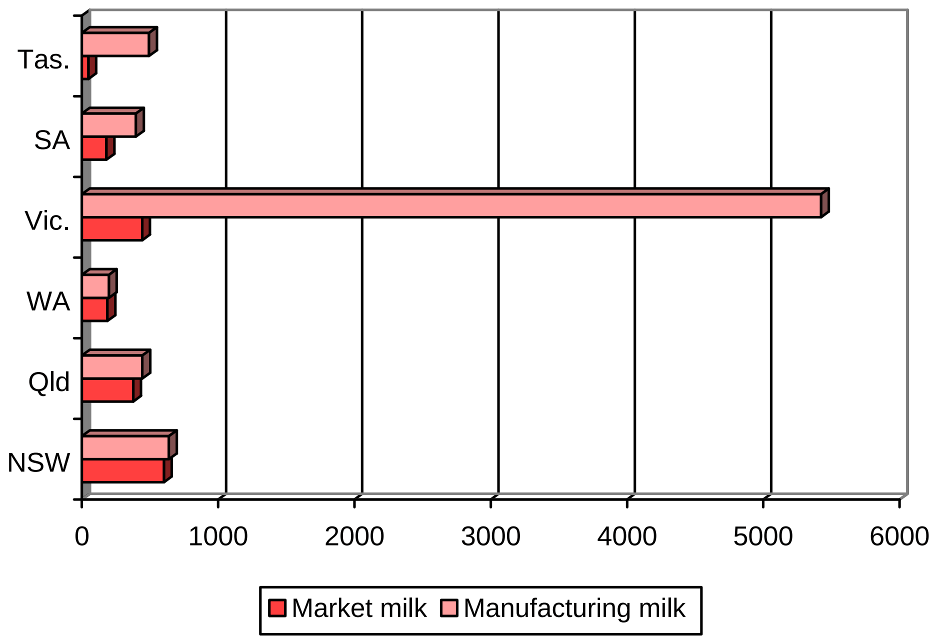
The Department has taken extensive steps to strengthen the project control and governance framework for the project. However, it concurs with audit's view that continual reassessment of the management arrangements is essential. A constant monitoring and reassessment regime is included in the Project Control Group's charter and in the work program of the senior officers accountable for delivery of TAP.

WIND-UP OF THE VICTORIAN DAIRY INDUSTRY AUTHORITY

Regulatory environment prior to July 2000

3.5.57 The dairy industry in Australia provides milk for drinking (known as market milk) and milk for the manufacture of dairy products (known as manufacturing milk). While each State produces market milk, Victoria produces the bulk of milk for manufacture. Chart 3.5J below highlights the amount of market and manufacturing milk produced annually in each State.

CHART 3.5J
ANNUAL MILK PRODUCTION IN EACH STATE, 1998
(million litres)



Source: *Deregulation of the Australian Dairy Corporation,* Report by the Commonwealth Senate Rural and Regional Affairs and Transport References Committee, October 1999.

3.5.58 Following the phasing-out of farm contracts for the supply of market milk in the 1970s, the pricing and supply of this milk became regulated by statutory authorities established by the respective State Governments within Australia. This contrasted with the previously unregulated market for manufacturing milk, where the selling price varied in response to supply and demand for dairy products, and movements in the prices of these products on world markets.

3.5.59 The mechanism used to regulate the pricing and supply of market milk varied from State-to-State and depended on the type of milk predominantly produced. In Victoria, South Australia and Tasmania, where revenue derived from the production of manufacturing milk significantly exceeds revenue derived from the production of market milk, farmers received a share of the revenue generated from sales of market milk, according to:

- each farmers' share of that State's total milk production; and
- the ratio of total market milk sold in the State to total milk produced.

3.5.60 In New South Wales, Western Australia and Queensland, the supply of market milk was managed through the allocation of production quotas (which were tradeable assets) to farmers. Production of milk in accordance with these quotas guaranteed farmers a fixed pre-determined price for their produce.

3.5.61 A major consequence of industry regulation was that the price of market milk was higher than that of manufacturing milk. The relatively higher price of market milk was maintained by restricting interstate trade for this milk though a voluntary agreement between the dairy industries in each State.

3.5.62 In this regulated environment, it became important for the Commonwealth Government to support the manufacturing milk sector and assist with developing its international competitiveness. This was achieved through the introduction of a number of market support schemes, the most recent of which was the Domestic Market Support Scheme, which ceased on 30 June 2000. Under the Scheme, farmers producing manufacturing milk received annual payments to encourage them to produce milk for manufacturing. The payments were funded by a levy of 3.6 cents per litre on manufacturers using milk for the production of dairy products consumed in Australia and a levy of 1.9 cents per litre on farmers selling market milk. The funds generated from the levies were pooled and distributed to the farmers based on the quantity of manufacturing milk they produced.

3.5.63 The regulated environment provided a minimum price per litre to dairy farmers producing market milk, while at the same time levying them at the rate of 1.9 cents per litre of milk produced, which subsidised those farmers producing manufacturing milk.

3.5.64 However, during the 1990s as the production of manufacturing milk increased in response to overseas demand for dairy products, the payments under the Scheme were spread over a greater volume of milk. This increased production resulted in a reduction in subsidy payments to farmers producing manufacturing milk from about 1.9 cents per litre in 1997-98 to approximately 0.95 cents per litre in 1999-2000.

Role of the former Victorian Dairy Industry Authority

3.5.65 In Victoria the State Government, under the authority of the former *Victorian Dairy Industry Authority Act* 1977, established the Victorian Dairy Industry Authority (VDIA) with responsibility for the pricing and supply of market milk within the State. In accordance with the Act, the VDIA acquired all market milk directly from farmers for sale to milk processors, with the proceeds generated from these sales used to pay these farmers for their produce.

3.5.66 Payments to farmers, which were made on a monthly basis, consisted of:

- a base payment per litre of milk supplied, which was set by the VDIA to match as closely as possible the price paid by factories for manufacturing milk; and
- a distribution from the proceeds of market milk sold by the VDIA, at a premium, to milk processors.

3.5.67 The VDIA was also responsible for:

- promoting the consumption of dairy produce and market milk produced in Victoria and conducting milk marketing and promotional activities;
- fostering the development of new types of milk and dairy produce and funding product development, research, education and training; and
- setting and administering standards for the production, testing, processing and handling of dairy produce.

3.5.68 In recent years, the VDIA reduced its commercial activities and, in preparation for the possibility of deregulation, began concentrating on its core regulatory functions. Major changes impacting on the operations of the VDIA included:

- Transferral, in July 1994, of milk marketing and promotional activities to Australian Milk Marketing Ltd, a not-for-profit company jointly owned and controlled by the United Dairy Farmers of Victoria (UDV), the Milk Processors Association of Victoria (MPAV) and the VDIA. The VDIA transferred its interest in the company to the UDV and the MPAV in October 1996 for nil consideration;
- Abolition, in July 1995, of minimum prices for market milk at wholesale, semi-wholesale and retail levels, and withdrawal from milk transport; and
- Establishment, in July 1997, of Food Quality Services Ltd as a wholly-owned subsidiary to provide, on a commercial basis, food safety, quality assurance and training services to the dairy and wider food industries.

Impetus for deregulation

3.5.69 Over a number of years, the regulated environment for market milk provided the Australian dairy industry with relatively stable returns and allowed it to achieve a high level of international competitiveness. However, manufacturers of dairy products became increasingly concerned about their competitive position, given that imported dairy products did not incur the levy paid by Australian manufactures under the Domestic Market Support Scheme. This level of concern was particularly high in Victoria, which produces approximately 63 per cent of all milk and 72 per cent of Australia's manufacturing milk.

3.5.70 The end of the agreement associated with the Domestic Market Support Scheme on 30 June 2000 and the impact of the Commonwealth Government's National Competition Policy (NCP), which required each State Government to review its dairy legislation by 2000 to determine whether its legislation restricted competition, provided the industry with an opportunity to move to a deregulated market.

3.5.71 A NCP review of Victoria's *Dairy Industry Act* 1992 was completed in July 1999. The findings of the review supported the deregulation of the dairy industry in Victoria and recommended winding-up the VDIA, but concluded that there would be public benefit in continuing the State's regulatory function over food safety.

3.5.72 In August 1999, the then State Minister for Agriculture and Resources accepted the recommendations of the review team and announced that the operation of the VDIA would be terminated on 1 July 2000.

3.5.73 In order to facilitate the deregulation of the industry, 2 working groups, the Dairy Food Safety Working Group and the Dairy Industry Services Working Group were established. These groups, which included representatives of industry and government, were required to review the future arrangements for dairy food safety and the management of the residual assets of the VDIA, respectively.

3.5.74 However, with the change in State Government in September 1999, the newly elected government requested that the 2 working groups not complete their reviews until it had made a decision on the deregulation of the industry.

3.5.75 The 2 working groups, which reported in February 2000, recommended that a statutory authority to regulate dairy food safety be established and that the net assets of the VDIA be transferred to a new legal entity and be used for the benefit of the Victorian dairy industry and people who reside within dairy farming regions.

PHOTO NOT AVAILABLE

Friesian dairy cows out to pasture.

Dairy Industry Adjustment Package

3.5.76 In April 1999, the Australian Dairy Industry Council (ADIC) submitted a proposal to the Commonwealth Government seeking a national milk industry restructure package to encourage deregulation of the market milk industry in Australia and help manage the impact of the deregulation.

3.5.77 In response to this proposal, the Commonwealth Government announced a $1.78 billion Dairy Industry Adjustment Package. Provision of assistance under the package was conditional on dairy farmers in all States agreeing to remove existing controls over the production and sale of market milk by 30 June 2000.

3.5.78 The package comprises 3 programs, the details of which are outlined below:

- Dairy Industry Structural Adjustment Package, to assist dairy farmers to restructure their business in order to operate successfully in a commercial environment ($1.63 billion was to be provided over 8 years, with Victorian dairy farmers to receive approximately $740 million);
- Dairy Exit Program, to provide eligible dairy farmers who elect to exit the industry with a tax free payment of up to $45 000 each (Program is expected to cost $30 million); and
- Dairy Regional Assistance Program, to provide project specific funding to assist dairy farming regions develop new industries and deal with social issues caused by deregulation (Program is expected to cost $45 million over 3 years).

3.5.79 Funding for the package was provided by a levy of 11 cents per litre on market milk, collected at the wholesale level.

3.5.80 In October 1999, the State Minister for Agriculture announced that the deregulation of the dairy industry would not proceed without the support of the industry, as indicated by a Statewide poll of dairy farmers.

Deregulation of the dairy industry

3.5.81 The vast majority (89 per cent) of Victorian dairy farmers, who participated in the State Government's December 1999 dairy industry poll, voted in favour of deregulating the dairy industry and accepting the Dairy Industry Adjustment Package. Following the outcome of the poll, the Minister for Agriculture, at a joint meeting of State Agriculture Ministers in December 1999, announced that Victoria would deregulate its dairy industry.

3.5.82 Price and supply controls on milk in Victoria were removed by the State Government with the passing of the *Dairy Act* 2000, which came into operation on 1 July 2000. Specifically, the Act:

- repealed the *Dairy Industry Act* 1992;
- established a statutory body known as Dairy Food Safety Victoria as the successor of the VDIA;
- provided a licensing system for the dairy industry; and
- enabled Codes of Practice and food safety programs to be implemented in relation to dairy food.

3.5.83 In accordance with the Act, the VDIA ceased operating on 26 October 2000 at which time its net assets were distributed to Dairy Food Safety Victoria and the Geoffrey Gardiner Dairy Foundation.

Dairy Food Safety Victoria

3.5.84 Dairy Food Safety Victoria commenced operations on 30 September 2000, with responsibility for safeguarding public health in the Victorian dairy industry.

3.5.85 An amount of $1.86 million was provided by the VDIA to fund the establishment of the new authority and assist with transitional arrangements. **This amount consisted of $1.8 million, specified under the *Dairy Act* 2000, to establish the Authority and an additional sum of $65 000 for costs associated with the appointment of the Board.**

3.5.86 Future funding of the authority will be provided through a combination of fees-for-services provided by the authority and from license fees issued to dairy farmers, manufacturers, food carriers and distributors, with the authority expected to become fully self-funding within 2 years.

The Geoffrey Gardiner Dairy Foundation

3.5.87 The Geoffrey Gardiner Dairy Foundation, a company limited by guarantee, was established under the Corporations Law on 11 October 2000 to receive the residual assets of the VDIA following the establishment of Dairy Food Safety Victoria. The Foundation was developed by Victorian dairy farmers, processors and manufacturers, in consultation with the Department of Natural Resources and Environment, and the Department of Treasury and Finance. The assets and liabilities of the VDIA were transferred to the Foundation on 27 October 2000.

3.5.88 According to its constitution, the Foundation can engage a maximum of 5 directors, comprising a person with knowledge and experience in dairy farming, a person with knowledge and experience in dairy processing and manufacturing, an independent person with knowledge and experience in finance and investment, an independent person with knowledge and experience in dairy industry development activities, and an independent chairperson.

3.5.89 The Foundation's membership, which is not limited, must be drawn from dairy farmers, milk processors and manufactures. The initial membership of the Foundation consisted of the United Dairy Farmers of Victoria, the Milk Processors Association of Victoria and the Victorian Dairy Products Association.

3.5.90 The Foundation's objective is to manage the investment of funds allocated to it by the VDIA in order to maximise the benefit to all sectors of the Victorian dairy industry and dairy farming regions. Specifically, the Foundation is required to:

- fund and promote dairy industry development activities including the gathering, analysis and dissemination of information, research and development, education and training, and management of intellectual property;
- spend or commit a total of $3 million over 3 years to community support activities including support activities for families who own or operate a Victorian dairy farm, change management programs for people who reside within dairy farming regions, local infrastructure programs within dairy farming regions, and regional economic programs benefiting dairy farming regions; and
- make available a maximum of $300 000 per year for 2 years for dairy herd improvement services to Victorian dairy farmers previously funded by dairy license fees, which were paid by the VIDA to the Dairy Herd Improvement Fund administered by the National Herd Improvement Association.

3.5.91 The Foundation's constitution imposes a number of reporting and accountability requirements on it, including:

- preparation of a strategic plan for the investment and expenditure of funds;
- preparation of an annual operating plan including an expenditure program to achieve the Foundation's expenditure obligations;

- preparation of an annual report containing details of the Foundation's investment strategy and investment performance, and expenditure necessary to fulfil its objectives, including a description of all projects or activities that have received funding and the amount of the funding; and
- auditing of the Foundation's records in accordance with the Corporations Law.

3.5.92 In addition, the Foundation is required to be wound-up, within a period of 6 months, if its unapplied funds are reduced to less than $1 million or its annual income is reduced to less than $500 000.

3.5.93 **Net assets transferred to the Foundation from the VDIA amounted to $62.6 million and expenditure incurred by VDIA, associated with the formation of the Foundation was $11 000. The majority of the net assets transferred related to proceeds from the sale of the VDIA's fixed assets and intellectual property.**

3.5.94 Thus, a significant amount of assets formerly managed by the VDIA, a government statutory authority, have been transferred to a private company for use in accordance with the *Dairy Act* 2000. **Although the private company is required to table audited annual financial reports in the Parliament, no independent review mechanism has been established to ensure that the funds transferred to the company are spent in accordance with the intentions of Parliament as outlined in the Act.**

Sale of milk brands

3.5.95 During the late 1970s and early 1980s the VDIA introduced the Big M, Skinny Milk, REV and Farmhouse milk brands to promote the consumption of milk in Victoria. Use of these brands was available to the industry in return for the payment of franchise fees, which were used to fund brand advertising and promotion, and at the time of their sale were used by 8 milk processors. Marketing and promotion of the brands was undertaken by the VDIA up until 1994 when this function was licensed to Australian Milk Marketing, a not-for-profit company.

3.5.96 In June 2000, the VDIA announced the decision to sell the milk brands. The brands were sold individually by way of tender, with the right to tender limited to parties licensed to conduct a business as a milk factory or processor. As a condition of sale, the 8 milk processors, currently using the brands, were entitled to continue using the brands for a period of 3 years following the date of their sale.

3.5.97 The sale process consisted of the following 4 phases:

- submission of expressions of interest in late July 2000;
- submission of non-binding indicative offers in mid-August 2000;
- conduct of due diligence investigations by interested parties; and
- submission of final binding offers by short-listed parties.

3.5.98 **In September 2000, following an evaluation of the offers received, the Big M brand was sold to National Foods and the REV, Skinny Milk and Farmhouse brands were sold to Parmalat Foods. The sale of the brands generated $57.2 million for the VDIA, with costs associated with the sale process amounting to $686 000.**

3.5.99 These funds formed part of the $62.6 million in net assets transferred by the VIDA to the Foundation.

Sale of shareholding in Chinese joint venture

3.5.100 Our May 1998 *Report on Ministerial Portfolios* commented on the VDIA's participation in a joint venture arrangement involving the manufacture and marketing of Big M milk products in China. The Report disclosed that from its inception in June 1995 to May 1998, the joint venture had cost the VDIA in excess of $1.2 million. With the winding-up of the joint venture it is now possible to disclose the full cost of the VDIA's involvement in this arrangement.

3.5.101 The VIDA initially invested $730 000 in the joint venture arrangement, the key objectives of which were 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.

3.5.102 From its commencement the joint venture experienced lower than anticipated demand for its products, operational difficulties and pressure on its selling prices. As a result, the joint venture never generated a profit.

3.5.103 In April 2000, the VDIA sold its interest in the joint venture to the Tianjin Dairy Corporation, a division of the Tianjin Farm Bureau which was the VDIA's original Chinese partner in the venture, for $50 000. This amount was $342 000 less than the value of the VDIA's share of the net assets of the joint venture. Expenses related to the sale of the joint venture totalled $91 300.

3.5.104 **At the time of the sale, the VDIA's share of the joint venture's accumulated losses totalled $1.2 million and its initial investment of $730 000 in the joint venture had been written-down to zero.**

3.5.105 **When the VDIA's direct costs associated with the management of, and accounting for, the joint venture are included, the overall cost to the VDIA as a result of its involvement in the joint venture was in excess of $2 million.**

3.5.106 An important element of the sale of the VDIA's interest in the joint venture was the mutually agreed termination of the Technology Licence Agreement, which enabled the Chinese Big M trademark to be included in the milk brand sale without any licensing obligations attached.

Sale of Food Quality Services Ltd

3.5.107 As indicated earlier in this Report, Food Quality Services Ltd was a wholly-owned subsidiary of the VDIA, established to provide food safety, quality assurance and training services to the dairy and wider food industries. Although the company was originally intended to be self-funding, the VDIA has provided it with a total of $1.2 million to fund its operations since it commenced trading in July 1997.

3.5.108 In October 1999, the VDIA sold the company to John L Bates and Associates following a public tender process. **Proceeds of $25 000 generated from the sale were $48 900 less than the carrying value of the company's net assets. The sale process also incurred costs of $72 000.**

***RESPONSE** provided by the Secretary, Department of Natural Resources and Environment*

The Geoffrey Gardiner Dairy Foundation

Clause 24.3 of the company's constitution states that "The Board will comprise the following Directors:

- *an independent Chairperson (currently Mr Chris Nixon);*
- *a person with knowledge and experience of the Victorian dairy farming sector (currently Mr Max Fehring, President of the United Dairyfarmers of Victoria);*
- *a person with knowledge and experience of the Victorian dairy processing and manufacturing sectors (currently Mr Ian MacAulay, Chairman of Murray Goulburn Co-operative Co. Ltd);*
- *an independent person with knowledge and experience in finance and investment (not yet appointed); and*
- *an independent person with knowledge and experience relevant to the Dairy Industry Development Activities (not yet appointed).*

For the purposes of this clause, "independent" means that the person is not a current employee or officer of a Member, and is not a current employee, officer or proprietor (whether of the whole or a part, but excluding the holding of 5 per cent or less of the equity or capital of a business, company, trust or partnership) of a dairy farm business, dairy processor business or dairy manufacturer business.

DNRE believes that the Foundation has adequate review mechanism to ensure that the funds are spent in accordance with the intentions of Parliament. The Foundation's membership, which includes all sectors of the industry, will provide a high level of scrutiny of the Foundation's performance in delivering the objects of the company specified in the constitution. This scrutiny will be enhanced by the reporting and accountability requirements in the constitution (clause 30) which involve industry, community and government stakeholders and by the requirement to provide the Annual Report to Parliament (clause 32.3). The constitution requires that any amendment or addition to the constitution receives the consent of the Minister for Agriculture (clause 13.2). Furthermore, in the event of the company winding-up, any surplus must go to a successor body(s) having objectives consistent with the objects of the company and approved by unanimous resolution of each class of Member and by the Minister (clause 49.3).

BUY-OUT OF BAY AND INLET COMMERCIAL FISHING ACCESS LICENCES

3.5.109 Fishing within Victoria can be broadly classified into 3 categories: ocean and off shore fishing (which is primarily the responsibility of the Commonwealth Government); inland fishing in lakes, rivers and streams; and bay and inlet fishing. Both inland fishing and fishing in bays and inlets are the responsibility of the State Government.

3.5.110 The State has more than 30 bays, inlets and estuaries that collectively cover more than 3 700 square kilometres.

3.5.111 The waters of Victoria's bays and inlets provide ecologically distinct environments to those existing in inland waterways and the ocean, and are the home to a variety of commercial fish resources, which include:

- scale fish - bream, flathead, mullet, snapper, whiting and trevally;
- crustaceans – crabs and prawns;
- shellfish - abalone, mussels and scallops;
- cephalopods – southern calamari, squid, cuttlefish and octopus; and
- shark.

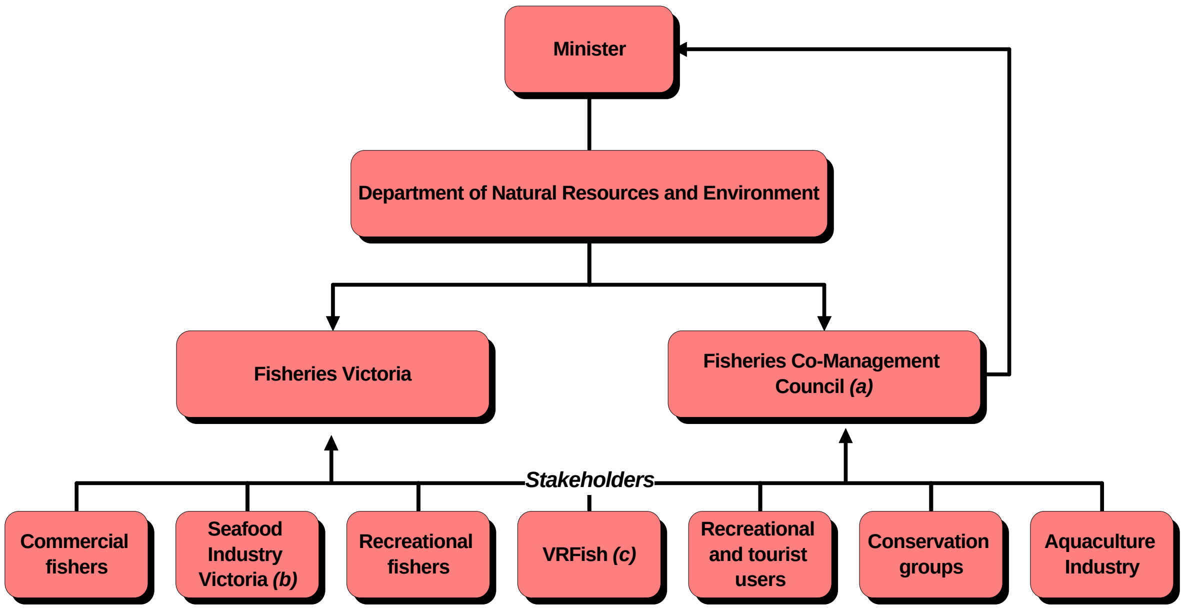
3.5.112 All commercial and recreational fishing activities in Victorian bays and inlets are controlled by the provisions of the *Fisheries Act* 1995, which provides the "legislative framework for the regulation, management, and conservation of Victorian fisheries including aquatic habitats".

3.5.113 In accordance with section 90 of the Act, the Fisheries Co-Management Council was established to promote the co-management of fisheries and provide advice to the responsible Minister on:

- Statewide priorities for fisheries management and fisheries research, and on matters relating to intergovernmental agreements and arrangements; and
- the introduction and issue of recreational fishery licences in marine waters and on the priorities for disbursement of funds obtained from such licences.

3.5.114 Victoria's bay and inlet fish resources are community assets managed, on behalf of a diverse group of stakeholders, by Fisheries Victoria (a business unit within the Department of Natural Resources and Environment). These stakeholders and the administrative arrangements for the management of the State's fish resources are outlined in Chart 3.5K.

CHART 3.5K
STAKEHOLDERS AND ADMINISTRATIVE ARRANGEMENTS



(a) Resources provided by the Department of Natural Resources and Environment and, as it is not a separate reporting entity, it is accountable to that Department.

(b) Seafood Industry Victoria represents commercial fishers.

(c) VRFish - the Victorian Recreational Fishing Peak Body.

Commercial fishing

3.5.115 The commercial fishing industry is regulated through the issue of fishing licences in accordance with the Fisheries Regulations 1998. These licences control fishing by:

- limiting the areas fished to 8 of Victoria's bays and inlets (Port Phillip and Western Port Bays are included together) and the number of licences issued within these areas (refer to Chart 3.5L);
- specifying, within each licence, the types of fish resources that can be caught; and
- through a variety of controls, which restrict the type and specifications of fishing gear permitted, regulate the equipment used, limit the catch size for certain fish species, specify fishing access times and designate areas closed to fishing.

CHART 3.5L
LOCATION OF BAYS AND INLETS SUBJECT TO COMMERCIAL AND RECREATIONAL FISHING ACTIVITIES PRIOR TO THE BUY-OUT PROGRAM

CHART NOT AVAILABLE

3.5.116 The various types of commercial fishing equipment permitted by the regulations include:

- Seine nets, (used to generate approximately 61 per cent of the total annual value of the bay and inlet catch) which are flat usually rectangular nets with a weighted bottom edge and buoyed upper edge. The types of fish nets used (e.g. haul seines and purse seines), the mesh size, length of net and method of operation vary according to the gear restrictions applying to the particular embayment and fish species targeted;
- Mesh (gill) nets, account for approximately 28 per cent of the annual catch value, are flat rectangular nets with a weighted bottom edge (lead line) and buoyed upper edge (float line);
- Long lines, account for approximately 8 per cent of the annual catch value, are made of long, usually monofilament mainlines weighted at each end and are mostly used to catch snapper; and
- Hand lines, account for approximately 3 per cent of the annual catch value, are occasionally used by commercial fishers, usually in conjunction with other fishing techniques. This technique is largely directed towards catches of calamari or King George whiting in Port Phillip Bay.

3.5.117 There are no restrictions on the amount of fish a licensee is able to catch, however, commercial licence holders are prohibited from fishing during weekends.

3.5.118 Prior to March 2000, licences were either transferable (Gippsland Lakes, Port Phillip/Western Port, Mallacoota and Corner Inlets) or non-transferable (Lake Tyers, Shallow, Andersons and Tamboon Inlets).

3.5.119 Historically, commercial fishing in Victoria's bays and inlets has been characterised by family-owned businesses, which have held licences for long periods of time, in some cases up to 5 generations.

3.5.120 Commercial fishing access licences were first made compulsory in the late 1960s with the issue of new licences restricted during the 1970s.

3.5.121 In 1987, the State Government initiated procedures designed to:

- reduce the number of licences in Gippsland Lakes, Port Phillip/Western Port, Mallacoota and Corner Inlets, through consolidating licences on their transfer (licences to fish these bays and inlets could only be obtained by purchasing 2 existing licences which were then consolidated into one licence); and
- phase-out commercial fishing from the 4 smaller bays and inlets of Tamboon, Lake Tyres, Shallow and Andersons Inlets following the retirement of existing licence holders.

3.5.122 Commercial fishers are required to pay annual fees to enable access to fish resources. The standard fee for the issue or renewal of a commercial licence is $32. Licence transferees pay an additional $562. Licence renewals attract a further fee of $390 for management compliance and research.

PHOTOS NOT AVAILABLE

Commercial fishers in operation.
(Photos courtesy of Seafood Industry Victoria.)

Review of bay and inlet fisheries

3.5.123 In January 1997, VRFish (the Victorian Recreational Fishing Peak Body) presented a submission to the then Minister for Agriculture and Resources which recommended:

- complete banning of commercial netting in bays and inlets from January 1998;
- introduction of a recreational fishing licence, which covered both fresh water and marine fishing, with part of the revenue raised by the licence used to fund research on behalf of recreational fishers; and
- establishment of catch quotas and species specific commercial fishing licences.

3.5.124 VRFish's preferred option of banning commercial fishing included a scheme to buy-out commercial licences, which was to be funded from a government interest-free loan to be paid back over 5 years, with money generated from the issue of recreational licences.

3.5.125 In April 1997, the Minister for Agriculture and Resources requested the Council, to conduct a review of commercial and recreational fishing for scale fish in Victoria's bay and inlet fisheries and their management.

3.5.126 The aim of the proposed review was to achieve "a balanced approach between commercial netting practices, recreational fishing, consumers and environmental matters in Victoria's bays and inlets to ensure sustainable fisheries for the State". The review represented a comprehensive analysis of the management of scale fish in Victorian bays and inlets, drawing on the expertise of 5 independent consultants.

3.5.127 Following completion of the review, the Council generated a report late in 1997 which identified that:

- **the sustainable future of bay and inlet fisheries was far more seriously threatened by habitat and environmental degradation than by current recreational or commercial fishing activities;**
- there would be little if any increase in the net economic benefit from significantly altering the current allocation of commercial and recreational shares of bay and inlet catches; and
- many bay and inlet commercial fishing licences were under-utilised and the economic viability of some commercial operators was marginal and that a reduction in licence numbers could remove latent effort and improve the economic viability of the remaining licence holders.

3.5.128 The threats to fish habitats identified by the review can be broadly classified into 3 categories:

- Degradation of water quality due to increased nutrients, sedimentation and turbidity, reduction in dissolved oxygen concentration, alteration of natural salinity regimes, and introduction of toxicants. (Degradation of water quality has detrimental effects on habitats and their dependent fish.);

- Physical disturbance which damage, cause stress and alter habitats including dredging and disposal of spoil, foreshore development and general human disturbance. (Physical disturbance is a major causal factor in the loss of habitat and reduction in habitat health.); and
- Introduction of exotic pest species such as starfish. (Exotic species may have adverse effects on fish habitats through the displacement of indigenous species, or compromising the integrity of local habitats and ecosystems.).

3.5.129 The review also disclosed that of the total commercial licence holders, 116 (59.5 per cent) were full-time, 42 (21.5 per cent) were part-time and 37 (19 per cent) were not fishing. (A number of commercial licence holders have more than one commercial licence.) Most part-time fishers are semi-retired and include a small number who have other businesses and sources of income. Part-time fishers are assumed to spend 20 per cent of their "working time" fishing.

Licence buy-out program

3.5.130 Prior to July 1999, recreational fishers were not required to be licensed except when fishing in Victorian inland waterways. The licence relating to Victorian inland waterways authorised the holder to take fish, other than for sale, using recreational fishing equipment. At that time, 100 000 licences had been issued generating approximately $1.77 million in revenue per annum.

3.5.131 In November 1998, the Minister for Agriculture and Resources announced a voluntary buy-out of commercial fishing access licences for all Victorian bays and inlets, which would be funded from the proceeds generated through the introduction of a general recreational fishing licence covering all fishing in the State.

3.5.132 On 15 July 1999, the All-waters Recreational Fishing Licence (AWRFL) was introduced in Victoria, with fees ranging from $5 for 2 days to $20 for an annual licence. The AWRFL was the first such licence to be introduced in Australia. In the first year of its introduction, 240 000 licences were issued, generating $3.87 million in revenue.

3.5.133 Responsibility for managing the commercial-scale fishing access licence buy-out program was assigned to the Council by the Minister. As the Council had 11 members, who between them have commercial fishing, fish processing, fish marketing, recreational fishing, traditional fishing uses, aquaculture, conservation and fisheries science experience and knowledge, the Council's role in the buy-back process provided commercial and recreational fishers an opportunity for input into the buy-out process.

3.5.134 In January 1999, a 3 person Sub-Committee of the Council was formed with the primary objective of achieving "***the voluntary surrender of the maximum number of licences without affecting commercially caught fish supplies***". Discussions with the Council indicated that this objective was not developed by the Council but directed by the Minister.

3.5.135 **As there was an explicit requirement that the size of the catch should not be reduced as a result of the buy-back, it was apparent that the primary aim of the scheme was to increase the economic viability of commercial fishers, rather than part of a broader strategy to ensure the sustainability of fish resources or to meet the expectation of recreational fishers for greater access to fish stocks.**

3.5.136 A secondary objective of the buy-out was to remove *latent effort* from the industry. (Latent effort occurs where a valid commercial fishing licence is not being actively utilised - that is, little or no fishing occurs.)

3.5.137 Other objectives of the buy-out involved ensuring the process was completed within a short timeframe, was fair and equitable, unambiguous, without discrimination, litigation free and inexpensive to administer. The Council and the Department were eager not to create an environment where the Department could be subject to litigation similar to that which applied following the discontinuation of scallop fishing in May 1996. At that time, there were concerns within the community regarding the impact of scallop dredging on the sea bed of Port Phillip Bay. As a consequence, the Government decided to legislate to end scallop fishing in the bay by compulsorily purchasing all existing licences for $120 000 per licence. The Government's decision caused considerable industry unrest and was subsequently challenged in the Supreme Court by scallop fishers.

3.5.138 To assist in the formulation of recommendations for the voluntary buy-out program, the Sub-Committee of the Council sought advice from a range of sources, including:

- A Reference Committee with membership drawn from existing Council committees including the Commercial Bays and Inlet Fishery Committee, the Recreational Marine Committee and the Inland Committee. The Reference Committee provided advice on the offer prices associated with an "invitation to treat" and the anticipated cost of the program. The Committee recommended that an "invitation to treat" be extended to all licence holders with the thrust of the invitation being that it was a "once only" request to licence holders to submit an irrevocable offer to surrender their licence for a fixed sum;
- Fisheries Victoria, provided the sub-committee with a proposal based on a buy-out methodology where latent and part-time licensees in each bay and inlet fishery would be offered a fixed price determined for that fishery as a multiple of the average annual net income. Full-time licensees would be invited to indicate the level of compensation they would require to surrender their licence; and
- An external Consulting Economist was engaged, following a review of the alternate schemes under consideration by the sub-committee, to make a recommendation on the most appropriate scheme. While the consultant had a preference for separate negotiations with individual licence holders, such a process was considered to be too expensive and time consuming.

3.5.139 Following consideration of the various information it had received, the Sub-Committee of the Council recommended, among other things, that:

- An "Invitation to Treat" be offered to all bay and inlet commercial licence holders (except the holders of "pensioner category" reduced fee access licences). The thrust of the invitation was to be a once only request to licence holders to submit an irrevocable offer to surrender their licences for a fixed sum;
- That the Invitation remain open for 2 months, and that acceptance should be honored within 3 months of the offer, funded by an advance provided by the State Government;
- In the event that the offer was oversubscribed, additional funding be sought so that the maximum number of licences can be removed from bay and inlet fisheries; and
- That the offer should include information on the likely future operations of commercial fishing in Victoria's bays and inlets, including possible future increases in licence fees, continuing the freeze on licence transfers, and possible future management changes, which may influence licence holders in their decision on whether to sell their licences.

3.5.140 In making its recommendations for the buy-out, the Sub-Committee discounted the use of a sealed bid process, did not take into account catch history, and did not differentiate between consolidated and unconsolidated licences. The Council accepted the recommendations of the Sub-Committee and then submitted the recommendations to the former Minister for Agriculture and Resources.

3.5.141 **Following the Ministers acceptance of the Committees recommendations, the Department initiated the licence buy-out scheme which resulted in the removal of more than half of the commercial fishing licences for Victorian bays and inlets for an average purchase price of $74 000. The voluntary buy-back scheme will be ultimately funded by the $20 recreational licence for anglers**.

3.5.142 An independent review of the buy-out program was initiated in November 2000 and at the date of preparation of this Report, the Minister for Energy and Resources was considering a report on the outcome of that review.

Basis of calculation of inducement for the voluntary surrender of licences

3.5.143 The Council's 1997 review recommended that any proposal to remove commercial licences would need to take into consideration the social impacts of the removal of licence on fishers and their families. Surveys conducted by the Council disclosed that all commercial fishing licence holders are male, with an average age in excess of 50 years. Their skills are largely limited to those associated with fishing and in many cases their families have been dependent on the income generated from fishing for several generations. The review indicated that, if commercial fishers were suddenly prevented from fishing, without compensation, there would be a significant negative impact on them and their families, whereas a staged buy-out process, with compensation, would minimise any adverse impacts.

3.5.144 During the buy-out process, restrictions were placed on the transfer of commercial licences. As there was no extensive trading in licences prior to the buy-out program, it was assumed by the Council that there were insufficient inducements for licence holders to exit the fishing industry. As a result, the Sub-Committee of the Council was of the view that it would need to provide an amount in excess of the market price to tempt licence holders to relinquish their licences.

3.5.145 Although the primary objective of the buy-out was to obtain the voluntary surrender of the maximum number of licences, the Council's aim was to buy back at least half of the licences issued at that time. According to advice received from the Sub-Committee, had the voluntary surrender of licences been under-subscribed, the buy-out process would have been perceived to have failed.

3.5.146 The prices offered for commercial licences were determined by the Council's Sub-Committee, following discussions with Fisheries Victoria staff and receipt of recommendations from a Reference Committee Workshop involving both commercial and recreational representatives. **The Sub-Committee recommended the payment of $80 000 for transferable licences relating to Gippsland Lakes, Port Phillip/Western Port, Mallacoota and Corner Inlets; $60 000 for non-transferable licences relating to Tamboon Inlet and Lake Tyers; and $30 000 for non-transferable licences relating to Shallow and Andersons Inlets.** The various sums offered were "inducement figures" aimed primarily at latent and part-time fishers and those who considered that they had only limited future in fishing.

3.5.147 **These offer prices were determined despite information in the Council's 1997 review which, based on survey information, estimated the value of licences to be within the range of $15 000 to $70 000, depending on where the licence entitled fishers to operate.**

Results of the buy-out program

3.5.148 **The licence buy-out program, which was completed in March 2000, resulted in the removal of 108 (52 per cent) of the 208 licences on issue at a cost of $8 million. The buy-out was funded from an initial $6 million advance from the State Government, and a further $2 million advance provided when the offer was over-subscribed**. At 30 June 2000, $3.5 million of this advance had been repaid, funded from the newly introduced recreational fishing licence, with the remaining $4.5 million to be repaid by June 2003. Table 3.5M summarises the results of the licence buy-out.

TABLE 3.5M
COST OF LICENCE BUY-OUT

	Licences prior to buy-out	*Acceptances*	*Remaining licences*	*Licences removed*	*Buy-out cost per licence*	*Total buy-out cost*
	(no.)	*(no.)*	*(no.)*	*(%)*	*($'000)*	*($'000)*
Transferable licences						
Gippsland Lakes	32	13	19	41	80	1 040
Port Phillip/Western Port	115	62	53	54	80	4 960
Corner Inlet	30	10	20	33	80	800
Mallacoota Inlet	8	4	4	50	80	320
Non-transferable licences						
Andersons Inlet	4	4	0	100	30	120
Shallow Inlet	5	5	0	100	30	150
Lake Tyers	10	7	3	70	60	420
Tamboon Inlet	4	3	*(a)* 1	75	60	180
Totals	**208**	**108**	**100**	**52**	**74**	**7 990**

(a) The Department has subsequently refused to renew this licence. The licence holder is currently appealing against this decision.

3.5.149 The above table discloses that the removal of commercial licences ranged from 33 per cent in Corner Inlet to 100 per cent in Anderson's Inlet and Shallow Inlet.

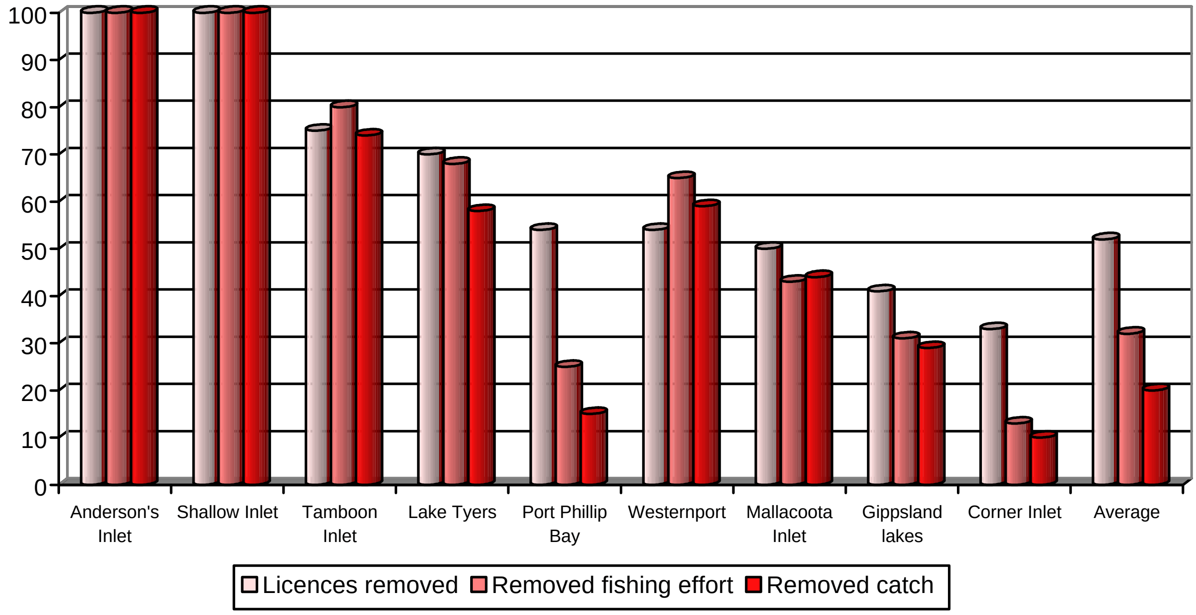
3.5.150 Administrative costs associated with the buy-out, which were absorbed within the Department's and the Council's respective operating budgets, were minimal.

3.5.151 In order to determine the likely impact of the buy-out on commercial fishing, especially on latent fishing licences, audit reviewed an analysis undertaken in October 2000 by the Department's Marine and Freshwater Resources Institute (MAFRI). The State Government established MAFRI to provide research, consultancy and education services required for the sustainable management of aquatic resources and their environment.

3.5.152 The analysis undertaken by MAFRI assessed the impact on each fishery of removing commercial licences, using the catch history of these licences for the period prior to the buy-out, as reported in catch returns generated by commercial fishers from 1995 to 1999. As indicated above, **the buy-out removed 52 per cent of fishing licences which based on previous catch and effort history accounted for 32 per cent of the total effort (fishing days) and 20 per cent of the total catch. In addition, 61 licences that were removed, (56 per cent) related to full-time fishers**.

3.5.153 Chart 3.5N illustrates the impact of licences removed on fishing days and total catch, which assumes that the remaining commercial fishers do not increase their fish take following the buy-out. However, it is likely that the overall fish take in areas other than Shallow and Andersons Inlets will remain relatively stable following the buy-out, as the remaining licensees take advantage of reduced competition to increase their yield.

CHART 3.5N
IMPACT OF LICENCES REMOVED BASED ON FISHING EFFORT AND CATCH HISTORY, 1995 T0 1999
(per cent)



Source: Information provided by MAFRI.

3.5.154 From a review of the chart it is evident that the buy-out reduced latent effort. This was particularly evident in Port Phillip Bay and Corner Inlet.

Has the program achieved its objectives?

3.5.155 As part of our audit review we assessed the effectiveness of the buy-out process in respect of the extent to which it achieved its primary objective and also in respect of its impact on the stakeholders and the environment.

3.5.156 As indicated earlier in this Report, the primary objective of the program was "the voluntary surrender of the maximum number of licences (within the confines of available funding) without affecting commercially caught fish supplies".

3.5.157 We consider that the buy-out process achieved its primary objective based on the following findings:

- A voluntary process was adopted;
- Given the amount of funding available for the buy-out was fixed, the Council probably removed the maximum number of licences; and
- MAFRI advised that it is too early to determine whether the supply of fresh fish to the community was been maintained. However, assuming that all other factors such as the fish stocks and market prices remain the same, the overall fish catch is not expected to diminish as the remaining fishers are likely to increase their fish take as a result of a decrease in commercial competition.

3.5.158 Furthermore, audit found that the recreational and commercial fishing peak bodies and the Council all agreed that it was appropriate to use revenue generated from recreational fishing licences to fund the buy-out.

Impact on commercial fishers

3.5.159 **With the voluntary nature of the buy-out scheme and the remaining licensees having the ability to increase their fish take, commercial fishers stood to benefit from the buy-out.** While some commercial fishers could choose to exit the industry and receive a monetary benefit, the remaining fishers benefited by having greater access to fish stocks, due to the reduced competition from other commercial fishers with the value of their licences increasing as the number of licences reduced.

3.5.160 This observation is supported by a departmental survey of all fishers who accepted the buy-out offer, which disclosed that 58 per cent of respondents indicated that they thought the buy-out program had achieved its objectives. In addition, 41 per cent of respondents cited personal (retiring and ill health) and financial considerations as the primary reasons for accepting the offer.

3.5.161 Issues raised by fishers responding to the survey, that were either uncertain or did not believe the program to be a success, included the lack of clarity regarding the buy-out objectives and concern that the buy-out alone would not ensure a sustainable future for bay and inlet fisheries. A number of fishers were also concerned with the impact of, and the lack of regulation over, the operations of recreational fishers, on the future sustainability of fisheries. Some responses suggested that a similar outcome to that achieved by the buy-out process could have been attained by increasing restrictions on commercial and recreational fishers.

Impact on recreational fishers

3.5.162 Discussions with VRFish indicated that, prior to the buy-out, recreational fishers had a number of concerns with commercial fishing operations in Victoria's bays and inlets including their belief that:

- catches taken by commercial fishers reduce the quantities of fish available for recreational fishers with consequent effects on recreational catch rates;
- commercial netting represents a threat to the sustainability of some fish stocks, specially in relation to the level of target catch removed and the perceived impacts on the juveniles of target species such as King George whiting, black bream and snapper;
- some nets used (and the manner in which they are used) by commercial fishers kill large quantities of under-sized and non-target species; and
- some netting methods used by commercial fishers have adverse impacts on important fish habitats such as seagrass and light reef areas.

3.5.163 These concerns were raised in the January 1997 VRFish submission to the former Minister of Agriculture and Resources, which recommended the banning of net fishing in Port Phillip and Western Port Bays.

3.5.164 **The buy-out is expected to have negligible impact on the commercial fish catch in bays and inlets with the exception of Shallow and Anderson's Inlets, and has not directly addressed recreational fishers' concerns with net fishing**.

3.5.165 In order to ascertain whether the concerns raised by recreational fishers were soundly based, audit held discussions with the Council, Fisheries Victoria and MAFRI. Based on these discussions and the research undertaken by the Council, it appears that:

- In most cases, environmental changes in bays and inlets have greater impacts on fish resources than either commercial or recreational fishing. For example, in Western Port Bay declines in fish catches during the 1970s and 1980s correlated with the loss of 170 square kilometres of seagrass. Similar impacts have been observed in Corner Inlet;
- There is little evidence of substantial adverse impacts on habitats from commercial fishing. Specifically, seine nets are considered to have negligible impacts on seagrass; and
- Commercial seine netting is likely to have little impact on the mortality of juvenile and non-target fish, provided that good netting practice is followed.

Economy of the buy-out process

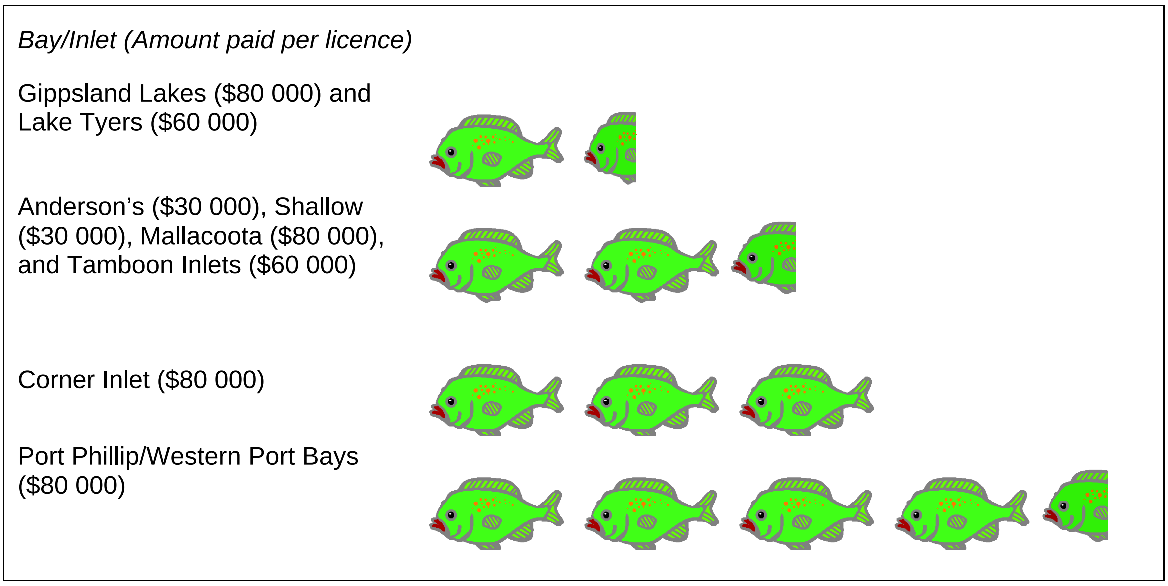
3.5.166 In any licence buy-out, the structure of the process employed determines the likely impact of the buy-out on the resource manager. At one extreme, a voluntary system with a set price is likely to provide an easily managed process, which can be completed in a short time frame with minimal administration and litigation costs.

3.5.167 At the other extreme a targeted system where the price paid is determined for each licence, based on factors such as the type of licence, the level of licensee activity and the location and fish resources in that fishery, is more likely to ensure the maximum benefit to the government at the lowest purchase cost. This approach could also be used to target areas where over fishing is adversely impacting on fish resources. However, such a process is likely to be more difficult to manage and result in higher administrative and litigation costs.

3.5.168 Without forming a view on the appropriateness of the buy-out scheme chosen by the Council in this instance, it is fair to say that **a differently structured buy-out, where the factors relevant to each licence was taken into account when setting the purchase price, would in all likelihood, have achieved a similar outcome in terms of a number of licences removed at a substantially reduced cost per licence.**

3.5.169 **It is also worth noting that the method chosen for the buy-out has created significant differences in the benefits received by fishers in different locations.** Chart 3.5O shows the price paid for licences as a multiple of the average net annual cash income per fisher generated from the respective bays and inlets. As can be seen from the chart the amount paid for licences in Port Phillip and Western Port bays was 4.5 times the fishers' average net annual cash income, whereas for Gippsland Lakes and Lake Tyers, fishers received on average only 1.7 times their average net annual cash income.

CHART 3.5O
PRICE PAID FOR COMMERCIAL LICENCES AS A MULTIPLE OF AVERAGE ANNUAL NET INCOME PER FISHERY *(a) (b)*



(a) Each fish represents the average net annual cash income generated by licence holders operating in the respective bay/inlet.

(b) Quantum of fish relating to each bay/inlet represents the amount paid for the buy-out of each licence.

3.5.170 Audit also consider that it would have been prudent if other options had been explored to maximise the return from public funds generated from the All Waters Recreational Fishing Licences. Such options include, among other things:

- selectively buying-out licences in areas which are over fished or where there are too many fishers; and
- applying sections 57 and 58 of the Act which requires licensees to show sufficient cause why a licence should not be renewed, cancelled or suspended if the licence holder has ceased to be actively, substantially and regularly engaged in the activities authorised by the licence.

Latent effort

3.5.171 As mentioned earlier in this Report, a secondary aim of the buy-out process was to remove latent commercial fishing licences from the industry. With many of the latent commercial fishing licences in Western Port Bay and Port Phillip Bay held by fishers older than 50 years of age, the Council was concerned that these fishers on retiring, may transfer their licence to younger fishers, thereby increasing commercial fishing activity. For example, in Western Port Bay the number of active commercial fishers could have potentially increased from 12 active fishers to 80. If this was to occur, it is unlikely that fish stocks in either of the bays could accommodate this increase in effort without risking fish resource sustainability, particularly considering that recreational fishing effort is also likely to expand. However, **the Council's views were not supported by a detail review of individual latent license holders to determine why they were not utilising their licences, and the likelihood of them either returning to full-time fishing or selling their licence.**

process *and a* cost *that met the needs of the various communities involved. The outcome was an industry restructuring that was done quickly, with no litigation, at low administrative cost, was widely perceived as equitable, and that resulted in a significant risk to our coastal fish stocks (latent effort) being removed.*

***RESPONSE** provided by the Secretary, Department of Natural Resources and Environment - continued*

The fishery is now well placed to implement long term ESD based management arrangements later this year. As remarked by the Chair of the Australian Seafood Industry Council, Mr Nigel Scullion in a national fisheries conference in 2000, the buy out of Bays and Inlet licences in Victoria should be regarded as 'an icon of fisheries management in Australia'. Notwithstanding the ongoing need for probity in everything that is done, retrospective analysis of the processes should not lose sight of the wider triple bottom line outcomes sought in natural resources management.

ALPINE RESORTS LAND STABILITY

3.5.175 Victoria has 6 alpine resorts, which are located on approximately 10 815 hectares of land owned by the State. These resorts provide a wide variety of recreational and leisure activities, attracting in excess of 600 000 visitors a year.

3.5.176 Since 30 April 1998, the resorts have been managed by individual Alpine Resort Management Boards. These boards were established under the *Alpine Resorts (Management) Act* 1997, replacing the former Alpine Resorts Commission. The Act also created the Alpine Resorts Co-ordinating Council with responsibility for:

- making recommendations to the Minister on matters related to the provision and improvement of services and facilities in alpine resorts;
- co-ordinating, in conjunction with Tourism Victoria, the promotion of the alpine resorts;
- and attracting investment for the improvement of the alpine resorts.

3.5.177 Over the past 200 years, since European occupation of Australia, there have been hundreds of reported landslides that have been responsible for the deaths of at least 74 people and the damage or destruction of over 200 buildings. In addition, damage estimated at hundreds of millions of dollars has been caused to infrastructure and privately-owned assets including roads, railway lines, pipelines and crops.

3.5.178 Australia’s worst landslide occurred in 1997 above the New South Wales alpine resort of Thredbo, and resulted in the collapse of 2 large ski lodges and the loss of 18 lives. A coronial inquest investigating the incident found that the landslide was caused by a leaking water main located in the embankment of a road above the lodges. This road was originally constructed for short-term use in connection with the Snowy Mountains Hydro-Electric Scheme and not for the purpose for which it had been used by the resort.

Review of alpine resorts land stability in Victoria

3.5.179 Following the Thredbo landslide, the State Government, through the Department of Natural Resources and Environment, initiated a comprehensive review (the Review) of land stability at all 6 of Victoria’s alpine resorts. Mt Buffalo was not included in the Review as it is classified as a national park and is managed by Parks Victoria.

3.5.180 The Review consisted of 3 stages:

- a preliminary geotechnical risk assessment of roads and car at the alpine resorts;
- mapping (geographical and aerial) of the alpine resorts to provide information on specific site features and to assist in the development of a basis for classifying land stability risk; and
- using the information gathered on each site to assess the stability of developed areas, proposed development areas and access roads within the alpine resorts.

3.5.181 A preliminary assessment of roads and car parks was carried out by the Roads Corporation (VicRoads), on behalf of the former Alpine Resorts Commission, during the period from November 1997 to January 1998. The objectives of that assessment were to:

- identify areas requiring detailed site investigation;
- disclose sites where remedial action may be required; and
- provide preliminary information prior to undertaking a more detailed appraisal of these areas.

3.5.182 The assessment, which concentrated on the higher risk areas, was based on visual inspection only by VicRoads geotechnical engineers. Problem sites were categorised into 3 levels of risk:

- Priority 1 – potential high risk/high impact;
- Priority 2 – potential high risk/low impact or low risk/high impact; and
- Priority 3 – potential low risk/low impact.

3.5.183 The assessment process identified 43 existing Priority 1 sites, the majority of which were located at Falls Creek (21 sites) and Mt Buller (14 sites).

3.5.184 Following receipt of the preliminary assessment undertaken by VicRoads, the Department assigned responsibility for undertaking further investigations and any associated remedial works to the Alpine Resort Management Boards. These works were incorporated into a remedial works program developed by each Board, with urgent works scheduled and completed prior to the commencement of the 1998 ski season.

3.5.185 In late 1998, the Department appointed a firm of engineering consultants to undertake stages 2 and 3 of the Review, with the purpose of identifying and reporting on areas within the resorts that were at risk of landslip. Particular emphasis was placed on:

- the existing land developments and roads located in the resort village areas;
- potential development sites;
- utility and service corridors; and
- ski fields and slopes.

3.5.186 The Review included the production of hazard assessments for approximately 660 developed and potential development sites at the resorts. The landslip hazards were classified into 4 types of instability, namely, natural shallow landslides, rockfall, failure of cut slopes, and failure of fill slopes.

3.5.187 Two of these instability types (natural shallow landslides and rockfall) relate to naturally occurring landslips. The likelihood of these instability types occurring is influenced by natural features including the angle of the slope, the shape of the slope, site geology, the thickness and strength of foundation material, the concentration of surface and ground water, and the incidence of previous instability.

3.5.188 The remaining 2 types of instability (failure of cut slopes and failure of fill slopes) result from development activities that are within the site under construction. Modification that may affect slope instability includes slope modification by cutting, slope modification by filling, removal of low strength material, installation of sub-surface drainage, poor management and disposal of run-off and snowmelt water, and poor disposal of sewerage.

3.5.189 The Review involved:

- mapping alpine land within each resort and determining the sites' stability hazards, based on a review of the respective landforms;
- visually inspecting leased sites at each resort to identify any areas of concern;
- identifying and prioritising remedial works and/or further geotechnical assessment (either monitoring or investigation); and
- preparing guidelines, focusing on planning, monitoring and maintenance, for the control of land instability.

3.5.190 For the purpose of the Review, each site was assessed by experienced geotechnical engineers and assigned a hazard rating for each of the 4 types of instability, based on the presence and type of the site features. The hazard ratings ranged from very high to very low, the implications of which are outlined in Table 3.5P below.

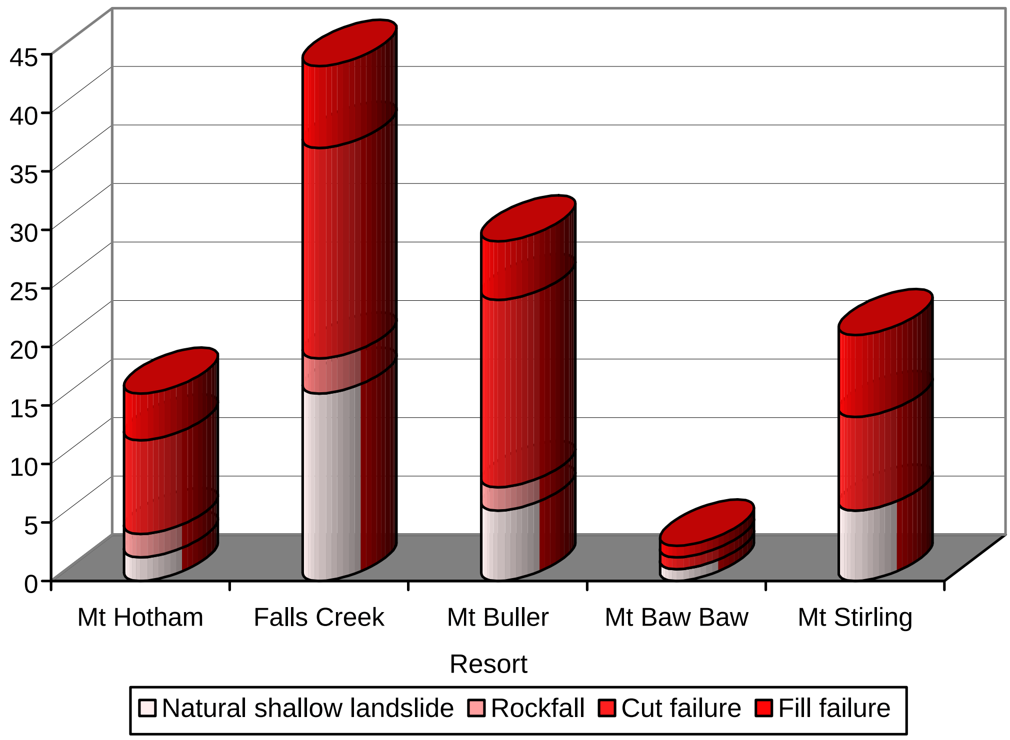
TABLE 3.5P
HAZARD RATINGS AND ASSOCIATED IMPLICATIONS

Hazard rating	*Implications*
Very high	Extensive investigation, planning and implementation of treatment options essential to reduce risk to acceptable levels.
High	Detailed investigation, planning and implementation of treatment options essential to reduce risk to acceptable levels.
Moderate	Acceptable provided a treatment plan, such as active monitoring, is implemented to maintain or reduce risk.
Low	Acceptable, however, treatment to maintain or reduce risks should be defined.
Very low	Acceptable, provided managed by routine procedures.

3.5.191 **Of the 660 sites assessed, 76 were rated as either a high or very high hazard, with many sites at risk of more than one type of instability**. Lake Mountain, which had very little development, was the only resort to have a low to very low hazard rating for all its sites.

3.5.192 Chart 3.5Q below discloses, for each type of instability, the instances of high or very high hazard at each resort.

CHART 3.5Q
INSTANCES OF EACH TYPE OF INSTABILITY AT EACH RESORT, RATED AS A HIGH OR VERY HIGH HAZARD



3.5.193 The main causes of the hazards identified by the Review were:

- the steepness of the slopes;
- concentration of groundwater; and
- considerable excavation into the natural slope surface, which was supported by retaining walls that had deteriorated over time.

3.5.194 **While the Review was in progress, in January 1999, a major warning was issued at Falls Creek in respect of an aqueduct site and the surrounding areas as a result of the consultant's inspection of the site. An immediate detailed site analysis was initiated and remedial works undertaken, which included sealing sections of the aqueduct, replacement of fill, construction of drainage and installation of piezometers to measure water tables. The works were predominantly funded by the lessee of the site.**

3.5.195 **Subsequent monitoring of piezometers at the site revealed dangerously high ground water levels, requiring drains to be bored into the hillside to prevent land saturation and slippage.**

3.5.196 Furthermore, following evidence presented to the Thredbo Coronial Inquest in February 1999, which indicated that a faulty water main was responsible for that land slip, an investigation of the water mains at Falls Creek by the Resort Management Board identified a large quantity of plastic pipe found to be prone to cracking and leaking. As a result, the Board decided to immediately replace all plastic water mains at the resort, at a cost of $177 000.

3.5.197 In September 1999, the Department referred the results of the Review to the individual Resort Management Boards for further investigation and resolution. Based on the Review's recommendations, the Boards appointed specialist geotechnical consultants to undertake detailed studies of high and very high hazard sites identified by the Review.

3.5.198 With the exception of Mt Buller, where many sites (initially rated as having a high or very high hazard) were downgraded to a moderate hazard following these detailed studies, the high to very high hazard ratings at the resorts were generally confirmed. These detailed studies also identified:

- an additional site at Mt Stirling, not assessed as part of the land stability review, with a very high risk of slope fill failure; and
- underlying geotechnical problems, requiring further detailed geotechnical assessment, at up to 25 sites at Mt Hotham that were initially rated as having a moderate hazard.

Remedial works program

3.5.199 Remedial works at the alpine resorts are being undertaken in 3 stages, with the majority of the works occurring during Stages 1 and 2 in 1999-2000 and 2000-2001, respectively. **High and very high hazard sites requiring urgent attention were managed at acceptable levels by the June 2000 snow season following the undertaking of remedial work and it is anticipated that the remaining remedial work will be completed by mid-2002.**

3.5.200 The remedial works are being directed at the following 3 main areas:

- reducing the slope angle;
- increasing the strength of construction material; and
- lowering the water table and improving drainage.

3.5.201 Each Resort Management Board has prioritised the remedial works according to factors such as the risk to human life, buildings and infrastructure, and the impact on service delivery, ski fields, roads, car parks, property values and insurance premiums.

3.5.202 Drainage was identified by the Review as a major issue at all resorts and the Review recommended that a comprehensive drainage scheme be developed as part of each resort's remedial works program. As a result of the Review, significant resources have been devoted to assessing and improving drainage as part of Stage 2 of each resort's remedial works program. Specific problems related to drainage highlighted by the Review, which have been or are in the process of being addressed, include:

- the area around the chairlift base station and access road at Mt Baw Baw, which were of risk of collapse due to the discharge of stormwater drainage directly onto the ground and the deterioration of timber retaining walls;
- an unsealed road constructed at Mt Buller without appropriate drainage, which was channelling stormwater onto sites situated below the road and at risk of failure;
- a site at Mt Buller containing gas tanks and a storage shed, which was unstable as it was situated on a cut into the side of the slope with a dangerously high water table;
- a car park at Mt Buller showing evidence of slope failure, and erosion due to poor drainage and uncontrolled surface run-off;
- poor drainage at Mt Stirling and Lake Mountain, which may have contributed to road failures and concern with the stability of the car park at these resorts, respectively; and
- inconsistent standards of drainage provided for site and roof water run-off at Mt Baw Baw, Mt Buller, Falls Creek and Mt Hotham.

3.5.203 In addition to the above, remedial works have been undertaken at the resorts to address:

- Inadequately supported cuts into the hill slope at 2 sites at Mt Hotham, which required emergency remedial works to be commenced in late 1999. These works included the replacement of a damaged crib retaining wall behind one of the lodges. Detailed geotechnical investigations also recommended the immediate decommissioning and replacement of a water main at the resort; and
- Unstable sections of the resort access road and circuit road embankment at Mt Stirling, which had been reconstructed following a major stability incident in 1998. Detailed investigations revealed that, due to unsatisfactory repairs to the embankment, the likelihood of slope failure was almost certain with over 50 per cent of the road formation at risk of collapse. The factors contributing to the instability included:
    - the use of poor quality materials and workmanship to carry out the reconstruction;
    - the inappropriate use of logs to temporarily support the embankment; and
    - uncontrolled water seepage flowing from the base of the embankment.

PHOTO NOT AVAILABLE

Remedial works being carried out at Higgi Drive, Mt Hotham, behind the Arlberg apartments.
(Photo courtesy of Mt Hotham Alpine Resort Management Board.)

Monitoring of sites

3.5.204 In addition to the identification of remedial works, the Review and subsequent detailed investigations recommended the implementation of a system to monitor all hazardous sites. The aim of the monitoring system was to ensure that the Resort Management Boards receive timely information regarding any changed conditions at these sites and that the Boards have confidence that remedial works undertaken are performing as intended. The Boards are currently developing, as part of their remedial works program, appropriate monitoring strategies for the control of slope instability in accordance with the guidelines prepared as part of the Review.

3.5.205 The guidelines required the:

- installation and measurement of piezometers at locations where site conditions indicate that the groundwater may be near the surface; and
- monitoring of land displacements by regularly reviewing the location and elevation of site markers in areas where landslide movement is suspected.

3.5.206 **The importance of, and need for, ongoing monitoring of not only hazardous but also potentially hazardous sites is illustrated by the collapse, in January 2001, of a significant section of the fill supporting the resort access road at Mt Baw Baw.** This problem had not previously been identified in any geotechnical investigations or reports. The Mt Baw Baw Resort Management Board was subsequently advised by the geotechnical consultants that a realignment of the road and substantial road works and would be required to address the issue. Audit was advised that these remedial works have since been completed.

3.5.207 A comprehensive review of sections of the access road at Mt Baw Baw, not previously assessed, was also scheduled to be undertaken during Stage 2 of the remedial works program in order to identify and investigate other locations that may be prone to instability.

PHOTO NOT AVAILABLE

Repaired pavement - Mt Baw Baw access road.
(Photo courtesy of the Department of Natural Resources and Environment.)

Asset maintenance

3.5.208 Maintenance guidelines for the control of land instability, prepared as part of the Review, require:

- regular cleaning of all drains to remove material that may divert or restrict run-off; and
- surface protection and slope support involving maintenance of grassed surfaces, repair of eroded areas and regular condition monitoring of the retaining walls.

3.5.209 **The Review highlighted a number of deficient maintenance practices at the resorts, particularly in relation to roads, car parks and drainage. Specifically, the Review found:**

- **a road at Mt Buller with a failed stormwater drainage system where the run-off from the road was affecting lodge sites at the north-east side of the resort village;**
- **unstable retaining walls at Mt Buller, Mt Hotham, Mt Baw Baw and Falls Creek;**
- **evidence of soil erosion at most resorts, often resulting from a lack of vegetation and poor vegetation practices; and**
- **a blocked drain that had weakened a sealed car park at Lake Mountain.**

Funding of remedial works

3.5.210 In April 2000, the Government approved the provision of funding of $8.5 million to the alpine resorts over 3 years, concluding in the 2001-2002 financial year, for land stability risk mitigation programs.

3.5.211 Table 3.5R shows the allocation of the funding between the resorts.

TABLE 3.5R
FUNDING PROVIDED TO ALPINE RESORTS FOR REMEDIAL WORKS
($'000)

Resort	*1999-00*	*2000-01*	*2001-02*	*Total*
Mt Buller	650	560	240	1 450
Falls Creek	840	710	375	1 925
Mt Hotham	768	1 460	215	2 443
Mt Baw Baw	630	670	430	1 730
Lake Mountain	140	230	20	390
Mt Stirling	230	225	80	535
Total	**3 258**	**3 855**	**1 360**	**8 473**

3.5.212 Provision of the funding is administered by the Department of Natural and Resources and Environment through annual service agreements with the Resort Management Boards. In May 2000, the Department wrote to all Resort Management Boards and invited them to enter into the first of these service agreements, for works undertaken during the 1999-2000 financial year.

3.5.213 Continuation of remedial works funding is, in accordance with the service agreements, conditional on the Boards submitting information to the Department including annual "post-completion" evaluation reports of the works undertaken and quarterly reports containing the objectives and a description of the proposed works, justification for undertaking the works, and timeframes for commencement and completion.

3.5.214 **However, the Boards have experienced difficulties in complying with the reporting requirements outlined in the service agreements, with many of them submitting late reports. At the beginning of May 2001, the second quarter report, due on 1 February 2001, remained outstanding from all Resort Management Boards except Mt Stirling. Despite this, the Department indicated that it has received informal communication from the Boards as to the progress of the remedial works.**

3.5.215 The Government's decision to provide remedial works funding was subject to the *development of "… a State-wide strategy for alpine resorts (including an examination of the financial position of the Alpine Resort Management Boards to ensure their ongoing viability and long-term ability to undertake the required works and a strategy to mitigate risk in the long-term)"*.

3.5.216 In accordance with that direction, the Department has advised that it is currently undertaking a review of the financial management arrangements of the Boards and an assessment of each Board's ability to continue to manage the alpine resorts geotechnical land stability program on an ongoing basis. It is expected that the review will be finalised in mid-2001.

Cost of works and adequacy of funding

3.5.217 The level of funding provided by the Department for remedial works at the resorts was based on advice from the Boards as to the estimated cost of implementing the planned works on a timely basis.

3.5.218 However, the criticality of the remedial works at many sites required the majority of the Boards to commence their works programs prior to the provision of funding, by utilising internal cash resources. This situation created significant cash flow difficulties for the Boards, requiring the Department, at the beginning of 2000, to provide advances of between $250 000 and $300 000 to each Board with the exception of Mt Stirling and Lake Mountain. Funding subsequently provided under the service agreements was reduced by the amount of the advances provided.

3.5.219 **Stage 1 of the remedial works program was fully funded by the Department at all resorts with the exception of the Mt Hotham, where the total cost of the works exceeded the funding provided by $102 000. These additional costs were met by the Mt Hotham Resort Management Board's internal cash resources.**

Safety of alpine resort access roads

3.5.220 The alpine access roads to the resorts are managed by agreement between the Department, the Alpine Resort Management Boards and VicRoads in accordance with section 12 of the *Alpine Resorts (Management) Act* 1997.

3.5.221 In April 1998, the then Minister for Roads and Ports and the then Minister for Conservation and Land Management agreed that:

- VicRoads would assume responsibility for the maintenance of all resort access roads, although the funding of remedial works on the Mt Stirling access road needed to be resolved; and
- snow clearing on resort access roads would be the responsibility of the Alpine Resort Management Boards, with the exception of snow clearing on the Mt Hotham access road, which would be the responsibility of VicRoads.

3.5.222 However, in the period since that exchange of Ministerial correspondence, the Department and VicRoads have been unable to reach agreement on the funding of road maintenance on the Mt Stirling access road. VicRoads has offered, in discussions with the Department, to maintain the road subject to the Department first upgrading the road to a minimum standard.

3.5.223 **The Mt Stirling Alpine Resort Management Board has advised that without additional funding it will be very difficult for it to keep the access road properly maintained. This was confirmed by a risk assessment undertaken by geotechnical consultants in August 2000, which found that the alpine access road maintenance program at Mt Stirling has been deficient over several years** and recommended that, as the roads at the resort are used as long-term public access roads (despite not being designed or built as such) they need to be managed in a manner that recognises that problems with road safety are likely to arise in the future.

3.5.224 The Board has estimated that an annual road maintenance budget of $100 000 is required to ensure the safety of the resort's roads. This is $90 000 more than the Board's current budget for this purpose and is equal to approximately 50 per cent of the total funding provided by the State Government to support the Board's operations.

PHOTO NOT AVAILABLE

Mt Stirling access road needing repair.

3.5.225 The funding of remedial works on the Mt Baw Baw access road has also created problems for the Mt Baw Baw Resort Management Board. In early 2000, the Board requested that VicRoads undertake remedial works on the resort's access road prior to the up-coming snow season. Audit was advised that these works were not undertaken by VicRoads, as the tight timeframe required by the Board did not provide sufficient time for VicRoads to assess the proposed works and incorporate the works into the Government's annual road program.

3.5.226 As a consequence, the works required were incorporated into the Board's remedial works program and are expected to be completed in conjunction with the Board's other works to ensure that public safety and security of access to the resort is not compromised.

3.5.227 Additional funding has been provided by the Department for the works and the Board has advised the Department that it intends to seek to recover the costs from VicRoads in due course.

Planning policies

3.5.228 The use and development of land at the alpine resorts is regulated by the Alpine Resorts Planning Scheme, which was introduced by the Department of Infrastructure in November 1997 when it took over responsibility for resort development planning from the former Alpine Resorts Commission.

3.5.229 The Scheme encompasses statutory requirements and State and local government planning policies. It also outlines the information required to be submitted with planning applications and the matters to be considered when planning applications are decided. The Scheme currently specifies that planning applications for the development of ski fields and resort village areas are to be accompanied by details of soil, geotechnical and drainage conditions of the site. Applications for planning permits under the Scheme are made to the Department of Infrastructure and referred to the individual Resort Management Boards for comment. In applying the Scheme, the Department of Infrastructure is required to consider the capability of the land to accommodate the proposed use or development.

3.5.230 In August 2000, the Minister for Environment and Conservation wrote to the Resort Management Boards requesting them to provide details of land stability issues to the Department of Infrastructure for land subject to planning applications. At the time the Review of Land Stability was undertaken in 1998, it was the Department of Infrastructure's intention to use the hazard mapping of sites at the alpine resorts and guidelines developed as part of the Review in planning for future developments within resorts.

3.5.231 In particular, consideration was to be given to amending the Scheme to:

- identify risk categories;
- modify the uses and development permissible on land in different risk categories; and
- include conditions that should attach to planning permits, such as the way in which a development is carried out or is subsequently maintained.

3.5.232 **However, the Scheme has not been amended as concerns exist as to how to incorporate the findings of the Review into the Scheme without explicitly exposing the State to liability should any land stability issues arise. In addition, it was felt that by publicly disclosing the hazard ratings of individual sites, it was possible that the value of the developments on the high hazard sites may be negatively impacted.**

Management of safety at alpine resorts

3.5.233 Resorts by their nature are built in areas characterised by steep unstable terrain. These resorts are also major tourist attractions where large numbers of people congregate in relatively small areas. In this environment a landslide, especially where it might impact on infrastructure or buildings, could result in the loss of life and significant damage to property and the environment.

3.5.234 As a consequence, the Resort Management Boards have an obligation to ensure that all resort land under their control is managed to minimise the risk to the public and property. Sound asset management involves:

- recording of sites and documenting site features;
- assessing the level of risk associated with each site;
- ongoing monitoring of site conditions and associated risk;
- adequately maintaining infrastructure such as drains, roads, car parks and utility distribution assets;
- undertaking remedial works to address the problems in risk areas; and
- administering a planning scheme which, when assessing planning applications, takes into consideration the site conditions and risk profile.

3.5.235 **It is pleasing to report that the significant hazards identified by the Review have largely been addressed and the majority of the good infrastructure management processes identified above (with the exception of the amendments to the Planning Scheme) are, or will shortly be, in place.**

3.5.236 **It is quite clear that the Thredbo disaster was the catalyst for the action taken to identify the significant hazards at the Victorian alpine resorts and the subsequent actions taken to mitigate those risks.**

***RESPONSE** provided by Secretary, Department of Natural Resources and Environment*

In general terms, the Department is satisfied that the Report accurately reflects the scope of the Department's Alpine Resorts Land Stability Review and the programs that have been set in place by the Alpine Resort Management Boards to properly manage this important public safety issue. It is pleasing that the Report acknowledges that land stability hazards identified through the Department's Review have been addressed by the Alpine Resort Management Boards who have also established sound infrastructure management processes which have proceeded in a timely fashion with the benefit of government funding for the program.

The Report identifies that there is a need for ongoing management of land stability in the alpine resorts. In particular, the Report notes the importance and need for continuation of monitoring systems on an ongoing basis.

The audit review has been carried out at around the halfway point of a 3 year funding program. Because of the nature of the program, investigations have been carried out (and continue to be carried out) and the scope of anticipated remedial works undertaken by the Boards has subsequently changed; it is possible that the scope of remaining remedial works may be subject to further change. It is, therefore, difficult to be conclusive at this time about the adequacy of funding for the remaining stages of the program.

SCHEDULE A
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS

Report	*Subject*	*Status at date of preparation of this Report*
	MATTERS RESOLVED OR ACTION COMMENCED	
DEPARTMENT OF NATURAL RESOURCES AND ENVIRONMENT		
Second Reports, 1985-86 and 1986-87. Ministerial Portfolios, May 1989, pp. 45-6. May 1990, pp. 68-70.	Deficiencies in the debtors and revenue collection system, including long overdue debtors balances.	The Department's revenue collection systems have been significantly improved in recent years and debtor management is now an important component of line management responsibilities. Details of outstanding debtors balances are included in the monthly business reports submitted to the executive and senior management.
Ministerial Portfolios, May 1997, pp. 158-62.	There is a 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, does not ensure that the Department is aware, on a timely basis, of potential problems arising in committees of management.	A management framework to enhance the accountability of Committees of Management has been developed. The Department has advised that proposed legislative amendments to the *Crown Land (Reserves) Act* 1978 to support the framework will be placed before Parliament in Spring 2001.
Ministerial Portfolios, May 1997, p. 156.	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.	The Government has engaged a consultant to undertake a review of logging royalties and charges and to recommend appropriate methodology(s) to ensure they generate adequate returns. In recognition of the degree of stakeholder and broader community interest in this matter, the review will be undertaken in stages to allow extensive opportunity for comment. The Review is expected to be completed by November 2001.

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

Report	*Subject*	*Status at date of preparation of this Report*
	MATTERS RESOLVED OR ACTION COMMENCED - *continued*	
WATER RESOURCE MANAGEMENT		
Ministerial Portfolios, May 1997, p. 171.	There was a *prima facie* case to suggest that the current levels of unaccounted water relating to the retail water companies was too high and could be economically reduced.	In the period 1997-98 to 1999-2000, the 3 retail water companies have reduced their overall level of unaccounted water by 34 500 ML, this represented a reduction in unaccounted water from 18 per cent to 12 per cent of the total water supplied by these companies. An International Water Association study of 27 international companies across the world indicates that the performance of the Melbourne retail water companies is now close to world best practice.
WATER INDUSTRY REFORM		
Ministerial Portfolios, May 1996, p. 221 and May 1998, p. 175.	While the water reform process envisaged the issue of licence agreements between the Government and water authorities, and the establishment of an independent regulator, these aspects of the reform process have not been implemented.	The licensing of Melbourne Water Corporation and non-metropolitan urban authorities and the establishment of an independent regulator is being addressed through the establishment of an Essential Services Commission as an independent economic regulator.
WATER QUALITY		
Ministerial Portfolios, May 1998, pp.177-9. May 1999, pp.227-33.	In 1996-97, only 57 per cent of the population supplied by non-metropolitan water authorities received water that met the guidelines for micro-biological quality. Of particular concern was that one-third of water that was treated did not meet the guidelines. As at 30 June 1998, 60 per cent of country Victorians were in receipt of water that met the guidelines for micro-biological quality, but with a higher percentage of treated water, now 38 per cent, not meeting the guidelines.	Corporate plans prepared by non-metropolitan water authorities for the 1999-2000 financial year projected an overall 10 per cent improvement in authority compliance with bacteriological requirements of the World Health Organisation Guidelines. However, the actual improvement was 22 per cent. Infrastructure improvement works, designed to achieve full compliance with water quality guidelines, are currently under way and are expected to be completed by 2002.

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

Report	*Subject*	*Status at date of preparation of this Report*
	MATTERS RESOLVED OR ACTION COMMENCED – *continued*	
WASTEWATER MANAGEMENT		
Ministerial Portfolios, May 1998 pp. 179-81 May 1999, pp. 241-44.	In 1996-97, 13 per cent of wastewater treatment plants operated by non-metropolitan water authorities fully met the Environment Protection Authority standards outlined in their licence agreements for the discharge of treated wastewater into waterways. As at 30 June 1998, there was an improvement in compliance to 28 per cent.	The corporate plans prepared by non-metropolitan water authorities indicate that around 33 per cent of wastewater treatment plants fully met the Environment Protection Authority's licensing requirements for the 1999-2000 financial year. During that financial year, a significant number of new treatment plants came into operation, which are expected to further increase the overall compliance rate.
EMERGENCY MANAGEMENT		
Ministerial Portfolios, May 1999, p. 234. *Ministerial Portfolios June 2000, p. 238.*	While Melbourne Water Corporation and the 3 metropolitan retail water companies have in place emergency management plans, in excess of half of the 15 non-metropolitan water authorities had not finalised their plans. Given the significance of this issue, a high priority needs to be given to the finalisation of appropriate emergency management plans for the water sector.	Audit was advised that 4 of the 15 non-metropolitan water authorities are in the process of updating their incident and emergency response plans. All the other non-metropolitan urban authorities, rural water authorities and metropolitan water companies have current plans in place which are regularly reviewed as part of an ongoing improvement process.
	Approximately 60 per cent of authorities needed to prepare or review their dam emergency plans particularly for high hazard dams. In addition, risk assessments identified a need for almost half the authorities to review their dam surveillance practices.	With the exception of one authority, which has recently commenced the process of establishing a dam-specific emergency management plan, all water authorities have either completed or are in the process of completing their plans. In relation to dam surveillance programs, all authorities have either reviewed or are in the process of completing a review of their programs.

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

Report	*Subject*	*Status at date of preparation of this Report*
	MATTERS RESOLVED OR ACTION COMMENCED – *continued*	
VICTORIAN DAIRY INDUSTRY AUTHORITY		
Ministerial Portfolios, May 1998, pp. 183-8.	The Victorian Dairy Industry Authority's share of the estimated accumulated losses in a joint venture in China to 30 June 1998 was 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.	Refer to comments on the wind-up of the Authority in this Part of the Report.
WATER STORAGE MANAGEMENT		
Ministerial Portfolios, June 2000, p. 235.	With the value of dam improvement works identified in risk assessments undertaken by many authorities varying from those works originally anticipated when government funding decisions were made, there have been a mismatch between the actual costs of the works required to be undertaken and the government funding provided to authorities.	Risk assessments conducted by authorities indicated that some $122 million was needed for dam improvement works over a 5-year period, to reduce their risks. Around $35 million has been spent on improvement works since the risk assessments were undertaken. At the end of the 5-year plan (30 June 2003) authorities are required to review their programs and address any residual risks. Audit has been advised that applications for funding from the Government will be considered on a case-by-case basis, having regard to the overall risk posed by the storage facility, the priority assigned for the works to be undertaken and each authority's ability to fund the works.

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

Report	*Subject*	*Status at date of preparation of this Report*
	MATTERS RESOLVED OR ACTION COMMENCED - *continued*	
WATER STORAGE MANAGEMENT - *continued*		
Ministerial Portfolios, June 2000, p. 240.	In respect of private dams where there is a potential risk to local residents, there is a need for more formalised surveillance and monitoring processes to proactively identify and address any potential safety problems.	The Farm Dams Review Committee established by the Government recommended, in its December 2000 draft Report, that special management arrangements and appropriate regulations be enacted to deal with potentially hazardous dams.
Ministerial Portfolios, June 2000, p. 239.	Given the importance of dam safety and the significant consequences of dam failure, consideration should be given to the establishment of a single independent body to oversee dam safety within Victoria.	Current policies, practices and regulatory arrangements associated with dam safety are being reviewed by the Department. This review will, among other things, investigate the feasibility of establishing a single independent body responsible for dam safety. The Department has developed a draft issues paper dealing with the regulatory framework associated with this issue.
CATCHMENT MANAGEMENT AUTHORITIES		
Ministerial Portfolios, June 2000, p. 221.	Some 5 to 10 per cent of catchment management tariffs raised in 1998-99 had not been received by February 2000. In addition, the 4 power generation companies in the Latrobe Valley owed $2.1 million to West Gippsland Catchment Management Authority in respect of catchment management tariffs relating to the 1997-98 and the 1998-99 financial years.	The Government abolished the Catchment Management Authority tariffs in late 1999. Some of the outstanding tariffs have since been collected, while others were not pursued. An arrangement has been entered into with the four power generation companies in the Latrobe Valley regarding the unpaid tariffs.

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

Report	*Subject*	*Status at date of preparation of this Report*
	NO ACTION TAKEN	
MELBOURNE WATER CORPORATION		
Second Report, 1986-87, pp. 164-5. Ministerial Portfolios, May 1990, p. 343. May 1992, p. 432.	The enabling legislation does not confer on the Melbourne Water 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.	As Melbourne Water no longer provides retail water supply or sewerage services the issue of its ability to impose interest on arrears of rates and charges only arises in relation to drainage rates. If drainage rates are not paid they become a lien on the property and can be recouped when the property is sold. In respect of the 3 retail water companies, which have assumed responsibility for water and sewerage services, there is no intention to amend the relevant legislation to provide for the levying of interest on overdue amounts.

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS			
FINANCIAL YEAR ENDED 31 DECEMBER 1999			
Veterinary Practitioners Registration Board of Victoria	2 Aug. 2000	10 Aug. 2000	✓
FINANCIAL YEAR ENDED 30 JUNE 1999			
Casey’s Weir and Major Creek Rural Water Authority	24 Nov. 2000	21 Dec 2000	✓
FINANCIAL YEARS ENDED 30 SEPTEMBER 1995, 30 JUNE 1997, 30 JUNE 1998 AND PERIOD 1 OCTOBER 1995 TO JUNE 30 1996			
Tungamah Shire Water Board	21 Dec. 2000	21 Dec. 2000	Qualified opinion
(Reason for Qualification:	*inadequate accounting records)*		
FINANCIAL YEAR ENDED 30 JUNE 2000			
Department of Natural Resources and Environment	18 Sept. 2000	18 Sept. 2000	✓
AGRICULTURE			
Agriculture Victoria Services Pty Ltd	11 Sept. 2000	19 Sept. 2000	✓
Australian Food Industry Science Centre	27 Oct. 2000	15 Nov. 2000	✓
Emu Industry Development Committee *(a)*	7 April 2001	14 May 2001	✓
Food Quality Service Pty Ltd *(a)*	10 May 2000	10 May 2000	✓
Food Science Australia	27 Oct. 2000	15 Nov. 2000	✓
Melbourne Market Authority	17 Aug. 2000	15 Sept. 2000	✓
Murray Valley Citrus Marketing Board	4 Oct. 2000	13 Nov. 2000	✓
Murray Valley Wine Grape Industry Development Committee	20 Oct. 2000	27 Oct. 2000	Qualified opinion
(Reason for Qualification:	*unable to attest to the completeness of levy revenue)*		
Victorian Dairy Industry Authority *(a)*	20 Aug. 2000	13 Oct. 2000	✓
Victorian Meat Authority	4 Aug. 2000	11 Aug. 2000	✓
Victorian Strawberry Industry Development Committee	27 Sept. 2000	28 Sept. 2000	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS- *continued*			
ENERGY AND RESOURCES			
FINANCIAL YEAR ENDED 30 JUNE 2000 - continued			
Sustainable Energy Authority Victoria *(b)*	20 Sept. 2000	20 Sept. 2000	✓
ENVIRONMENT AND CONSERVATION			
Alpine Resorts Co-ordinating Council	18 Oct. 2000	2 Nov. 2000	✓
Barwon Regional Waste Management Group	21 Sept. 2000	10 Oct. 2000	✓
Barwon Regional Water Authority	27 Sept. 2000	29 Sept. 2000	✓
Calder Regional Waste Management Group	18 Sept. 2000	2 Oct. 2000	✓
Casey's Weir and Major Creek Rural Water Authority	24 Nov. 2000	21 Dec. 2000	✓
Central Gippsland Region Water Authority	4 Sept. 2000	14 Sept. 2000	✓
Central Highlands Region Timber Pty Ltd	17 Aug. 2000	29 Aug. 2000	✓
Central Highlands Region Water Authority	7 Sept. 2000	11 Sept. 2000	✓
Central Murray Regional Waste Management Group	12 Sept. 2000	14 Sept. 2000	✓
City West Water Ltd	31 Aug. 2000	31 Aug. 2000	✓
Coliban Region Water Authority	8 Sept. 2000	11 Sept. 2000	✓
Corangamite Catchment Management Authority	12 Oct. 2000	18 Oct. 2000	✓
Desert Fringe Regional Waste Management Group	16 January 2001	2 Feb. 2001	✓
Eastern Regional Waste Management Group	20 Sept. 2000	13 Oct. 2000	✓
East Gippsland Catchment Management Authority	28 Sept. 2000	9 Oct. 2000	✓
East Gippsland Region Water Authority	21 Sept. 2000	26 Sept. 2000	✓
Eco Recycle Victoria	21 Sept. 2000	21 Sept. 2000	✓
Environment Protection Authority	29 Sept. 2000	12 Oct. 2000	✓
First Mildura Irrigation Trust	22 Aug. 2000	3 Oct. 2000	✓
Gippsland and Southern Rural Water Authority	18 Aug. 2000	4 Sept. 2000	✓
Gippsland Regional Waste Management Group	17 Oct. 2000	18 Oct. 2000	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS *- continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS *- continued*			
ENVIRONMENT AND CONSERVATION *- continued*			
FINANCIAL YEAR ENDED 30 JUNE 2000 *- continued*			
Glenelg Region Water Authority	5 Sept. 2000	13 Sept. 2000	✓
Glenelg-Hopkins Catchment Management Authority	22 Sept. 2000	12 Oct. 2000	✓
Goulburn Broken Catchment Management Authority	19 Sept. 2000	27 Sept. 2000	✓
Goulburn-Murray Rural Water Authority	10 Aug. 2000	15 Aug. 2000	✓
Goulburn Valley Region Water Authority	16 Aug. 2000	24 Aug. 2000	✓
Goulburn Valley Regional Waste Management Group	6 Oct. 2000	19 Oct. 2000	✓
Grampians Region Water Authority	29 Sept. 2000	19 Oct. 2000	✓
Grampians Regional Waste Management Group	19 Oct. 2000	23 Oct. 2000	✓
Highland Regional Waste Management Group	6 Oct. 2000	19 Oct. 2000	✓
Lower Murray Region Water Authority	25 Aug. 2000	3 Oct. 2000	✓
Mallee Catchment Management Authority	8 Sept. 2000	6 Oct. 2000	✓
Melbourne Parks and Waterways	24 Nov. 2000	27 Nov. 2000	✓
Melbourne Water Corporation	18 Aug. 2000	18 Aug. 2000	✓
Mildura Regional Waste Management Group	7 Dec. 2000	11 Dec. 2000	✓
Mornington Peninsula Regional Waste Management Group	12 Oct. 2000	19 Oct. 2000	✓
North Central Catchment Management Authority	25 Sept. 2000	29 Sept. 2000	✓
North East Catchment Management Authority	10 Aug. 2000	25 Sept. 2000	✓
North East Region Water Authority	16 Aug. 2000	7 Sept. 2000	✓
North East Victorian Regional Waste Management Group	29 Aug. 2000	6 Sept. 2000	✓
Northern Regional Waste Management Group	10 Aug. 2000	25 Aug. 2000	✓
Parks Victoria	18 Aug. 2000	29 Aug. 2000	✓
Phillip Island Nature Park Board of Management	3 Oct. 2000	9 Oct. 2000	✓
Portland Coast Region Water Authority	23 Aug. 2000	11 Sept. 2000	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS- *continued*			
ENVIRONMENT AND CONSERVATION - *continued*			
FINANCIAL YEAR ENDED 30 JUNE 2000 - *continued*			
Royal Botanic Gardens Board	8 Sept. 2000	29 Sept. 2000	✓
South East Water Limited	28 Aug. 2000	28 Aug. 2000	✓
South Eastern Regional Waste Management Group	13 Sept. 2000	26 Sept. 2000	✓
South Gippsland Region Water Authority	1 Sept. 2000	7 Sept. 2000	✓
South West Water Authority	19 Sept. 2000	19 Sept. 2000	✓
South Western Regional Waste Management Group	9 Oct. 2000	19 Oct. 2000	✓
Sunraysia Rural Water Authority	11 Sept. 2000	27 Sept. 2000	✓
Surveyors Board of Victoria	23 Oct. 2000	23 Oct. 2000	✓
Trust for Nature (Victoria)	3 Oct. 2000	9 Oct. 2000	✓
Water Training Centre	22 Aug. 2000	28 Aug. 2000	✓
West Gippsland Catchment Management Authority	12 Oct. 2000	17 Oct. 2000	✓
Western Region Water Authority	16 Aug. 2000	6 Sept. 2000	✓
Western Regional Waste Management Group	10 Oct. 2000	23 Oct. 2000	✓
Westernport Region Water Authority	22 Sept. 2000	9 Oct. 2000	✓
Wimmera Catchment Management Authority	23 Aug. 2000	4 Sept. 2000	✓
Wimmera Mallee Rural Water Authority	7 Sept. 2000	7 Sept. 2000	✓
Yarra Bend Park Trust	15 Nov. 2000	16 Nov. 2000	✓
Yarra Valley Water Limited	23 Aug. 2000	23 Aug. 2000	✓
Zoological Parks and Gardens Board	22 Aug. 2000	8 Sept. 2000	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS *- continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS*- continued*			
ENVIRONMENT AND CONSERVATION *- continued*			
FINANCIAL YEAR ENDED 30 OCTOBER 2000			
Falls Creek Alpine Resort Management Board	15 Jan. 2001	15 Jan. 2001	✓
Lake Mountain Alpine Resort Management Board	30 Jan, 2001	2 Feb. 2001	✓
Mount Baw Baw Alpine Resort Management Board	7 Feb. 2001	9 Feb. 2001	✓
Mount Buller Alpine Resort Management Board	19 Feb. 2001	23 Feb. 2001	✓
Mount Hotham Alpine Resort Management Board	19 Jan. 2001	19 Jan. 2001	✓
Mount Stirling Alpine Resort Management Board	18 Jan. 2001	19 Feb. 2001	✓
FINANCIAL YEAR ENDED 31 DECEMBER 2000			
Veterinary Practitioners Registration Board of Victoria	30 April 2001	18 May 2001	✓
INCOMPLETED AUDITS			
FINANCIAL YEAR ENDED 30 JUNE 1999			
Victorian Plantations Corporation			Financial statements not received
FINANCIAL YEAR ENDED 30 JUNE 2000			
Northern Victorian Fresh Tomato Industry Development Committee			Financial statements not received
Shrine of Remembrance Trustees			Audit substantially completed
Victorian Plantation Corporation			Financial statements not received

(a) Final audit.
(b) Formerly known as the Renewable Energy Authority Victoria.

Part 3.6

Premier and Cabinet

KEY FINDING

Summary of audit results

- Similar to all other ministerial portfolios, there is scope for improvement in the timeliness of completion of audited financial statements by some entities in the portfolio.

Paras 3.6.5 to 3.6.9

SUMMARY OF AUDIT RESULTS

3.6.1 The Premier and Cabinet portfolio comprises the Department of Premier and Cabinet, a number of State-owned Arts bodies, an agency responsible for the provision of interpreting and translation services, an agency responsible for the provision of assistance to people by way of financial relief and 2 statutory Offices: the Office of the Ombudsman and the Office of Public Employment.

3.6.2 The Department of Premier and Cabinet has overall responsibility for the provision of support and strategic advice to the Premier, Ministers, Cabinet and the Governor-in-Council in attending to their administrative, parliamentary and governance responsibilities. These responsibilities include the provision of broad leadership across the Victorian public sector, including the co-ordination and implementation of whole-of-government initiatives, projects, activities, and approaches to policy and process issues. The Department's operations include the management of:

- Arts Victoria - responsible for implementing the Government's arts policy, including oversighting the operations of a number of State-owned cultural agencies and the provision of a range of programs which are designed to assist in the development of the arts industry. It also provides policy advice, research and planning services for the arts portfolio;
- Community Support Fund - used to finance research into the effects of gambling on the community and various programs and activities which benefit the community, including programs directed towards the prevention of problem gambling, drug rehabilitation, assistance to families in crisis, and the development of sports, arts and tourism in Victoria. These activities are funded from gaming revenues;
- Office of Women's Policy - aims to continually improve outcomes for all Victorian women, through the conduct of research and the provision of policy advice to government on issues of concern to women, and the monitoring and evaluation of government initiatives that impact on women;
- Victorian Office of Multicultural Affairs - provides advice and support to the Government and its agencies in ensuring that policies and services recognise and respond to the cultural diversity of the Victorian community.

3.6.3 The portfolio includes 6 State-owned cultural agencies whose broad objective is to promote, present and preserve the Arts and the State's heritage assets for the benefit of present and future Victorians, and a number of other small agencies with diverse functions.

3.6.4 The Premier who is also the Minister for Multicultural Affairs, together with the Minister for the Arts and the Minister for Women's Affairs have responsibility for the public sector agencies outlined in Table 3.6A. The Premier and these Ministers also have collective responsibility for the Department of Premier and Cabinet.

TABLE 3.6A
MINISTERIAL RESPONSIBILITY FOR
PUBLIC SECTOR AGENCIES WITHIN THE PREMIER AND CABINET PORTFOLIO

Ministerial portfolio	*Agencies subject to audit*
Premier	Office of the Ombudsman The Office of Public Employment Victorian Relief Committee
Arts	Cinemedia Corporation Council of Trustees of the National Gallery of Victoria Geelong Performing Arts Centre Trust Library Board of Victoria Museums Board of Victoria State Library of Victoria Foundation Victorian Arts Centre Trust
Multicultural Affairs	Victorian Interpreting and Translating Service
Women's Affairs	-

Timeliness of financial reporting

3.6.5 The annual reporting and audit requirements for entities within the portfolio are set out in the *Financial Management Act* 1994 and the *Audit Act* 1994. In particular, under section 45 of the Financial Management Act, each department and public body must submit its annual financial statements to the Auditor-General within 8 weeks of the end of the financial year. Under the Audit Act, the Auditor-General is then required to audit the financial statements within 4 weeks of their receipt. Finally, within 4 months of the end of the financial year or the next sitting day after the end of the fourth month, the relevant Minister is required to table in each House of the Parliament the annual report of each entity, which includes a report of operations and the audited financial statements.

3.6.6 During the 1999-2000 financial audit cycle, clear audit opinions were issued on all financial statements prepared by entities within the portfolio. Schedule B to this Part of the Report outlines the timing of finalisation of the financial statements and the issue of the audit opinions.

3.6.7 As previously mentioned, the legislative framework requires the audited financial statements of public sector entities to be completed within 12 weeks of the end of the financial year, that is by 22 September of each year. Table 3.6B illustrates the performance of portfolio agencies in meeting this statutory requirement during the 1999-2000 reporting cycle.

TABLE 3.6B
TIMELINESS OF FINALISATION OF AUDITED FINANCIAL STATEMENTS, PREMIER AND CABINET PORTFOLIO

	Entities	
Number of weeks after end of financial period	*Number*	*Per cent (cumulative)*
Less than 8 weeks	-	
8 to 10 weeks	3	25
10 to 12 weeks	1	33
12 to 14 weeks	5	75
14-16 weeks	2	92
Over 16 weeks	1	100

3.6.8 The table demonstrates that **there is scope for improvement in the timeliness of completion of audited financial statements by some portfolio entities, with only 33 per cent of entities meeting the 12 week legislated completion timeframe**. Schedule B to this Part of the Report provides details of the performance of individual agencies.

3.6.9 **Timeliness of reporting is an essential characteristic of an effective accountability process. Accordingly, it is important that avenues are identified and pursued to improve the timeliness of the financial reporting process.**

***RESPONSE** provided by the Secretary to the Department of Premier and Cabinet*

I agree that the provision of timely financial statements is a key element in the overall accountability framework, and that, in conjunction with your Office, we should strive to achieve a better result in future.

I will be writing to all agency heads within the portfolio to reinforce the importance of timely reporting. I will also request that those agencies which in 1999-2000 provided their signed reports late should provide a plan outlining how this situation can be corrected in the 2000-01 cycle.

With respect to those financial statements prepared centrally by the Corporate Services Centre, you will be aware that drafts were made available on a timely basis and that finalisation was delayed by one particular audit concern.

It is also important that the agencies have clear and effective communication mechanisms with your Office. There would be mutual benefit in a meeting between the Department's Chief Financial Officer and appropriate members of your staff to ensure that appropriate protocols are agreed prior to the 2000-01 year-end process.

Other major portfolio issues

3.6.10 No other matters of significance were identified in the audit of entities within the Premier and Cabinet portfolio.

SCHEDULE A
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS

Report	*Subject*	*Status at date of preparation of this Report*
	MATTERS RESOLVED OR ACTION COMMENCED	
MUSEUMS BOARD OF VICTORIA		
Ministerial Portfolios, June 2000, pp. 264-9.	At February 2000, the final cost of completing the Melbourne Museum complex was estimated at $291.8 million, compared with an original budget of $250 million.	At March 2001, the estimated cost of project completion was $293.1 million. However, there were a number of contractor claims in dispute or in the process of final determination, which may have an impact on the final cost.
	Due to delays in construction of the new museum, in February 2000 Museum Victoria decided that it would be necessary to undertake a staged opening of the new facility, commencing in late 2000 – almost 12 months later than originally scheduled.	Stage one of the Melbourne Museum was opened to the public in October 2000, while further sections were progressively opened since that date. It is planned that the final elements of the new facility will be open to the public by April 2001.

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS			
FINANCIAL YEAR ENDED 30 JUNE 2000			
Department of Premier and Cabinet	29 Sept. 2000	18 Oct. 2000	✓
ARTS			
Cinemedia Corporation	18 Sept. 2000	2 Oct. 2000	✓
Council of Trustees of the National Gallery of Victoria	31 Aug. 2000	19 Sept. 2000	✓
Geelong Performing Arts Centre Trust	28 Aug. 2000	13 Oct. 2000	✓
Library Board of Victoria	30 Aug. 2000	7 Sept. 2000	✓
Museums Board of Victoria	28 Aug. 2000	30 Aug. 2000	✓
State Library of Victoria Foundation	30 Aug. 2000	7 Sept. 2000	✓
Victorian Arts Centre Trust	2 Oct. 2000	4 Oct. 2000	✓
MULTICULTURAL AFFAIRS			
Victorian Interpreting and Translating Service	2 Nov. 2000	9 Nov. 2000	✓
PREMIER			
Office of the Ombudsman	3 Oct. 2000	4 Oct. 2000	✓
Office of Public Employment	2 Oct. 2000	4 Oct. 2000	✓
Victorian Relief Committee	29 Sept. 2000	5 Oct. 2000	✓

Part 3.7

State and Regional Development

KEY FINDINGS

Progress with Federation Square development

- The assignment of responsibility to Federation Square Management Pty Ltd (FSM) and the appointment of professional project managers, in conjunction with the establishment of a simplified project management structure, has alleviated some of the accountability and control deficiencies that were inherent within the previous management arrangements associated with the construction of Federation Square.

  Paras 3.7.20 to 3.7.29

- The original cost estimate for the development of the Square, set in March 1996, was \$110 million. Recently revised estimates bring total costs to complete the project to around \$369 million. At the date of preparation of this Report, \$202 million has been expended on the project. ***Paras 3.7.30 to 3.7.33***

- The State Government has committed \$224 million, the Commonwealth Government \$50 million and the City of Melbourne \$64 million towards the funding of the Square. When compared with the current estimate of the total cost to complete the project of \$369 million, a funding shortfall of approximately \$31 million remains.

  Paras 3.7.36 to 3.7.40

- The procurement of tenancies in accordance with the commercial retail strategy is a key element to the successful and sustainable operation of the Square. FSM advised that it was continuing in its endeavours to expedite the finalisation of leases for all tenancies. ***Paras 3.7.43 to 3.7.46***

KEY FINDINGS *- continued*

Status of the Melbourne Docklands development

- In early 2001, 7 hectares of the total area available to the Docklands Authority for redevelopment had been fully developed. Construction had commenced on 11.3 hectares and development agreements had been finalised for 55.2 hectares. The Authority is still to finalise arrangements for development of the remaining 34 hectares of the Docklands precinct.

  Paras 3.7.58 to 3.7.64

- The Authority advised that existing and future developers would be required to fund $167 million of trunk infrastructure works by way of a designated contribution. These developer contributions will fall short of recouping the total cost of trunk infrastructure in the Docklands precinct by around $8 million. The Authority advised that this shortfall will be recouped from land sales.

  Paras 3.7.67 to 3.7.71

- In February 2001, Transurban, a private sector consortium for the financing, construction and operation of the Melbourne City Link, lodged a $35.8 million claim against the Government seeking compensation for loss of revenue associated with the construction of Wurundjeri Way, and the widening of the Westgate Freeway. Transurban considers that these developments will have a material adverse effect on traffic volume on the City Link.

  Para. 3.7.81

- The review of the associated agreements entered into by the Docklands Authority for the Business Park precinct has identified that the Authority has implemented appropriate processes to ensure fair and equitable tendering and selection processes for development projects and appropriate protection to the State from any risks that may result from development agreements with the private sector.

  Paras 3.7.91 to 3.7.114

KEY FINDINGS - *continued*

Regional Infrastructure Development Fund

- Over a 3-year period to June 2003, a total of $180.7 million (including $54.4 million for 2000-01) is to be provided from the Regional Infrastructure Development Fund for infrastructure projects that benefit or support the development of regional Victoria.

  Paras 3.7.115 to 3.7.119

- At March 2001, the Department of State and Regional Development had received 166 first and second round applications for funding from the Fund. Eighteen applications were subsequently approved with funding to be provided totalling $37.7 million. In relation to the projects approved, only 3 projects related to non-government entities.

  Paras 3.7.145 to 3.7.149

- At March 2001, only $679 000 (1.8 per cent of approved funding) had been disbursed from the Fund. This is a reflection of the long-term nature of infrastructure development and that progress payments are subject to satisfactory achievement by the recipients of milestones agreed with the Department.

  Paras 3.7.150 to 3.7.152

- The Department has established an adequate administration and accountability framework for grants provided under the Fund. There are processes in place to protect the State against risks associated with grant programs and the accountability requirements reflect the underlying risk and materiality of grants provided.

  Paras 3.7.153 to 3.7.159

- More work needs to be done by the Department in terms of improving its prioritisation of projects, providing timely and complete information to applicants on the outcome of the assessment process, and establishing a performance measurement framework to assess the effectiveness of this initiative.

  Paras 3.7.134 to 3.7.144 and 3.7.160

SUMMARY OF AUDIT RESULTS

3.7.1 The Department of State and Regional Development has responsibility for a range of areas including attracting investment to the State; industry and regional development; industrial relations; multi-media and information technology; science, technology and innovation; small business and regulation reform; major projects; sport and recreation; tourism and racing.

3.7.2 The Department of State and Regional Development was restructured in November 1999 to better align the Department's activities with the new Government's priorities and policy objectives, and to strengthen the rural and regional focus of the Department in particular. Key changes included the following major functions being transferred to the Department:

- Industrial Relations;
- Office of Major Projects; and
- Office of Rural Affairs.

3.7.3 The restructure of the Department impacted on its strategic and operational activities as follows:

- increased emphasis on regional and rural development;
- assuming whole-of-government responsibility for promoting regional economic and community development;
- promotion of manufacturing as the core of the Victorian economy;
- facilitating the growth of Victoria's science, technology and innovation capabilities;
- providing focus to technology-related service improvements for small business and the development of new initiatives;
- implementing the information and communications technology policy, *Connecting Victoria;*
- adopting a new focus on infrastructure planning and promotion of skills, leveraging off the State's investment in major projects and extending infrastructure and major projects investment beyond the Melbourne metropolitan area; and
- supporting "grass roots" sport and recreation.

3.7.4 The Department has wide-ranging responsibilities for co-ordinating whole-of-government policy advice and service delivery to the business community.

3.7.5 The Minister for State and Regional Development, the Minister for Industrial Relations, the Minister for Small Business, the Minister for Manufacturing Industry, the Minister for Major Projects and Tourism, the Minister for Sport and Recreation, and the Minister for Racing have responsibility for operations within the State and Regional Development portfolio. These Ministers have collective responsibility for the Department of State and Regional Development.

3.7.6 Details of the specific ministerial responsibilities for public bodies within the State and Regional Development Portfolio are provided in Table 3.7A. These public bodies, together with the Department of State and Regional Development, were subject to my audit during the 1999-2000 financial year.

TABLE 3.7A
MINISTERIAL RESPONSIBILITIES FOR
PUBLIC BODIES WITHIN THE STATE AND REGIONAL DEVELOPMENT PORTFOLIO

Ministerial portfolio	*Entities subject to audit*
Industrial Relations	-
Manufacturing Industry	-
Major Projects and Tourism	Australian Grand Prix Corporation Docklands Authority Emerald Tourist Railway Board Federation Square Management Pty Ltd Melbourne Convention and Exhibition Trust Tourism Victoria
Racing	Greyhound Racing Control Board Harness Racing Board
Small Business	-
Sport and Recreation	Melbourne and Olympic Parks Trust Melbourne Sports and Aquatic Centre Trust Melbourne 2002 World Masters Games Limited Melbourne 2006 Commonwealth Games Pty Ltd Victorian Institute of Sport Ltd Victorian Institute of Sport Trust
State and Regional Development	Overseas Projects Corporation of Victoria Ltd Victorian Medical Consortium Pty Ltd

3.7.7 The annual reporting and audit requirements for entities within the portfolio are set out in the *Financial Management Act* 1994 and the *Audit Act* 1994. In particular, under section 45 of the Financial Management Act, each department and public body must submit its annual financial statements to the Auditor-General within 8 weeks of the end of the financial year. Under the Audit Act, the Auditor-General is then required to audit the financial statements within 4 weeks of their receipt. Finally, within 4 months of the end of the financial year or the next sitting day after the end of the fourth month, the relevant Minister is required to table in each House of the Parliament the annual report of each entity, which includes a report of operations and the audited financial statements.

Opinions issued

3.7.8 During the 1999-2000 financial audit cycle, 16 clear audit opinions were issued on financial statements prepared by entities within the State and Regional Development portfolio, with one financial statement subject to audit qualification. The qualified audit opinion related to the Melbourne and Olympic Parks Trust inappropriately recognising a liability associated with a future contribution they are required to make towards the construction of a new velodrome. Schedule B to this Part of the Report outlines the audit opinions issued in respect of portfolio entities during the audit cycle.

Timeliness of financial reporting

3.7.9 As previously mentioned, the legislative framework requires the audited financial statements of public sector agencies to be completed within 12 weeks after the end of the relevant financial year. Table 3.7B illustrates the performance of portfolio agencies in meeting this statutory requirement during the 1999-2000 reporting cycle.

TABLE 3.7B
TIMELINESS OF FINALISATION OF AUDITED FINANCIAL STATEMENTS, STATE AND REGIONAL DEVELOPMENT PORTFOLIO

	Entities	
Number of weeks after end of financial period	*Number*	*Per cent (cumulative)*
Less than 8 weeks	2	12
8 to 10 weeks	2	24
10 to 12 weeks	2	35
12 to 14 weeks	4	59
14 to 16 weeks	4	82
Over 16 weeks	3	100

3.7.10 The table demonstrates that **there is scope for improvement in the timeliness of completion of audited financial statement by portfolio entities, with only 35 per cent of entities able to meet the 12 week legislated completion timeframe.** The audited financial statements of the majority of the remaining entities were available within 4 weeks of the legislated completion timeline (that is within 16 weeks of the end of this financial year).

3.7.11 **Timeliness of reporting is an essential characteristic of quality information and the effectiveness of the accountability process. Accordingly, it is important that avenues are identified and pursued to improve the timeliness of the financial reporting process.**

PROGRESS WITH FEDERATION SQUARE DEVELOPMENT

3.7.12 My June 2000 *Report on Ministerial Portfolios* commented on key aspects of the development of the Federation Square project (the Square). The development of the Square commenced in March 1996, as a joint venture initiative of the Government and the City of Melbourne, and involved the development of a 3.8 hectare site that links the Central Business District of Melbourne with the Yarra River and the adjacent riverside park.

3.7.13 The aim of the Federation Square development project is to create a new civic and cultural hub for Melbourne where people can socialise, congregate and stroll through major cultural facilities and commercial outlets that integrate indoor and outdoor public spaces. Development plans outline the potential for the Federation Square to attract 6 million visitors annually and employ approximately 600 people within its mix of hospitality, cultural, leisure and entertainment facilities.

3.7.14 The design of the Square was based on the outcome of an international architectural design competition. In July 1997, *Lab Architecture Studio* of London, in association with *Bates Smart Architects* of Melbourne, were announced as the winners of the competition. Architectural concepts incorporated in the Square's design included the façade of the main building comprising a "pin wheel" triangular grid, in which every part is the same size but the orientation changes. The use of varying proportions of sandstone, zinc and glass cladding materials provides a continually changing view of the building's shell.

PHOTO NOT AVAILABLE

Atrium interior.

3.7.15 Key facilities incorporated into the design of the Square include a Civic Plaza and Atrium promenade, Amphitheatre, an Australian Art Gallery to be operated by the National Gallery of Victoria, an Australian Centre for the Moving Image incorporating Cinemedia and the State Broadcasting Service (SBS), a car park, a mix of food outlets, a boutique wine bar, a new federation-style hotel, a book and music superstore, and a visitor information centre.

3.7.16 In April 1998, 6 tenders for the appointment of a contractor to manage the design and construction and carry out works in relation to the Square were received and were assessed by an evaluation team. Following this process, the Secretary of the Department of Infrastructure approved the appointment of Multiplex Constructions Pty Ltd as managing contractor in May 1998 and building works commenced in July 1998.

3.7.17 Federation Square Management Pty Ltd (FSM) was established in June 1999 with responsibility for managing the Square after its completion. FSM is responsible for the commercial leasing program, preparing for the opening of the Square and developing a program of cultural and civic activities to be held at the Square into the future. Since October 2000, the company has also progressively assumed responsibility from the Office of Major Projects for managing and co-ordinating the construction phase of the project.

Key findings from our previous review

3.7.18 The key finding from our review of the development of the Square, reported in June 2000, was a lack of clarity about the scope and design of the Square from the outset of the project, which led to the project continually exceeding timelines and budgets.

3.7.19 Other findings of the review included the following:

- Prior to the calling of tenders for the construction of Federation Square, the Project Manager’s quantity surveyor estimated the cost of constructing the Square at $249 million based on the winning design, significantly above the initial cost limit;
- The tendering process for construction of the Square was not subject to an independent probity audit and construction of the Square proceeded ahead of the completion of design documentation;
- Under the State’s Agreement with the Managing Contractor, Multiplex Constructions Pty Ltd, the risk of omissions, discrepancies and ambiguities existing in the design and documentation of the works was to be borne by the contractor, but instead has been borne by the State without adjustment to the contractor’s fees;
- Concerns were held by the Steering Committee, established to oversee the development of the Square, on the timeliness of information provided by the project manager. Furthermore, the Steering Committee did not play a formal role in some key decisions relating to the Square due to certain deficiencies in the project management arrangements;

- A number of factors contributed towards the escalating costs of the Square with the cost estimate totalling $262 million as at August 1999. These factors included the introduction of additional design features, substantial expansion of project scope and facilities, suspension of work as a result of industrial disputes, delayed construction works and higher costs for trade package contracts than originally anticipated by the project manager; and
- Title to the Federation Square site had not been structured in accordance with the proposed basis of development. Arrangements had not been put in place that would enable FSM to sub-lease segments of the site to commercial tenants, thus hindering the finalisation of leasing arrangements with these tenants.

Recent changes to project management arrangements

3.7.20 In April 2000, a review of the project management arrangements for the Square, jointly commissioned by the then Secretaries of the Department of Premier and Cabinet, the Department of Treasury and Finance and the Department of State and Regional Development, outlined a number of concerns including:

- poor definition of roles, responsibilities and accountabilities of the various parties involved in the Square;
- insufficient distinction between the client agency and sponsor department;
- wide-ranging responsibilities of the project manager leading to potential conflicts of interest; and
- concerns over the adequacy of lines of accountability and relationships by the project manager with the shareholders (Department of Premier and Cabinet and the City of Melbourne).

3.7.21 In response to the findings of that review, project management arrangements were overhauled in June 2000, which led to the transfer of Ministerial responsibility for the Square from the Premier to the Minister for Major Projects. In November 2000, project management responsibilities were reassigned from the Office of Major Projects (OMP) to Federation Square Management Pty Ltd (FSM), a State owned company.

3.7.22 Although the Department of State and Regional Development had assumed responsibility for overseeing the project from the Department of Infrastructure, these arrangements were not formally transferred until 1 April 2001, when the necessary legislative changes came into effect. The transfer of project management responsibilities to FSM was effected through an instrument of delegation and subsequently formalised in a Deed between the Secretary to the Department of Infrastructure (which at that time was the agency still formally responsible for overseeing the project) and FSM. Pursuant to this Deed, FSM is required to perform specific services aimed at achieving, as far as practicable, the completion of the project facilities and project works on time and within budget.

3.7.23 The Deed also provided for the appointment by FSM of a professional project management company for the remainder of the development phase to assist FSM in its role as project manager of the Square. Following a selective tendering process, Clifton Coney Stevens Pty Ltd was selected, in October 2000, to provide project management services consisting of:

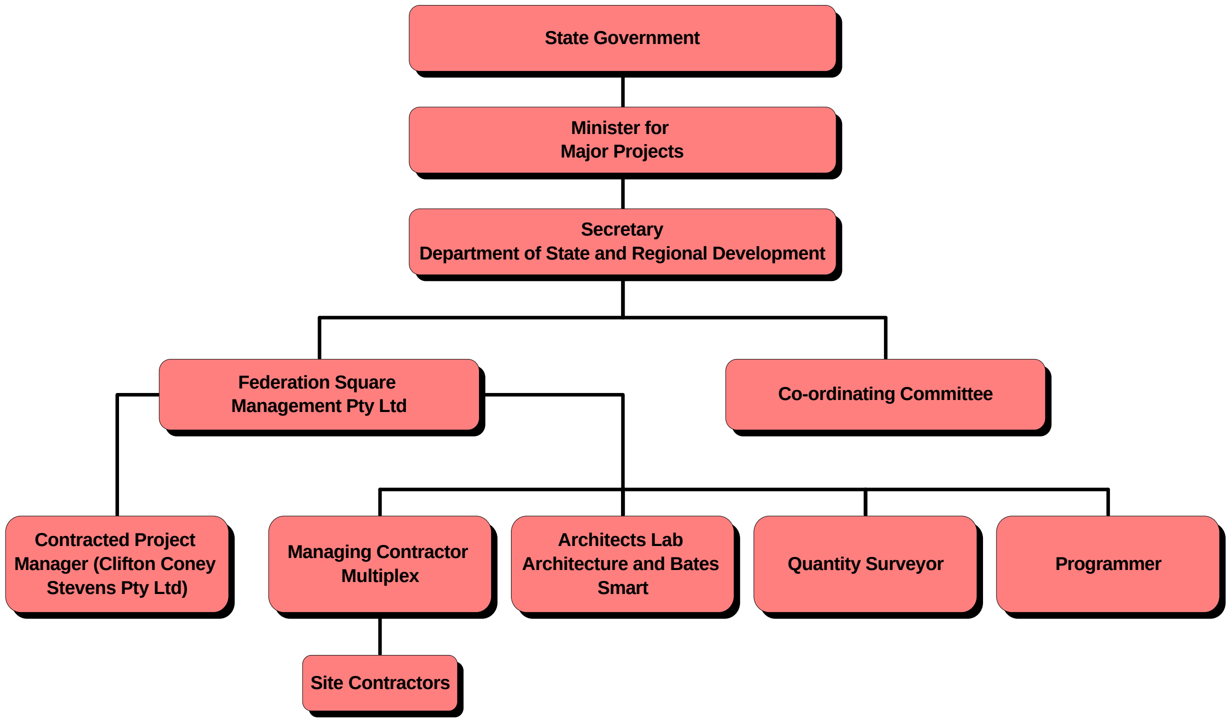
- understanding and incorporating tenant requirements;
- managing the project's design team within previously established project performance parameters;
- overseeing the activities of the managing contractor, Multiplex Constructions Pty Ltd; and
- in conjunction with the project's quantity surveyors, monitoring compliance with the project budget for the remainder of the project.

3.7.24 **Although the project management company has been providing these services since October 2000, contractual arrangements with the company were not finalised until March 2001.**

3.7.25 To streamline the management and accountability responsibilities for the project, a Co-ordinating Committee was also appointed in March 2001 to oversee the management of the project. This Committee includes representatives from the Department of Premier and Cabinet, Department of Treasury and Finance, Department of State and Regional Development, City of Melbourne and the Federation Square Management Pty Ltd. The Committee met for the first time during March 2001.

3.7.26 Chart 3.7C depicts the new management structure for the project following the changes outlined above.

CHART 3.7C
PROJECT MANAGEMENT STRUCTURE



Source: Federation Square Management Pty Ltd.

3.7.27 **The assignment of responsibility to FSM and the appointment of professional project managers, in conjunction with the establishment of a simplified project management structure, has alleviated some of the accountability and control deficiencies that were inherent within the previous management arrangements.**

3.7.28 However, a number of limitations still exist in the current project management arrangements. For example:

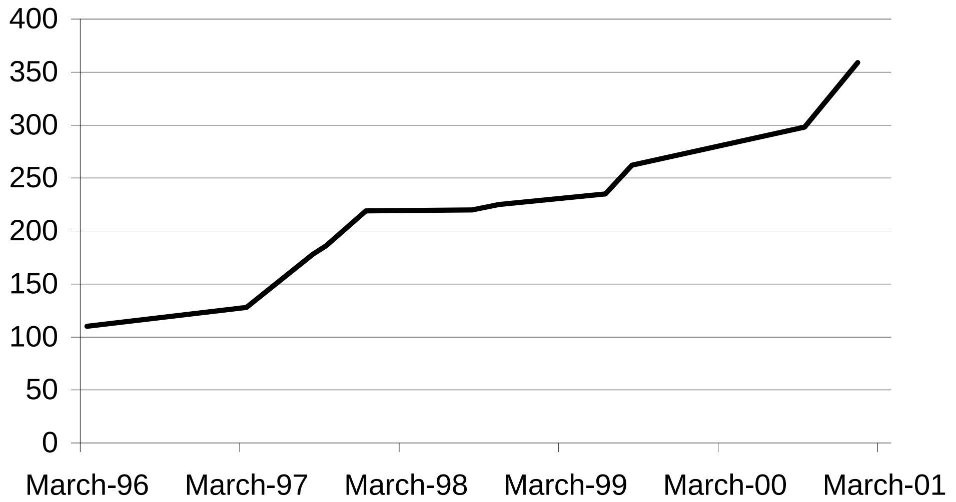
- At the date of preparation of this Report, the roles and responsibilities of the Co-ordinating Committee and its relationship with FSM had not been finalised; and
- Under the revised arrangements, FSM has responsibility for all major facets of the project including certain functions on behalf of the client agency (Department of State and Regional Development), for which the Square is being developed, the role of project manager for the development, and responsibility as facilities manager for the operations of the Square post-completion. This convergence of responsibilities may lead to competing interests and compromises in fulfilling these various roles. For instance, FSM as project manager has decided to reduce costs by reducing the quality of materials used in certain components of the development. This decision may not be consistent with the aims of FSM in its role to maintain the quality of the development as client and facilities manager.

3.7.29 **While further changes in project management arrangements are likely to be disruptive at this stage of the project, there is a need for the Department of State and Regional Development to be mindful of FSM's range of interests and ensure the oversight of FSM's various responsibilities are exercised in a thorough manner. In order to strengthen the reporting and accountability arrangements for the Square, the roles and responsibilities of the Co-ordinating Committee and its relationship with FSM should be clearly established as a matter of priority.**

Project costs

3.7.30 The original cost estimate for the development of the Square, set in March 1996, was $110 million. This estimate was based on a broadly defined project scope when only limited design work had been carried out. As depicted in Chart 3.7D, the estimated cost of the development of the Square has continued to escalate. At the time of my previous review on the project in June 2000, the estimated cost for completing the development of the Square was $262 million**. In September 2000, total funding approved for the completion of the project was increased to $338 million. However, recently revised estimates bring total costs to complete the project at around $369 million. At the date of preparation of this Report, $202 million has been expended on the project.**

CHART 3.7D
FEDERATION SQUARE
ESTIMATED COST OF DEVELOPMENT
($million)



3.7.31 The key reasons for the cost escalations from the initial March 1996 estimate of $110 million to the August 1999 estimate of $262 million were referred to earlier in this section of the Report. Certain of those factors, such as delays in construction as a result of contract variations and delays in finalising design documents, continue to adversely affect the cost of the project.

3.7.32 The subsequent increase from the August 1999 estimate of $262 million to the current estimate of $369 million is mainly attributable to:

- inadequate budgeting for the Square, including the omission of components, valued at $21 million, from previous estimates and the exclusion of the cost of 2 buildings, estimated to cost $14 million, which were intended to be privately financed;
- additional costs of $62.7 million including variation claims approved to date of $11.2 million as a result of changes in scope and delays in completing the project due to the restricted availability of building contractors, the complexity of the Square design, the quality of design documentation and the impact of industrial disputes;
- additional fit-out, furniture and fixture costs of $7.5 million; and
- appointment of external project managers estimated to cost $1.8 million.

3.7.33 A contingency amount has been provided within the existing budget for possible future risks associated with the Square, including cost variations, trade contract disputes, contributions to tenant fit-out costs and unresolved car park issues. This provision may be largely consumed by currently unresolved variation claims of $11.6 million and may therefore be insufficient to fund any cost escalation arising from any additional risks that may arise in the future. Given these factors, the current cost estimate for completion of the Square of $369 million may be exceeded.

3.7.34 Due to concerns regarding the potential for project cost escalations, FSM has introduced measures to contain project costs within the current cost estimates. These measures include improvements to project management and monitoring, and savings of approximately $6.9 million from modifications to certain “non-critical” design aspects of the Square.

3.7.35 **While attempts to constrain project costs are welcomed, FSM should ensure that any modifications to the Square do not compromise the durability, ambience and design aesthetics that the original design proposals envisaged.**

PHOTO NOT AVAILABLE

Federation Square development.

Project funding

3.7.36 Under the terms of a March 1996 Agreement, the State Government and the City of Melbourne were each to contribute $50 million towards the development of the Square. Required contributions from each of the parties were subsequently increased to $64 million in June 1997.

3.7.37 **Since the date of this arrangement, the State Government has committed $224 million, the Commonwealth Government $50 million, and the City of Melbourne $64 million towards the current approved funding of the Square of $338 million. When compared with the current estimate of the total cost to complete the project of $369 million, a funding shortfall of approximately $31 million remains.**

3.7.38 Given that the State Government has indicated its reluctance to provide further funding, FSM has advised that the shortfall of $31 million is expected to be funded through a mix of sponsorships, loans and joint venture relationships that are currently being negotiated. If funds cannot be obtained from these sources, FSM plans to defer completion of certain elements of the Square.

3.7.39 The identified unfunded elements of the project currently include:

- some aspects of the multimedia across the site which will be installed progressively after the opening of the Square;
- the Amphitheatre not being fitted-out with the large video screens originally proposed for free public entertainment;

- certain aspects of the redevelopment of the old Batman Avenue and the adjacent river edge area beyond the site's boundary; and
- changes to the design and capacity of the car park.

3.7.40 Negotiations are also currently underway with certain tenants of the Square including the National Gallery of Victoria, SBS and Cinemedia with regard to responsibility for funding the base building and fit-out works for these tenancies. The outcome of these negotiations will have an impact on the funding and final cost of the Square.

Project monitoring and reporting

3.7.41 Concerns over project monitoring arrangements under the previous project management framework included the lack of adequate information and resources to facilitate comprehensive monitoring and management of the Square. However, since FSM assumed responsibility for managing and co-ordinating the construction phase of the project during October 2000, improved monitoring arrangements have been introduced including:

- establishment of a number of committees to monitor and report on various aspects of the project;
- monthly reporting by FSM to the Department of State and Regional Development on the financial performance of the project;
- increased oversight and review of contractor claims;
- improved cost monitoring and reporting to enable management decision making and ministerial oversight;
- efforts to improve the speed and co-ordination of design documentation;
- attempts to identify and recognise the cost of all elements of the Square in updated cost estimates; and
- improved control over the building contractor and architects.

3.7.42 A number of project risks have been identified and are reviewed by FSM on a regular basis as part of the overall project monitoring process. **However, to enable the structured management and control of identified project risks, an integrated risk management framework should have been developed from the outset of the project detailing identified risks, the impact of such risks on the delivery and costs of the Square, and proposed strategies to mitigate against risk exposures.**

Commercial tenancy arrangements

3.7.43 A retail strategy was adopted during 1998 that defined the commercial theme, retail mix and projected financial outcomes of the commercial operations of the Square. The strategy identified 11 separate commercial opportunities, including the federation-style hotel, a book and music superstore, multi-media retail outlet, a function centre and 5 restaurants and cafes. Since the preparation of the retail strategy, an additional 6 potential opportunities have been identified. An expression of interest process commenced in December 1998 to secure tenants and operators for the commercial activities of the Square. A major aspect of negotiations to secure commercial tenancies has been the cost of leases and the level of contribution by the State for tenancy fit-outs.

3.7.44 In addition, as reported in my June 2000 Report, title to the Square site had not been structured in accordance with the proposed basis of development, and arrangements had not been put in place that would enable FSM to sub-lease the respective segments of the site to commercial tenants. This issue remains outstanding but is expected to be resolved by June 2001 when title is expected to pass to FSM from the Victorian Rail Track Corporation, which currently owns the land on which the Square is being constructed.

3.7.45 At the time of preparation of this Report, 3 tenancy leases had been finalised and negotiations and arrangements were proceeding satisfactorily in respect of the remaining tenancies.

3.7.46 **The procurement of tenancies in accordance with the commercial retail strategy is a key element to the successful and sustainable operation of the Square. FSM advised that it was continuing in its endeavours to formalise title arrangements and negotiate issues relating to the level of tenancy contributions to finance fit-outs and associated outgoings to expedite the finalisation of leases for all tenancies.**

Status of the project

3.7.47 **At the time of my review in June 2000, the expected completion date for the Square was May 2001. FSM has advised that completion of the development of the Square is now scheduled for March 2002.**

3.7.48 Through mutual agreement with the Centenary of Federation organisers, FSM propose to partially open Federation Square as the key event with which to conclude the Centenary of Federation celebrations. **A Federation Ceremony is scheduled for November 2001 at which time the Australian Centre for the Moving Image, incorporating SBS and Cinemedia, is expected to be completed.**

3.7.49 Table 3.7E below sets out the initial timelines set for completion of key stages of the project, compared with current completion targets. The achievement of these dates will, however, be impacted upon by the nature and extent of any further project variations.

TABLE 3.7E
COMPLETION TIMELINES

Project milestone	*Initial target (March 1998)*	*Revised target (July 1999)*	*Current target (May 2001)*
Design finalisation	January 2000	January 2000	December 2001
Construction completion	December 2000	March 2001	March 2002
Tenancy fit-out works	August 2000	May 2001	March 2002
Leasing of commercial assets	November 1998	January 2001	November 2001
Opening of the Square	January 2001	May 2001	March 2002

Ongoing management of the Square

3.7.50 FSM has principal responsibility for managing the Square post-completion which will encompass the management of all tenancy leases, the development and scheduling of public events and performance programs, marketing and promotion activities, and ongoing maintenance of the Square.

3.7.51 Funding for the operations of the Square post-completion is expected to be obtained from a number of revenue bases including tenancy lease rentals, car park operations, ticketing revenue from public programs and events, and hiring of public spaces.

3.7.52 Financial projections regarding the operation of the Square post-completion are outlined in FSM's 2000-2001 business plan. **While these financial projections are currently being updated to incorporate information based on the current status of the Square, the validity of the projections needs to be reviewed in light of a number of outstanding issues that will impact on the levels of revenue and the future operations of the Square including:**

- Involvement of the City of Melbourne in the operations of the Square. The City of Melbourne as partner in the joint venture agreement with the State to develop the Square has an option to take up a share in FSM. This option had not been exercised by the Council at the time of preparation of this Report;
- The establishment of a refurbishment reserve requiring contributions from major tenants to enable periodic works on the Square to be undertaken. The long-term management of the accumulated funds within this reserve requires further consideration by the State Government; and
- The impact of the unfunded development components of the Square on its future operations.

3.7.53 **It is crucial that the above issues be addressed as a matter of priority given their potential impact on both the short and long-term financial and administrative operations of the Square.**

RESPONSE *provided by Secretary, Department of State and Regional Development*

Project management

The engagement of Clifton Coney Stevens Pty Ltd (CCS) to provide project management services was made immediately following the State Government's decision in October 2000 for FSM to assume management of the project. Fundamental contractual terms, including the services to be provided and the remuneration payable etc. were documented in either the tender brief, the proposal submitted by CCS or subsequently negotiated with CCS following its selection as preferred tenderer.

It was impractical to delay the appointment of a Project Manager on a project of the size and complexity of Federation Square, or to resolve fully the more detailed contractual arrangements in advance of CCS commencing work.

The role of the Co-ordinating Committee is not one of direct control over the project but rather a mechanism to facilitate the dissemination of relevant information to the key stakeholders. The Co-ordinating Committee does not make decisions on the project. Discussions will take place with the City of Melbourne regarding the involvement of the City in the project, and the role of the Co-ordinating Committee in providing a formal conduit for information and discussion.

Overall, the revised project management and departmental oversighting structures are working both effectively and efficiently with adequate controls, decision-making processes and reporting practices in place to ensure appropriate levels of performance and accountability.

While Federation Square Management handles a number of aspects of the project and the ongoing management of the Square, it is the body most appropriately placed to control costs and make decisions that may impact on the ultimate outcomes at Federation Square.

As the organisation responsible for the future management of Federation Square, FSM has the motivation necessary to take decisions with a long-term horizon, and to ensure that the long-term requirements are fully taken into account in project delivery decisions in the shorter-term.

Clearly, budgetary control over a project such as this may involve options being selected that are less costly than alternatives. The objective of all concerned will be to ensure that the long-term quality of the project is maintained to the extent possible within the funds available for the project. In particular, FSM will use its best endeavours to ensure that modifications imposed by cost constraints do not compromise the durability, ambience and design aesthetics of the original design proposals.

Project costs

The estimated project cost depicted in Chart 3.7D has the potential to mislead users of the Report, given the failure to represent the increasing scope of works.

Many of the costs identified recently by FSM are for integral components of the project that form part of the original design, but were not reflected in the original total estimated cost.

The currently projected total project cost is \$369 million, with all-of-government support totalling \$338 million. The difference is to be found by FSM from loans, revenue opportunities and construction savings.

RESPONSE *provided by Secretary, Department of State and Regional Development - continued*

Project monitoring and reporting

The risks inherent in the project are monitored regularly by FSM and are included as part of the formal reporting procedures. However, as the bulk of the projected end cost has been committed already through existing contractual arrangements it would be inappropriate to divert resources to developing an integrated risk management framework for the project at this late stage.

The acknowledgment by audit of improved monitoring arrangements introduced since FSM assumed responsibility is supported by the Department.

STATUS OF THE MELBOURNE DOCKLANDS DEVELOPMENT

3.7.54 Melbourne Docklands covers approximately 200 hectares of land and water and is located to the west of the Melbourne central business district on the waterways of Victoria Harbour and the Yarra River.

3.7.55 Redevelopment of the Docklands has been an ongoing initiative of successive State Governments. The redevelopment project is one of the largest urban renewal projects in Australia. The project is expected to span many years and have a potential development value in excess of $6 billion. By the year 2020, a developed Docklands is expected to have the potential to attract 20 million visitors annually, employ 15 000 Victorians and house 20 000 residents.

3.7.56 The Docklands Authority was established in 1991 to manage the redevelopment of the Docklands on behalf of the Government. The redevelopment is being undertaken by the private sector under contract to the Authority.

3.7.57 In late November 1998, the *Local Government (Governance and Melton) Act* 1998 was passed amending the *Docklands Authority Act* 1991 to provide the Authority with certain powers of a municipal council in respect of the Docklands area. However, the current Government has indicated an intention to return the municipal powers to relevant local government authorities at a time yet to be established.

Status of the project

3.7.58 In August 1995, following 3 years of planning and research, the Government endorsed the Authority's strategy which identified 7 precincts within the Docklands area for redevelopment. These were known as Business Park, Victoria Harbour, Yarra Waters, Batman's Hill, Technology Park, Stadium and West End. Precincts within the Docklands area have since been redefined and are currently referred to as North-West, MAB New Quay, Digital Harbour at Comtechport, Stadium, Batman's Hill, Lend Lease Victoria Harbour and Mirvac Yarra's Edge precincts. The following photograph shows the location of these current development precincts.

PHOTO NOT AVAILABLE

Docklands precincts, 2001.
Source: Docklands Authority.

3.7.59 Over recent years, the Authority has marketed development opportunities and entered into development agreements with private sector developers for the redevelopment of various precincts of the Docklands. Previous Reports to Parliament by my Office have commented on the status of the redevelopment, including arrangements with developers for the Yarra Waters and Stadium precincts.

3.7.60 The Authority has made significant progress in finalising agreements with private sector developers since my last Report. In particular:

- A development agreement for 13.8 hectares in the Business Park precinct was finalised with MAB Docklands (a private consortium) in April 1999. The agreement provides for a 14 year development comprising 1 800 residential dwellings, 20 000 square metres of commercial office space, retail space and marina berths. MAB Docklands commenced development of their first residential tower in June 2000;
- Development rights on a 4.4 hectare site in the Commonwealth Technology Port precinct were awarded to Digital Harbour Holdings in December 2000 subject to certain conditions. The development is aimed at creating a commercially viable environment to attract major corporations, research and educational institutions, small to medium enterprises and technology start-up businesses; and
- In April 2001, the Premier announced the appointment of Lend Lease Corporation Pty Ltd for a $1.8 billion development of the Victoria Harbour precinct. The development is to be completed over a period of 15 to 17 years, will cover 27.7 hectares and is to include residential, commercial, retail and community facilities.

3.7.61 Table 3.7F sets out the status of agreed or proposed developments within each of the development precincts.

TABLE 3.7F
STATUS OF DEVELOPMENT IN DOCKLANDS

Precinct	*Status of Development*
Stadium (covering 13.2 hectares)	The Stadium precinct comprises 4 developments, namely: • A *multi-purpose sport and entertainment stadium* (Colonial Stadium) constructed by Docklands Stadium Consortium, which opened in March 2000. • The *Seven Network's new Melbourne Headquarters and Digital Broadcast Centre* on the north-western corner of the Stadium, which will be completed in May 2001, occupied shortly after that date and commence broadcasting by January 2002. • Proposed development of *residential, sports, entertainment, leisure, restaurant and retailing facilities* around the Stadium precinct fronting the new Bourke Street Bridge. Docklands Stadium Consortium has been selected as the preferred developer and contractual arrangements are currently being finalised. • Development of the *North-East Stadium site* for mixed use such as commercial, recreation and leisure, cafes and restaurants. The Authority has awarded a 12 month exclusive right to the Pan Urban/Abigroup Consortium to allow for the securing of a tenant and to ensure the certainty of financing. It is intended that this development will become unconditional by January 2002.
Mirvac Yarra's Edge (formerly known as Yarra Waters and covering 14.5 hectares)	A development agreement was executed in December 1997 with the Mirvac Group for a 12 year development of approximately 2 000 *apartments and townhouses, restaurants, marina and commercial and retail areas*. Development commenced in early 2000, the first stage consisting of 175 apartments, a $10 million recreation facility and a 700 metre waterfront promenade. In April 2001, construction of a second building commenced consisting of 2 towers on a single podium with a total of 280 apartments.
MAB New Quay (formerly part of the precinct known as Business Park and covering 13.8 hectares)	A development agreement for this precinct was finalised with MAB Docklands for a 14 year development comprising 1 800 residential dwellings, commercial office space, retail space and marina berths. MAB Docklands commenced work in June 2000.
North-West (formerly part of the precinct known as Business Park and covering 22.4 hectares)	The Authority is currently considering replacement developments following the termination in June 2000 of a conditional agreement with Studio City Melbourne Pty Ltd for a $500 million development of this precinct comprising a theme park, working film studio, cinema Megaplex and retail outlets.
Lend Lease Victoria Harbour (covering 27.7 hectares)	An agreement was finalised in April 2001 with Lend Lease for a $1.8 billion development of the 27.7 hectare site. The development is to occur over 15 to 17 years and will include 2 100 residential apartments, 160 000 square metres of commercial office space, 20 000 square metres of retail, restaurant and café facilities and 15 000 square metres of community facilities.
Batman's Hill (covering 11.5 hectares)	Following termination of negotiations with Grollo Tower in April 1999, bids for the development of the precinct were sought for a mix of uses including commercial, retail, entertainment, hotel, and residential and cultural developments. At the date of preparation of this Report, the Authority was still completing its tendering process.

TABLE 3.7F
STATUS OF DEVELOPMENT IN DOCKLANDS *- continued*

Precinct	*Status of Development*
Digital Harbour at Comtechport (formerly known as Commonwealth Technology Port covering 4.4 hectares)	The Authority sought expressions of interest in May 1999 for the development of this 4.4 hectare precinct. In December 2000, development rights were awarded to Digital Harbour Holdings Pty Ltd. The precinct is to incorporate a commercially viable environment to attract major corporations, research and educational institutions, small to medium enterprises and technology start-up businesses. Development is to be partly funded by a Commonwealth Government grant of $22.5 million from the Federation Fund. In May 2000, a Federation Fund Grant Deed was finalised which provides for the funds to be applied to Stage 1 of the` project.
West End (covering 20.9 hectares)	From 1 July 2000, the Spencer Street Station Authority became responsible for the Spencer Street Station area, in addition to the land and air rights forming part of the West End precinct. The Authority advised that it expects to be compensated for the transfer of the developable area and that it will be consulted by the Spencer Street Station Authority to ensure that any upgrade of the area preserves the vision that it held for the West End precinct of the Docklands.

3.7.62 **At the date of preparation of this Report, 7 hectares (6.5 per cent) of the total area available to the Authority for redevelopment of 107.5 hectares had been fully developed. Construction had commenced on 11.3 hectares (10.5 per cent) and development agreements had been finalised for 55.2 hectares (51.3 per cent). The Authority is still to finalise arrangements for development of the remaining 34 hectares (31.7 per cent) of the Docklands precinct.**

3.7.63 This Report focuses on infrastructure works undertaken by the Authority, municipal activities assumed by the Authority, redevelopment of the Spencer Street Station and a development agreement entered into with a private sector consortium, MAB Docklands.

3.7.64 We intend to report on the recent arrangement entered into by the Authority with Lend Lease Corporation Pty Ltd for the $1.8 billion development of the Victoria Harbour precinct at a later date.

Infrastructure supporting the Docklands

3.7.65 The Authority is overseeing the construction of basic trunk infrastructure covering the Docklands precinct including roads, bridges, water and power supply which is required to attract private sector investment. Major contracts facilitated by the Authority for infrastructure development are:

- Appointment of the Transfield Powercor Consortium, in March 1998, for infrastructure projects including major roads and traffic works, major pedestrian and bicycle links, tram works, utilities, stormwater drainage and specific works such as development of public open space and waterfront precincts. The contracted sum payable to the Consortium was $64 million with an additional allowance of up to $51 million for optional works, as specified in the contract, which the Authority has subsequently let to the consortium; and

- Appointment of Walter Constructions in May 1999 for the realignment of Charles Grimes Bridge, reconstruction of Dudley Street, Flinders Street and North Wharf Road, and the extension of the tram service from Spencer Street to the extension of Bourke Street for a contract sum of $36 million.

3.7.66 Following completion, ownership of infrastructure assets is either retained by the Authority, in line with its responsibility for certain development and municipal activities, or, depending on the nature of the assets concerned, transferred to VicRoads, VicTrack, other relevant government agencies or the private sector.

Funding of trunk infrastructure

3.7.67 **As at 31 December 2000, total expenditure of $177 million had been incurred on infrastructure works** including payments of $115 million to the Transfield Powercor Consortium, $38 million to Walter Constructions and the balance to a number of other contractors. This expenditure includes an amount of $46 million relating to the construction of Wurundjeri Way which is not directly related to the Docklands precincts and has been funded by State Government contributions. Sources of funding for the balance of the works are outlined in Table 3.7G.

TABLE 3.7G
SOURCES OF FUNDING FOR INFRASTRUCTURE WORKS, AS AT 31 DECEMBER 2000
($million)

Source	*Amount*
Multi-loan facility from the Treasury Corporation of Victoria	72.6
Stadium Funding Facility	29.1
Contributions from developers -	
Mirvac Yarra's Edge	10.9
MAB Docklands	7.8
Seven Network	6.7
Digital Harbour	0.5
Commonwealth Government grant for Comtechport	3.0
Contributions from other Stakeholders	2.4
Total *(a)*	**133.0**

(a) In addition, the Government has agreed to provide $46 million ($45 million received to date) for construction of Wurundjeri Way, a replacement State Highway, which benefits non-Docklands related traffic and $1 million for the extra costs associated with bringing forward the timing of associated tram extension works before 30 June 2001. The Authority has acted as project manager for this infrastructure project.

3.7.68 Specific comments on the major sources of funding as outlined in the above table are provided in the following paragraphs.

Recoupment from developers

3.7.69 The Authority initially estimated in November 1996, that total trunk infrastructure costs to the Authority would be $158 million, inclusive of a 20 per cent contingency, with the developers constructing the remainder of the required infrastructure. At 30 June 2000, estimated total trunk infrastructure costs to be incurred by the Authority had increased to $175 million as a result of required increased scope of works. This estimate does not include:

- $46 million related to the construction of Wurundjeri Way;
- $38 million for the Collins Street Bridge which is to be funded from the sale of land in the Victoria Harbour and Batman's Hill precincts;
- $51.9 million for remediation works, on the West Melbourne Gasworks site (Victoria Harbour precinct); and
- the cost of the redevelopment of the Spencer Street Station to be undertaken by the Spencer Street Station Authority specifically established for this purpose.

3.7.70 The Authority advised that, existing and future developers would be required to fund $167 million of trunk infrastructure works by way of a designated contribution. **This contribution will fall short of recouping the total cost of trunk infrastructure in the Docklands precinct by around $8 million. The Authority advised that this shortfall will be recouped from the proceeds of land sales to developers**. As at the date of the preparation of this Report, $25.9 million of trunk infrastructure contributions had been received from developers.

3.7.71 **Due to the nature and scale of the development project, it is acknowledged that trunk infrastructure works and expenditure projections will be revised to suit changing conditions. The Authority should, however, continue to ensure that any escalation in infrastructure costs is recoverable from the proceeds of future agreements with private developers.**

Treasury Corporation of Victoria loan facility and contributions from developers

3.7.72 The government policy for the Docklands development is for all trunk infrastructure to be ultimately funded by developers in the form of a designated trunk infrastructure contribution included as part of the overall settlement proceeds for the awarding of development rights.

3.7.73 The Authority operates under a rolling debt facility with the Treasury Corporation of Victoria which was increased to $125 million in September 2000 to finance ongoing infrastructure works and other operations of the Authority. Progressive contributions by developers, made in accordance with development agreements, are utilised to repay this facility.

3.7.74 At 31 December 2000, the Authority had drawn-down $101 million under this debt facility of which $72.6 million had been applied to the funding of infrastructure works and $28.4 million used to meet interest costs, the costs of site presentation and the ongoing operating costs of the Authority.

3.7.75 The Authority is required to repay all borrowings under the facility by no later than 30 June 2009 from proceeds of land sales, developer contributions for infrastructure and lease income. The ability of the Authority to meet this repayment timeframe will be contingent on its financial performance, the rate of development under existing agreements which is determined by market conditions, and on its success in finalising arrangements with private developers for the remaining areas of the Docklands.

3.7.76 The Authority advised that its financial performance is regularly reviewed by the Department of Treasury and Finance. At the time of these reviews, the Treasurer may vary the terms of the debt facility if deemed appropriate.

Stadium funding facility

3.7.77 In September 1997, the Authority entered into a lease arrangement which extends until March 2025 (being 25 years after the "practical completion" of the Stadium) with Docklands Stadium Consortium for the consortium to build, own and operate Colonial Stadium. As outlined in our May 1999 *Report on Ministerial Portfolios*, the Authority received an interest-free loan of $28.4 million from the developer as part of the arrangement.

3.7.78 The arrangement also provided an option for the Australian Football League to assume ownership of the Stadium, following expiry of the lease, by payment of $30 million to the Authority within 12 months of the practical completion of the Stadium. If the League exercised this option, the Authority was liable to repay the loan of $28.4 million to the developer.

3.7.79 The Australian Football League exercised its option in relation to Colonial Stadium by payment of $30 million to the Authority in April 2001. On receipt of this amount, the Authority repaid $28.4 million to the Docklands Stadium Consortium in full settlement of the loan.

3.7.80 Of the amount of $30 million received from the Australian Football League, $29.1 million has been utilised on infrastructure works associated with the Stadium precinct.

Specific infrastructure developments

3.7.81 A number of major infrastructure and related works have taken place in and around the Docklands area to facilitate development, meet service obligations to the Docklands Stadium and to integrate the waterfront with Melbourne. Major works include:

- **Wurundjeri Way.** The Government has provided funding totalling $46 million, via the Department of Infrastructure and the Roads Corporation (VicRoads), as a contribution for the construction of Wurundjeri Way, and $1 million for the extra costs associated with bringing forward the timing of associated tramworks.

Wurundjeri Way is a replacement 4-lane State Highway opened to traffic in April 2000 and replaces Footscray Road (now renamed Harbour Esplanade). The 2 kilometre highway links the Montague Street intersection at the Westgate Freeway with Footscray Road. The road begins at the realigned Charles Grimes Bridge, crosses the Yarra River as it turns onto Flinders Street, and runs parallel with Spencer Street, under the new Bourke Street Pedestrian Bridge and La Trobe Street Bridge to connect with Dudley Street and onto Footscray Road and the City Link.

The total cost of the project, which includes the reconfiguration of the Charles Grimes Bridge, will be $55 million with $47 million funded by the Government, as part of Victoria's State Highway network, and $8 million from the Authority via the debt facility. The Government contribution funded the public works component of the project associated with non-Docklands related traffic such as traffic travelling south from the western suburbs, commercial vehicles using Docklands as a regional corridor, port traffic and general regional traffic growth. Ownership of the road was transferred to VicRoads upon its completion during 1999-2000.

In February 2001, Transurban, a private sector consortium for the financing, construction and operation of the Melbourne City Link, lodged a $35.8 million claim against the Government seeking compensation for loss of revenue associated with the construction of Wurundjeri Way, and the widening of the Westgate Freeway. Transurban considers that these developments will have a material adverse effect on traffic volume on the City Link. The Government has indicated that it will contest the claim.

- **Charles Grimes Bridge.** The upgrading of Wurundjeri Way by VicRoads required the reconfiguration of the Charles Grimes Bridge at an estimated cost of $17 million which was included in the total cost of construction of Wurundjeri Way. Walter Constructions commenced construction of a bridge design, which was subsequently identified as not being in accordance with contractual requirements, and encroaching on Crown land leased to a private company. The contractor requested VicRoads assistance in October 1999 to compulsorily acquire the land and VicRoads, in turn, sought the Authority's assistance to secure a commercial outcome on compulsory acquisition. Negotiations were completed and access to the land was granted in December 1999. VicRoads is in the process of negotiating to recover from the contractor all the costs incurred by VicRoads and the Authority associated with the acquisition.
- **Bourke Street Pedestrian Bridge.** The bridge, completed at a cost of approximately $30 million by the Authority, excluding platform access and ticketing machines, links the Melbourne central business district and Spencer Street Station with Colonial Stadium and the Docklands waterfront.

PHOTO NOT AVAILABLE

The completed Bourke Street Pedestrian Bridge.

- **La Trobe Street Bridge.** This bridge was funded by the Authority at a cost of $25 million.
- **Harbour Esplanade.** Esplanade works are estimated to cost $33 million over the next 10 years, of which $10 million is to be funded by the Authority as part of its trunk infrastructure expenditure and the balance by the successful developer of the Victoria Harbour Precinct.
- **Tram extensions/ticketing.** Tram extensions have been completed along Flinders Street and LaTrobe Street at a cost of $17 million. In addition, the Authority has gained agreement from the Department of Infrastructure that its exposure for automatic ticketing equipment is capped at $2.6 million with any additional costs to be met by the Department of Infrastructure.
- **Collins Street Bridge.** A bridge extending Collins Street into the Docklands was announced by the Government in June 2000. The bridge which has an estimated project cost of around $38 million will extend over the Spencer Street Station railway tracks and Wurundjeri Way before descending into the Batman’s Hill precinct. The construction of the bridge is expected to commence in 2001 and take approximately 18 months to complete. The Authority is expecting to recoup the cost of its construction from the sale of land.

- **Gas Regulator Station.** The Authority has commenced work to relocate a Gas Regulator Station (GRS) from its current above ground location in Blythe Street within the Melbourne Docklands. In-principle agreement was reached among the gas distribution companies that utilise the GRS and the Office of Gas Safety to relocate the GRS to other locations both within and outside the Docklands area. The works need to be undertaken during lower gas demand periods, such as the summer months, and are currently programmed for November 2001 to April 2002.
- **West Melbourne Gasworks Site remediation works.** The works, estimated to cost $51.9 million, are required under a clean-up notice issued to the State Electricity Commission of Victoria (SECV) under the *Environmental Protection Act* 1970. The Authority is acting as project manager on behalf of the Department of Treasury and Finance which assumed funding responsibility for the site (funded via an SECV dividend payment made in the 1999-2000 financial year).

PHOTO NOT AVAILABLE

Remediation works carried out at Victoria Harbour precinct.

Municipal activities of Docklands Authority

3.7.82 From July 1999, the Authority assumed responsibility for municipal activities associated with the Docklands area from the Melbourne City Council. Accordingly, assets, including roads, drains and footpaths, valued at $6.9 million, were transferred from the Council to the Authority during the 1999-2000 financial year. As previously referred to in this Report, the Government has announced its intention to return municipal responsibility to relevant local government authorities. The details and actual timing of the transfer are yet to be established.

3.7.83 To assist the future transition of municipal arrangements, the Docklands Authority decided that occupiers in the Docklands area would be levied rates on the same basis as occupiers in the Melbourne central business district, namely, at a fixed rate based on the net annual value of their property. However, as detailed in our May 1999 *Report on Ministerial Portfolios*, the development agreement with Stadium Operations Ltd provides for a partial exemption from rates and for a separate agreement with the Authority.

3.7.84 During negotiations with the Stadium Development Consortium, an issue arose as to the rates that will be payable in respect of the Stadium land. Under the *Cultural and Recreational Lands Act* 1963, the Melbourne Cricket Ground, National Tennis Centre (Melbourne Park), Flemington Racecourse and other "recreational lands" enjoy capped rates for municipal and other services. These stadiums are required to pay rates calculated as a reasonable charge for the services provided after taking into account the benefit derived by the community from the recreational land. However, the Authority subsequently identified that the Stadium did not fall within the strict definition of "recreational land" and therefore was not entitled to be subject to the "charge for service" regime under the Act.

3.7.85 **To ensure that the stadium was not placed at a competitive disadvantage, the previous Government decided that the Docklands Stadium should have a comparable rating regime to competing stadia in Melbourne. A formal instrument to limit rates payable by the Stadium was approved by the Treasurer in May 2000.**

Redevelopment of Spencer Street Station

3.7.86 The Government has commenced preparation of a master plan for the Spencer Street Station precinct covering an area of around 21 hectares and stretching from Dudley Street, along Adderley and Spencer Street and down Flinders Street.

3.7.87 The Spencer Street Station redevelopment comprises a major refurbishment of the rail terminal, the provision of significant new transport infrastructure and the integration of the precinct with the west end of the Melbourne central business district and Docklands. The redevelopment may include an airport-style concourse, restaurants, shops, and links to the Docklands Stadium and beyond. The Government plans include a multi-modal interchange for passengers on country and metropolitan rail services, trams and regional buses and the commercial development of the Station as an international business and tourism centre. This is in addition to rail infrastructure required to facilitate fast trains to regional centres, as announced in September 2000, and the airport rail link, which is currently subject to a feasibility study.

3.7.88 The Minister for Transport announced in June 2000 that the project was likely to proceed with private sector involvement under the Government's *Partnership Victoria* program. The Government has allocated $3 million in the 2000-01 financial year for the development of a concept plan for Spencer Street Station, together with a master plan for the 21 hectare site.

3.7.89 In December 1999, Parliament passed the *Rail Corporations and Transport (Amendment) Act* 1999. One of the purposes of the legislation was to establish the Spencer Street Station Authority. The functions of the Authority are to manage the precinct and its development for transport and related purposes, and to monitor current and future requirements for transport facilities at the precinct.

3.7.90 Given the transfer of responsibility for development of this area to the Spencer Street Station Authority, the precinct is no longer considered to be part of the Melbourne Docklands development.

Business Park precinct tender process

3.7.91 In May 1996, the Authority sought expressions of interest for the development of the 36.2 hectare Business Park precinct. Following an evaluation between June and October 1997 of indicative bids received, 7 parties were short-listed and invited to submit proposals for the financing and development of the precinct. After assessing the bids, the Authority formed the view that the precinct potential would be maximised through sub-dividing it into two parts.

3.7.92 The Authority's processes for bid evaluation and negotiation was previously outlined in our May 1998 *Report on Ministerial Portfolios.* In summary, the evaluation process includes consideration of the following criteria: design and amenity; integration; finance and risk considerations; commercial viability; and other issues including any risk or benefit to the State or the Authority flowing from the development.

3.7.93 In February 1998, the Authority's Board recommended to the Government that the Authority enter into development agreements with the following 2 successful bidders:

- Studio City Melbourne Pty Ltd for a $500 million development of an area known as Part A of the precinct, comprising a theme park, working film studio, cinema megaplex and retail outlets, subject to achieving financial close by October 1999; and
- MAB Docklands Corporation Pty Ltd (MAB Docklands) for an area known as Part B of the precinct on the condition that outstanding issues identified during the evaluation process were successfully resolved by July 1998.

3.7.94 In relation to the area known as Part A of the precinct, a conditional development agreement was executed with Studio City Melbourne Pty Ltd in March 1998. In October 1999, the Authority approved a contract time extension for the developer for financial close by the end of March 2000 which was later extended to 30 June 2000. However, in June 2000, the Authority terminated the conditional development agreement due to the financial failure of Studio City Melbourne Pty Ltd.

3.7.95 In relation to the area known as Part B of the precinct, the Authority's Board granted an extension of time to MAB Docklands to resolve commercial viability issues relating to the development proposal, which subsequently occurred in June 1998.

3.7.96 **A probity audit by the Authority in relation to MAB Docklands was conducted with no adverse findings. The probity auditor appointed to oversee the tender and selection process concluded in reports issued in November and December 1998 that the bidders of this element of the Business Park precinct received fair and equitable treatment in the various stages of the process.**

3.7.97 In April 1999, a development agreement was entered into with the successful developer, MAB Docklands, for part B of the Business Park Precinct.

3.7.98 In June 2000, MAB Docklands took possession of the land and commenced construction of Stage 1 of the development on 0.74 hectares of the 13.8 hectare site. Additional design works relating to the potential integration of this site with Studio City delayed construction by 8 months (as the original due commencement date was in October 1999).

3.7.99 MAB Docklands' proposal includes a $900 million property development called pment horizon of between 10 to 15 years. The "New Quay" development is proposed to include a mixture of 1 800 residential apartments, over 20 000 square metres of retail space, which will include restaurants and shops, as well as 100 000 square metres of "high-tech" commercial space. The development is also expected to incorporate 250 room hotel/serviced apartments and a 300 vessel marina.

PHOTO NOT AVAILABLE

MAB "New Quay" Stage One under construction.

Key rights and obligations under the development agreement

3.7.100 The key rights and obligations allocated to the developer, MAB Docklands, and the Authority under the development agreement for Part B of the Business Park precinct are outlined in Table 3.7H.

TABLE 3.7H
KEY OBLIGATIONS OF PARTIES UNDER THE DEVELOPMENT AGREEMENT

Obligations of the developer	*Obligations of the Authority and the State*
Land sales and revenue sharing	
Pay $3.9 million (in 1998 dollars) adjusted for CPI movements over a period of 10 years commencing in April 1999 for acquisition of the 13.8 hectare site. Make additional payments where the value of land transferred exceeds the amount in the schedule of fixed payments. Under revenue sharing arrangements, progressively pay the Authority a fixed share of revenue generated from sales made by the developer.	No key obligations
Construction	
Must complete specified works in accordance with a schedule of practical completion milestones. May seek approval to construct 600 additional residential apartments but must pay the Authority additional specified amounts for these additions. Must rectify areas of non-compliance with quality standards as identified by an independent assessment before practical completion of a stage. Accepts all risks and costs of dealing with community objections. Has responsibility for all site conditions and bears the risk of loss or damage to land, the works and the project. Must meet all costs associated with any demolition required before commencement of construction. Must develop and install all precinct infrastructure. Make a fixed contribution of $7.8 million (paid in April 1999) for trunk infrastructure constructed by the Authority.	Assume any cost associated with any change in precinct boundaries or to final plans and specifications initiated by the Authority, a government agency or the State. May approve, at its discretion, the development of 600 additional residential apartments. Bears the risk of any costs associated with any government delay in access to the site by the developer. Bears all risks relating to site-specific legislation, which affects industrial relations. Is responsible for the development of basic infrastructure covering the Docklands precinct.
Other	
Must meet all remediation costs necessary to obtain a statement of environmental audit. However, the developer has no responsibility to remedy any pollutant or contaminant in the water or on the river bed, except where the pollutant or contaminant is disturbed by the developer. Must enter into an agreement under the *Planning and Environment Act* 1987 precluding claims against the State and Authority for any further remediation works under subsequent redevelopments. Must maintain landscaping within stages, as stages are developed to the satisfaction of the Authority. Must allocate an amount equivalent to 1 per cent of total development costs to public art and development of public areas including a contribution of 0.2 per cent of the development costs to the Authority to be spent on specific artworks spread throughout the Docklands area.	Is liable for any costs arising from more stringent environmental standards imposed by changes in State legislation. Must spend a portion of the development cost contributed by the developer (0.2 per cent) on specific artworks spread throughout the Docklands area.

Provisions within the agreement for default events

3.7.101 The development agreement also incorporates extensive provisions related to default events, including:

- failure to comply with the agreement;
- failure to achieve a milestone date or a date for stage practical completion;
- a decision by the financiers to cease funding the project;
- the developer abandoning or substantially ceasing to carry out the works for more than 4 consecutive weeks, other than in accordance with the agreement;
- material failure to proceed with the works in accordance with the works program, the development plan or approved documents;
- non-payment of any sum due to the Authority under the agreement or the land sale contract within 5 business days after the amounts become payable; and
- the developer ceasing to have access to the technical capacity to achieve project practical completion.

3.7.102 In relation to default events, the agreement provides for the developer or, in certain circumstances, its financier to:

- pay interest, accruing at a daily rate, for delays in project completion; and
- pay compensation to adequately redress the Authority's loss or damage caused or contributed to by the default where the default event occurs after practical completion of the project.

3.7.103 The agreement also provides for the developer to indemnify the Authority and the State, on demand, for all losses, liabilities, costs and expenses, in connection with the occurrence of any default event for which the developer or its employees, agents, sub-contractors or consultants is responsible.

Provisions for termination of the agreement

3.7.104 The Authority may terminate the agreement with the developer if:

- a default event has occurred before project practical completion and the default is not cured or not capable of being cured by the developer or financier; or
- commencement of construction of less than 90 per cent of the project has not occurred by an agreed date.

3.7.105 If the agreement is terminated by the Authority then the developer, with effect from the date of termination, grants to the Authority and all persons authorised by the Authority, a licence to use and reproduce all of the project development rights, title and interest in and to all the approved design documentation.

3.7.106 In the event of the developer not proceeding with the development, the Authority may call upon a performance guarantee issued in its favour for the project. Furthermore, the Authority may claim damages from the developer in the event that the costs exceed the performance guarantee.

3.7.107 If the Authority terminates the agreement due to a default event not remedied or a termination event, the rights and obligations of each of the parties are specified in the agreement.

3.7.108 In summary, under the agreement, many of the day-to-day design, construction and ownership risks are assigned to the developer. The State has retained certain risks associated with areas such as changes in legislation, pre-existing contamination and pollutants, changes to precinct boundaries or final plans, site access delays and risks associated with a lack of market demand.

Adequacy of the Business Park land and trunk infrastructure sale price

3.7.109 The Authority will receive a minimum of $11.7 million from MAB Docklands, comprising $3.9 million from the sale of land (adjusted for CPI movements from July 1997), and a trunk infrastructure contribution of $7.8 million. This amount excludes the benefit to be derived from the revenue sharing scheme and public art contribution as outlined in Table 3.7H. At the date of preparation of this Report, $8.7 million had been received.

3.7.110 The sale price was approved following an assessment by the Valuer-General of the value of land to be transferred to the developer. This assessment was based on the reasonableness of the bid proposal within the general parameters of the land uses proposed by MAB Docklands and included a market analysis of selling prices, selling rates, rental income streams and proposed project costs as outlined in bid documentation, among other general valuation considerations. In assessing the land price component of the bid, the Valuer-General considered market data inside and outside the Docklands area. On this basis, the Valuer-General concluded that the settlement price under the arrangements with MAB Docklands was reasonable.

3.7.111 In February 1999, the Valuer-General concluded that the proposed project provides a reasonable prospect for the achievement of an economically viable outcome, the project does not have an unacceptable degree of risk attached to it and the current bid offered for the site is considered reasonable.

Conclusion

3.7.112 The Docklands Authority has made substantial progress towards increasing the rate of development within the Melbourne Docklands, particularly through finalisation of its recent agreement for a $1.8 billion development of the Victoria Harbour precinct. The rate of completion of trunk infrastructure necessary for the future development of various Docklands precincts has also increased with total expenditure of $177 million incurred to 31 December 2000.

3.7.113 During the year, responsibility for the redevelopment of the Spencer Street Station and surrounding areas at the west end of the Docklands project was allocated to a new public sector agency, the Spencer Street Station Authority. Co-operation between the Docklands and Spencer Street Station Authorities will be required to ensure that development works in both these key areas are complementary to the overall vision for the west end of Melbourne.

3.7.114 The review of the associated agreements entered into by the Docklands Authority for the Business Park precinct has identified that the Authority has implemented appropriate processes to ensure fair and equitable tendering and selection processes for development projects and appropriate protection to the State from any risks that may result from development agreements with the private sector. **It will, however, be necessary for the Authority to ensure that all relevant increases in the value of trunk infrastructure for the Melbourne Docklands are recovered from the settlement proceeds from future development agreements with the private sector.**

REGIONAL INFRASTRUCTURE DEVELOPMENT FUND

3.7.115 In December 1999, under the authority of the *Regional Infrastructure Development Fund Act* 1999, the Regional Infrastructure Development Fund was established as a trust fund within the Public Account under the responsibility of the Minister for State and Regional Development.

3.7.116 The Fund is administered by the Department of State and Regional Development which is responsible for:

- assessing funding submissions and proposals and making recommendations to the Minister;
- monitoring the progress of approved projects;
- assessing and evaluating project outcomes; and
- financial management and accountability.

3.7.117 Over a 3 year period to June 2003, a total of $180.7 million (including $54.4 million for 2000-01) is to be provided from the Fund for infrastructure projects that benefit or support the development of regional Victoria. These projects include:

- industry development, such as physical works, to facilitate economic development;
- transport improvements, such as roads, rail, ports or airports, of strategic regional significance;
- tourism-related capital works; and
- strategic education, and information and communication technology infrastructure.

3.7.118 Under the arrangements established for the operation of the Fund, there are 2 funding rounds per year (except for the first year where there will be 3 rounds) where applications are sought by advertisement in major regional newspapers. Further submissions may also be accepted throughout the year and evaluated on a case-by-case basis subject to the availability of funding. The intention is to contribute towards, rather than fully fund, a project.

3.7.119 The establishment of the Fund was a major commitment of the Government in its pre-election policy statement, Reviving Regional and Rural Victoria. The aim of the policy is to rebuild country Victoria and assist investment attraction, employment and export through infrastructure projects which build on regional strengths and provide scope for new business activity and private sector co-operation.

Planning for an effective program

3.7.120 An effective grants program must be well planned and the Department's planning processes have addressed a number of the necessary elements including establishing:

- objectives, eligibility criteria and assessment procedures;
- a suitable administration and accountability framework reflecting the underlying risk and materiality of individual grants; and
- an effective monitoring regime.

3.7.121 In establishing the grant program the Department has identified the following key risks:

- awarding grants to ineligible organisations which may not be able to complete a project effectively;
- awarding grants for projects which are inconsistent with the Fund's objectives;
- grants being used for purposes contrary to the terms and conditions of the funding arrangements; and
- ongoing recurrent commitments of the projects being passed on to the State.

3.7.122 Specific action taken by the Department in this regard is commented upon later in this Part of the Report.

3.7.123 Nevertheless, we found that an aspect of the planning process in terms of performance measurement was not addressed. Specifically, at the outset the Department had identified certain information relating to project outcomes it required from recipients. However, as performance indicators had not been developed during the planning process the Department could not be certain the performance information relating to project outcomes required to be submitted by recipients was relevant and appropriate for measuring the Fund's objectives. The Department is currently addressing this aspect which is commented upon later in this Part of the Report.

3.7.124 **Aside from the issue of developing performance indicators, we consider the Department's planning processes were adequate.**

Establishment of an administration and accountability framework

3.7.125 The administration and accountability framework for managing the Department's responsibilities associated with the Fund exhibits several strong features which will assist the achievement, over time, of the Government's policy objectives. These features include:

- detailed explanatory guidelines for applicants covering the assessment, approval and monitoring of funding provided to organisations;
- prioritisation of projects to determine provision of assistance; and
- a management control framework governing the provision of funding.

Development of guidelines

3.7.126 In early 2000, the Minister issued draft guidelines and application forms following consultation with relevant bodies such as municipal councils and industry bodies. After taking account of feedback received, in May 2000, the Minister issued *Guidelines – Regional Infrastructure Development Fund* for parties seeking assistance for infrastructure development projects from the Fund.

PHOTO NOT AVAILABLE

Guidelines developed by the Department on behalf of the Minister to assist organisations when submitting a grant application.

3.7.127 The *Guidelines* include details of:

- eligibility criteria and projects which would not be eligible for funding;
- who can apply;
- funding available; and
- funding conditions.

3.7.128 Details of eligibility criteria are shown in Table 3.7I.

TABLE 3.7I
PROJECT ELIGIBILITY CRITERIA

Socio-economic
Applicants are required to clearly demonstrate how the proposed project will address each of the following: • enjoys local community and industry support; • consistency with ecologically sustainable development; • builds on identified key regional strengths; • adds value to existing products and services; • attracts investment and complements other investments in region; • creates jobs and stimulates regional economic growth; • provides an adequate social and/or economic return to the community; and • facilitates the integration of the region into global markets.
State and regional priority
Applicants are required to clearly demonstrate how the proposed project is consistent with: • objectives and key outputs of local or regional economic development strategies; and • the Victorian Government's stated policy commitments to regional Victoria.
Project feasibility and delivery
Applicants are required to demonstrate: • Access to project management experience in both the developmental and operational phases of the project; • All legal, land tenure, planning and environmental issues have been identified and resolved (or satisfactory resolution strategies are in place). For example, is the project or part of the project subject to any planning, environmental or heritage approval, permit, licence or requirement?; • The project is ready for implementation in the scheduled timeframe; • Project risks have been identified and strategies in place to manage them; and • Adequate project delivery and management arrangements in place, including system establishment to monitor progress payments, confirm funding contributions by others and measure agreed benefits upon completion.
Financial
Applicants are required to: • maximise funding support from a range of sources, Commonwealth and local government, community, private sector and regional organisations; • demonstrate that the viability of the project is not dependent on ongoing funding or continuing government support; and • demonstrate how future operating costs will be underwritten without recurrent subsidy from State Government sources.

Source: Guidelines – Regional Infrastructure Development Fund.

3.7.129 The *Guidelines* were distributed to all Members of Parliament so that they could encourage communities in their electorates to apply for funding. In addition, the Fund was promoted to potential recipients through the media, through dispatching publications to relevant groups and by lodging information on the internet. Departmental staff also liaised with potential applicants prior to them submitting their application with a view to ensuring quality applications.

3.7.130 Of the initial 166 applications received in the first 2 rounds, a large number had not been satisfactorily completed in that applicants did not clearly indicate the objectives of the proposed project and related costings. This necessitated additional information being sought from a number of applicants which in turn resulted in delays in completing the assessment process. For example, in the first round of applications on average 98 days elapsed from the receipt of an application until a recommendation was submitted to the Minister for approval. This was reduced to 79 days in the second round. We understand that, in addition to incomplete applications, the initial delay was exacerbated further due to staff responsible for assessing applications not commencing duties until around 60 days after the close of round one applications.

3.7.131 In January 2001, the Department reviewed its processes which included discussing its approach with some applicants. Potential enhancements to the application form were subsequently identified, considered and adopted as deemed appropriate prior to the 3rd round of funding applications in March 2001.

3.7.132 Additional guidelines have also been established for the Fund's 2 sub-programs, which have Statewide impacts, namely:

- construction of stock underpasses and overpasses; and
- upgrading of power infrastructure for dairy farms.

3.7.133 **Overall, we consider that the guidelines developed by the Department on behalf of the Minister to inform and assist parties in preparing funding applications were clear and provide sufficient detail of the eligibility criteria.**

Prioritisation of projects

3.7.134 The Department's approval process comprises 4 key stages which are outlined in Chart 3.7J.

CHART 3.7J
KEY STAGES IN THE APPROVAL PROCESS

Initial assessment
Applications assessed for eligibility and allocated high/low priority.

↓

Detailed assessment
If an application is deemed eligible it will undergo further assessment. Comments are sought from other departments relevant to the project and a financial risk assessment is carried out.

↓

Regional Infrastructure Development Committee
All applications are presented to a Regional Infrastructure Development Committee for further assessment and recommendation is made to the Minister.

↓

Ministerial approval
Recommendations on all applications are forwarded to the Minister for consideration and final approval.

3.7.135 Senior staff of the Department are responsible for the initial assessment of all applications received. If an application is deemed eligible it will undergo further assessment which includes obtaining comments on the proposed development from other relevant government departments and agencies.

3.7.136 Funding proposals submitted by applicants are assessed against a number of criteria specifically linked to the purpose for establishing the Fund and are required to demonstrate the applicant's ability to meet a significant number of the criteria. As many applications meet a significant number of the general eligibility criteria to some degree, in July 2000 specific criteria was established by the Department to assist in prioritising projects. Aspects considered in developing the criteria included the general criteria, the guidelines and the legislation relating to the Fund. Chart 3.7K outlines the criteria utilised to prioritise projects.

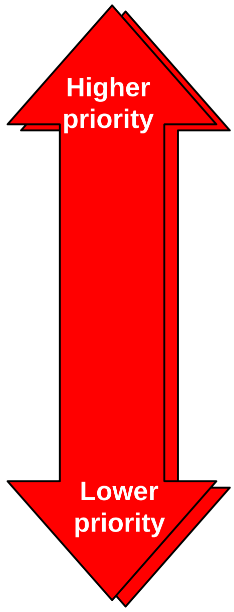
CHART 3.7K
CRITERIA FOR PRIORITISING PROJECTS

Higher priority projects

- *Rates highly in terms of demonstrable project benefits related to sustainable employment, investment and exports;*
- *Is a State or regional priority;*
- *Maximises funding support from a range of sources; and*
- *Is ready for implementation.*

Lower priority projects

- *Can be implemented through another government funding program;*
- *Does not relate to the key areas of focus of the Fund (economic infrastructure, tourism, transport linkages or education and information communication technology infrastructure);*
- *Does not have a demonstrable social and economic benefit;*
- *Is not ready for implementation;*
- *Is not a State or regional priority; and*
- *Does not maximise funding support from other sources.*



Source: Department of State and Regional Development.

3.7.137 The prioritisation criteria are applied in the initial assessment of applications and again when more detailed assessments are undertaken. The more detailed assessments involve extensive internal departmental discussions and referrals to other agencies, such as the Department of Infrastructure. This culminates in a recommendation to the Regional Infrastructure Development Committee, an inter-departmental committee comprising representatives from the Department of State and Regional Development, Department of Infrastructure and Department of Premier and Cabinet. The Department of Treasury and Finance sits on the Committee in an observer role for those applications seeking $2 million or more from the Fund.

3.7.138 The Committee assesses applications in the context of the Guidelines applicable to the Fund and provides a recommendation to the Minister for State and Regional Development. Those applications that seek funding of $2 million or more are also forwarded to the Minister for Finance for authorisation.

3.7.139 The prioritisation framework was established subsequent to calling for funding applications and accordingly in the first round approximately 100 applicants submitted proposals for funding without being aware of the prioritisation criteria. These applicants were potentially disadvantaged through not being aware of the aspects that need to be emphasised to give their project the best chance of success. We also noted that, notwithstanding the establishment of criteria, the Department has not assigned a weighting to rank the relative importance of each criteria.

3.7.140 **We consider the Department should explore the feasibility of ranking the relative importance of each criteria and re-write them more succinctly with a view to enhancing its selection and prioritisation process.**

Management controls

3.7.141 For structured management controls governing the provision of funding to be effective they should include:

- criteria for assessing applications;
- formal agreements (based on the nature, risk and value of funds provided) outlining the terms and conditions of assistance including:
    - roles, expectations and obligations of each party;
    - purpose of the project;
    - clauses to cover project failure;
    - desired output and outcomes of the project; and
    - content of status and financial reports, including possible audit requirements;
- progressive disbursement of funds based upon achievement of agreed milestones; and
- ongoing monitoring of projects, including site visits.

3.7.142 **Based upon our examination, we consider that the Department's processes for managing the assessment, approval and monitoring stages under the Fund constitute a sound management framework. Agreements were clear and appropriate to the nature, risk and value of funds provided.**

Measuring the fund s achievements

3.7.143 The Department has commenced development of a performance and reporting framework. This framework will measure actual achievements against expected outputs and outcomes in order to assess the effectiveness of the Fund. At the date of preparation of this Report, work had commenced on developing some performance indicators and upgrading the management information system to facilitate the collection of data on project outcomes in terms of the Fund's objectives.

3.7.144 **The development and implementation of a performance and reporting framework for the Fund should be a high priority for the Department, including the collection of relevant data.**

Distributions from the Fund

3.7.145 As it is not the Government's intention to fully fund projects, applicants are encouraged to seek funding from other sources as well, such as Commonwealth and local government and private sector organisations. Consequently, the Department has established mechanisms to ensure it co-ordinates its activities with those agencies that administer similar grant programs.

3.7.146 The Department informed our Office that in some cases where an application for funding from the Fund has been rejected, it has assisted a number of applicants obtain funding from other funding programs. For example, a council in the Western Region applied for funding from the Regional Infrastructure Development Fund of $582 000 for a Community Resource Centre and, although not approved, the council was assisted in successfully negotiating funding of $290 000 from the Community Support Fund.

3.7.147 At March 2001, the Department had received 166 first and second round applications seeking funding totalling $227 million. Eighteen applications were subsequently approved with funding totalling $37.7 million to be made from the Fund for projects worth $85.9 million. At the date of audit, the Department was assessing a further 16 third round applications. Chart 3.7L illustrates the total amount of funding sought and the funding approved as at March 2001 in the Department's 5 rural regions.

CHART 3.7L
REGIONAL AREAS ASSISTED BY THE FUND,
MARCH 2001

CHART NOT AVAILABLE

3.7.148 As can be seen from Chart 3.7L, at March 2001 funding under this initiative has been provided to all regional areas, with the most provided to the South-West Region ($15.4 million) and the least to the North-East Region ($550 000).

Approved projects

3.7.149 Table 3.7M illustrates the range of approved projects and amount of funding provided to applicants at March 2001.

TABLE 3.7M
APPROVED PROJECTS AND DISTRIBUTIONS FROM THE FUND, AS AT MARCH 2001
($'000)

Applicant	*Project*	*Total project cost*	*Amount approved*	*Actual funds provided*
Gippsland				
Latrobe City Council	Latrobe Regional Airport Development.	350	270	-
Parks Victoria	Buchan Caves Infrastructure Development Works.	1 090	605	-
East Gippsland Shire Council	East Gippsland Regional Saleyards Redevelopment.	1 950	1 450	-
		3 390	2 325	-
North-East				
Greater Shepparton City Council	Shepparton Aerodrome – Extension of Runway.	280	200	-
Murrindindi Shire Council	Road Works to aid expansion of the Murrindindi Valley Economic Development.	837	350	-
		1 117	550	-
Northern				
Mt Alexander Shire Council	Reinstatement of rail facilities at Castlemaine Station.	100	100	-
Birchip Cropping Group Ltd	Expansion of research facilities through the construction of a new office, laboratory and conference facility.	550	110	-
Campaspe Shire Council	Restoration of rail link from Echuca Station to Port of Echuca.	465	185	-
Latrobe University Bendigo	Refurbishment of campus building to create a Centre for Sustainable Regional Communities.	543	250	-
Greater Bendigo City Council	Industrial development in North Bendigo.	2 786	400	-
Lower Murray Water	Treated water to Thurla.	2 065	500	-
Loddon Shire Council	Upgrade of power and irrigation infrastructure to support high value crops, including peppers, tomatoes, grapes and olives in the Boort Region.	7 390	3 274	-
		13 899	4 819	-
Western				
University of Ballarat	Construction of an Information Technology Cluster Development on the Ballarat Technology Park.	3 400	2 600	-
		3 400	2 600	-

TABLE 3.7M
APPROVED PROJECTS AND DISTRIBUTIONS FROM THE FUND, AS AT MARCH 2001 – *continued*
($'000)

Applicant	*Project*	*Total project cost*	*Amount approved*	*Actual funds provided*
South-West				
Corangamite Shire Council	Development of Cobden Industrial Estate.	516	258	-
RMIT/Southern Grampians Shire Council	Construction of a RMIT Flexible Learning Centre in Hamilton.	3 415	3 135	-
City of Greater Geelong	Redevelopment of Geelong Central Activities Area (e.g. improvements in pedestrian access, off street parking and access to major infrastructure).	20 190	12 000	-
		24 121	15 393	-
Statewide				
Victorian Farmers Federation	Construction of cattle underpasses.	8 000	4 000	495
Powercor Australia Ltd and TXU Networks Pty Ltd	Power infrastructure to assist the expansion of dairy industry.	32 000	8 000	184
		40 000	12 000	679

3.7.150 In relation to the projects approved as at the date of audit, only 3 projects related to non-government entities, for grants approved totalling $12.1 million (Birchip Cropping Group, Victorian Farmers Federation, and Powercor Australia and TXU Networks Pty Ltd). As at March 2001, only $679 000 (1.8 per cent of approved funding applications) had been disbursed from the Fund. This is a reflection of the long-term nature of infrastructure development and that progress payments are subject to satisfactory achievement of milestones agreed with the Department by the recipients.

3.7.151 **We consider all approvals had been effected in accordance with the Fund guidelines, criteria established by the Department, and relevant legislation including the Fund's broader objectives. Our examination of a selection of applications received in the 2000-01 financial year indicates that the Department had complied with its structured management controls governing the provision of funding.**

3.7.152 **We also found disbursements were in line with milestones specified in the respective funding agreements. However, given the small amount disbursed at the date of audit, we will continue to monitor the disbursement of funds by the Department.**

Applicants' views on administration arrangements

Recipient visits

3.7.153 As part of the audit we visited 5 organisations which had proposals approved to assist us in forming an opinion on the adequacy of the application process, including the approval and negotiation of agreements. The organisations visited had received approval for funding totalling $26 million.

3.7.154 We found that all recipients were generally satisfied with the application process, in particular, the assistance given by departmental staff. The Fund was seen as an excellent initiative for the development of regional infrastructure in Victoria with 3 of the 5 organisations stating that, without funding, the projects would not have proceeded. In terms of improvements, the recipients suggested greater public visibility of approved projects as this would serve to increase the general awareness of the type of successful projects funded through the Fund.

Survey of applicants

3.7.155 As part of the audit, we conducted a survey of a sample of successful and unsuccessful applicants to ascertain their level of agreement or disagreement with key aspects of the application process. We surveyed 50 applicants (15 successful, 35 unsuccessful), with a response rate of 68 per cent (12 successful, 22 unsuccessful).

3.7.156 The survey found that 64 per cent of the respondents were satisfied with the Department's management of the application process. Details of the survey results are shown in Table 3.7N.

TABLE 3.7N
LEVEL OF AGREEMENT WITH KEY ASPECTS OF THE APPLICATION PROCESS
(per cent)

Survey questions	*Respondents overall level of agreement*	*Successful applicants*	*Unsuccessful applicants*
The Fund was adequately promoted.	76	81	74
The guidelines were clear and easy to follow.	74	83	69
The application form was clear and easy to follow.	74	75	74
There was sufficient time between advertising the availability of grants and the deadline for submitting applications.	68	77	63
The application processing time was reasonable.	60	67	56
Sufficient opportunity was provided to discuss the application prior to submission.	68	77	64
Constructive feedback was provided following rejection of their application.	47	n.a.	47

3.7.157 Given that the survey also included unsuccessful applicants (65 per cent of respondents), the result reflects well on the Department. Nevertheless, several applicants highlighted some concerns with the operation of the Fund, primarily that:

- funding appeared to be more focused on large regional centres than rural communities; and
- feedback on the progress and outcome of an application was not always provided in a timely manner (e.g. some of the applications lodged in May 2000 were not responded to until November 2000).

3.7.158 **We consider the Department should provide timely and complete information to applicants relating to the outcome of the assessment process.**

Overall conclusion

3.7.159 Overall, our examination found that the Department has established an adequate administration and accountability framework for grants provided under the Fund. There are processes in place to protect the State against risks associated with grant programs and the accountability requirements reflect the underlying risk and materiality of grants provided.

3.7.160 More work needs to be done by the Department in terms of improving its prioritisation of projects and establishing a performance measurement framework to assess the effectiveness of this initiative.

3.7.161 We also found that approvals to date were in line with relevant legislation, including the Fund's broader objectives.

***RESPONSE** provided by the Secretary, Department of State and Regional Development*

Planning for an effective program

As the administrative operations of the Regional Infrastructure Development Fund have been successfully established and implemented (as outlined in the Auditor-General's Report), the Department is now focusing on the establishment of performance measures for both the administration of the Fund and outcomes of funding. A report from successful project applicants identifying project benefits is included as a requirement in all funding agreements. Modifications are currently being made to the Fund database to facilitate the management of this information. An updated business plan identifying administrative measures is also under development.

Development of the Guidelines

The Regional Infrastructure Development Fund Guidelines were developed with input from core stakeholders. The Department has endeavoured to ensure that the Guidelines and Fact Sheets are widely distributed and available to all interested parties. Department staff are currently implementing a communication strategy to further promote awareness of the Fund.

After the first 2 funding rounds, Department staff reviewed and revised the Fund application form. Subsequent amendments were based upon feedback received from applicants, with the aim of further clarifying the information required in an application, thereby reducing the need to seek further detail from applicants during the assessment phase.

RESPONSE *provided by the Secretary, Department of State and Regional Development - continued*

Prioritisation of projects

All applications are assessed against the criteria established in the Guidelines and the Prioritisation Methodology. These documents are publicly available. Applicants unsuccessful in the first funding round when the Prioritisation Methodology had not been widely published are able to submit revised applications in future funding rounds where appropriate.

The Department considered the assigning of weights to criteria when establishing administrative processes for the Fund. However, it was agreed that given the wide scope of infrastructure projects covered by the Fund, i.e. tourism, transport, education and Information and Communication Technologies, and economic development, it was not feasible to assign weights to criteria. To do so would result in an assessment process skewed towards "industry development" projects in larger regional centres. Weighting would always result in these projects receiving a higher weighting than, for example, a tourism project in a smaller rural community, where the economic benefits are more indirect in nature, although just as important to the development of the region. The Department believes that the current assessment process contains both the formal criteria to ensure fair and consistent assessment and the flexibility to account for applications that vary greatly in nature and scope.

The Fund is a whole-of-government fund, and comments on applications are therefore sought from other departments and agencies as appropriate. This ensures that expert advice is included in the assessment process and that appropriate weight and consideration is given to all aspects of a project presented to the Committee.

Furthermore, criteria have, and continue to be established for specific classes of project. The Department of Natural Resources and Environment has assisted us to develop criteria specific to irrigation and saleyard projects, while VicRoads has assisted in the development of criteria for road applications. These criteria allow "like" projects to be compared and prioritised in a consistent fashion. Those identified as the highest priority in that category can then be compared with the priorities from other categories against the published criteria, and an overall decision made. It is the role of the Interdepartmental Committee to make this final decision and recommendation to the Minister.

The operation of the Interdepartmental Committee further ensures a comprehensive and fair assessment process. With representation from the Departments of Infrastructure, Premier and Cabinet, and State and Regional Development, the Committee consists of individuals with diverse experience and expertise. In addition, the Department of Treasury and Finance participates in Committee deliberations, in an observer capacity, for projects requesting funding of $2 million or more. The Committee takes a strong "whole-of-Government" role in weighing the economic and social benefits of potential projects, both in isolation and compared with other applications, further enhancing the rigour of assessment.

Management controls

Grants from the Fund are managed in accordance with the Department's grant management framework, which has operated effectively over an extended period. The Interdepartmental Committee adds a further level of management control to the process. The Fund database is currently being upgraded to further improve monitoring systems.

RESPONSE *provided by the Secretary, Department of State and Regional Development - continued*

Measuring the Fund's achievements

The Department acknowledges the importance of measuring the Fund's achievements, and with the Fund now "rolled out" and operating effectively, the Department is refocusing on the ongoing management of the Fund, particularly the measurement of outcomes. The stated objectives of the Fund are being communicated to stakeholder groups through a communication strategy. Upgrades to the Fund database are being undertaken to facilitate the recording and reporting of this information, which will be collected by Department staff during construction of, and on completion of funded projects. Clauses in all funding agreements ensure that the Department is able to seek relevant information from project proponents.

Approved projects

All eligible projects undergo assessment by Department staff. Further input is provided from other government agencies as appropriate. An Interdepartmental Committee reviews all applications and makes the final recommendation to the Minister. This process ensures that all approved applications are effected in accordance with the prevailing legislation and guidelines.

All disbursements from the Fund are conditional upon project proponents meeting certain milestones. These milestones are formalised in the relevant funding agreement. The Department will continue to ensure that payment to proponents is in accordance with the established agreements.

It is worth highlighting that the majority of funded projects have a construction phase of greater than one financial year. As a result, although a project may be approved in one year, often payments will be made in subsequent years. Under the performance-based contracts that are a feature of grants from the Fund, payment will always lag behind approvals.

Applicant's views on administration arrangements

The Department makes every effort to provide timely and complete information to applicants relating to the outcome of the assessment process. For the first funding round, the Department lacked resources to manage the large number of applications received within the preferred time lines. This has now been remedied, and significant improvements are being made in the time taken to assess applications and advise applicants of the result (as identified in this Report). The extensive assessment process, which includes advice from other departments and agencies, as well as assessment by an Interdepartmental Committee, does prolong the time taken to notify applicants, however, it is the Department's view that this is far outweighed by the benefits that this professional and comprehensive assessment process provides.

Furthermore, the Department strongly encourages applicants to discuss proposals before submitting them to the Fund. This allows applicants the opportunity to clarify any uncertainties and focus their proposals towards the Fund's objectives. Although the Fund has established funding rounds, applications may be accepted between rounds, on a case-by-case basis. This flexibility enables applicants who, for legitimate reasons, are unable to submit their application before the close of a funding round, to submit it at a later date.

RESPONSE *provided by the Secretary, Department of State and Regional Development - continued*

Applicant's views on administration arrangements *- continued*

Pre-application discussions with proponents also assist in identifying whether a proposal is best suited for funding. During initial discussions, Department staff may identify more appropriate sources of government funding for a proposed project. Where this is the case, Department staff will contact the appropriate funding agency to investigate the possibility of funding. Where it is established that the proposal has an opportunity of being successful under the alternative program, the project proponent will be referred on to this program for submission of their application.

When advising applicants on the result of assessment, Department staff contact each applicant to provide feedback. Applicants, therefore, have the opportunity to question staff about any aspect of the assessment and deficiencies in their application. All applicants also receive formal written notification of the outcome of the assessment process.

SCHEDULE A
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS

Report	*Subject*	*Status at date of preparation of this Report*

MATTERS RESOLVED OR ACTION COMMENCED

STATE AND REGIONAL DEVELOPMENT

Construction of the multi-purpose venue at Melbourne Park

Ministerial Portfolios, June 2000, pp. 303-8.	The construction of the multi-purpose venue was planned to be completed by November 1999. Project delays have resulted in the postponement of the opening of the facility. The projected final cost could not be determined as negotiations relating to contractor's final claims and rectification of defects was not complete.	The venue was handed over and available for use from 20 June 2000. Contract claims arising out of alleged acts and omissions of the Office of Major Projects and counter claims made by that Office against the contractor, including liquidated damages for late completion and defective work, have not been settled.

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS			
FINANCIAL YEAR ENDED 30 JUNE 2000			
Department of State and Regional Development *(a)*	2 Oct. 2000	4 Oct. 2000	✓
MAJOR PROJECTS AND TOURISM			
Australian Grand Prix Corporation	29 Aug. 2000	29 Aug. 2000	✓
Docklands Authority	30 Oct. 2000	30 Oct. 2000	✓
Emerald Tourist Railway Board	16 Aug. 2000	21 Sept. 2000	✓
Federation Square Management Pty Ltd	19 Oct. 2000	24 Oct. 2000	✓
Melbourne Convention and Exhibition Trust	30 Aug. 2000	4 Sept. 2000	✓
Tourism Victoria	23 Oct. 2000	23 Oct. 2000	✓
RACING			
Greyhound Racing Control Board	19 Sept. 2000	25 Sept. 2000	✓
Harness Racing Board	4 Sept. 2000	15 Sept. 2000	✓
SPORT AND RECREATION			
Melbourne and Olympic Parks Trust	19 Oct. 2000	19 Oct. 2000	Qualified opinion
(Reason for Qualification: Inappropriate recognition of a liability associated with a future contribution towards the construction of a new velodrome.)			
Melbourne Sports and Aquatic Centre Trust	6 Oct. 2000	6 Oct. 2000	✓
Melbourne 2002 World Masters Games Limited	13 Oct. 2000	17 Oct. 2000	✓
Melbourne 2006 Commonwealth Games Pty Ltd	13 Sept. 2000	4 Oct. 2000	✓
Victorian Institute of Sport Ltd	16 Aug. 2000	18 Aug. 2000	✓
Victorian Institute of Sport Trust	16 Aug. 2000	18 Aug. 2000	✓
STATE AND REGIONAL DEVELOPMENT			
Overseas Projects Corporation of Victoria Ltd	10 Oct. 2000	11 Oct. 2000	✓
Victorian Medical Consortium Pty Ltd	19 Oct. 2000	20 Oct. 2000	✓

(a) Name changed from Department of State Development with effect from 29 October 1999.

Part 3.8

Treasury and Finance

KEY FINDINGS

Financial standing of the Victorian WorkCover Authority

- During the 6-month period to 31 December 2000, the Victorian WorkCover Authority incurred an operating loss of $651 million, bringing the accumulated losses to almost $1.1 billion.

Paras 3.8.14 to 3.8.15

- The increase in the operating loss for the 6 months to 31 December 2000 has arisen due mainly to significant increases in the level of claims, the substantial reduction in investment revenue earned, and changes in economic assumptions used in the valuation of the outstanding claims liability.

Paras 3.8.16 to 3.8.19

- The Authority's consulting actuaries do not expect the WorkCover Fund to return to a fully-funded position before 30 June 2006, 3 years later than intended when the amending legislation was enacted in May 2000.

Paras 3.8.20 to 3.8.21

- The common law component of the outstanding claims liability had increased by around 138 per cent from $630 million to over $1.5 billion since 30 June 1998, with the majority of the increase taking place during the 2000 calendar year.

Paras 3.8.27 to 3.8.28

KEY FINDINGS *- continued*

Motor vehicle fleet management by Department of Treasury and Finance

- LeasePlan's contract to provide fleet management services to public sector agencies expired in May 2000. LeasePlan's offer to renew the contract at a revised fee was declined by the Department of Treasury and Finance. As a consequence, the Department assumed responsibility for providing fleet management services to those agencies previously contracted to LeasePlan.

Paras 3.8.52 to 3.8.58

- The Department had not determined the ongoing costs associated with providing fleet management services and, therefore, was not in a position to determine whether it should continue to provide such services in the future.

Paras 3.8.58 to 3.8.62

State Revenue Office information technology systems

- Over the past 3 years, the State Revenue Office (SRO) has embarked on a comprehensive information technology development project involving the key revenue systems of the State of Victoria. While changes have occurred over this time in the scope and timing of the project, these have been largely managed without significant impact to date on either the ultimate completion of key phases or the cost of the project.

Paras 3.8.65 to 3.8.98

- At 31 January 2001, the SRO had spent $19.9 million on the project and estimated that total direct costs associated with the project will amount to $30.2 million which is comparable with the initial cost estimate.

Paras 3.8.90 to 3.8.93

- The project is currently in the critical phases of testing and final implementation. The progress made in these final phases and the extent of any significant issues encountered at this stage will ultimately determine the success of the SRO in implementing effective revenue collection systems in line with the stringent timeframes established for the project. Any delays may also impact on both the direct costs of the project and the extent of internal resources utilised by the SRO on the project.

Paras 3.8.81 to 3.8.89 and 3.8.96 to 3.8.98

KEY FINDINGS *- continued*

State Revenue Office information technology systems *- continued*

- The cost estimate for the project may increase should existing systems and mainframe hardware be required to be operated past 30 June 2001 as a result of delays in meeting revised implementation dates for the new systems. The SRO has estimated that additional costs associated with operating the mainframe after 30 June would amount to around $50 000 per week.

Paras 3.8.90 to 3.8.93

- The SRO under a current policy does not allow credit card payment options by taxpayers. In light of the current trends toward e-commerce and the increasing usage by consumers paying by credit card, the appropriateness of the current policy may require review.

Paras 3.8.94 to 3.8.95

SUMMARY OF AUDIT RESULTS

3.8.1 The Treasury and Finance portfolio comprises the Department of Treasury and Finance and a diverse range of other entities that provide a broad range of services across Victoria and operate within highly complex industry sectors.

3.8.2 The Department of Treasury and Finance is one of the core central agencies within the Victorian public sector, with responsibility for the provision of leadership in economic, financial and resource management across the State. It is also responsible for the delivery of certain services associated with government financial accounting, liability management, budget production and risk management, and for leadership in these areas.

3.8.3 The Department includes the State Revenue Office which is the major revenue collection agency for the State and the Victorian Government Purchasing Board which is responsible for the establishment, promotion and oversight of procurement and contracting policies and guidelines within the budget sector.

3.8.4 The Treasury and Finance portfolio also incorporates a number of major public bodies whose activities mainly include:

- provision of financial services across the State – mainly through major financial institutions such as the Treasury Corporation of Victoria, the Victorian Funds Management Corporation and State Trustees Limited;
- management and administration of major insurance schemes - mainly the transport accident and workers' compensation schemes managed by the Transport Accident Commission and the Victorian WorkCover Authority, respectively, and the insurance arrangements for budget sector agencies managed by the Victorian Managed Insurance Authority;
- provision of superannuation to Victorian public sector employees - mainly through the State Superannuation Fund and the Emergency Services Superannuation Scheme;
- regulation of major utilities, mainly including the privatised electricity and gas industries – through the Offices of the Regulator-General, Chief Electrical Inspector and Gas Safety;
- regulation and oversight of casino and gaming operations across the State – through the Victorian Casino and Gaming Authority; and
- management of the residual financial obligations and other issues remaining from the previous privatisation of the electricity, gas and port industries – through the State Electricity Commission of Victoria and Gascor Pty Ltd.

3.8.5 The activities undertaken by entities within the portfolio have a significant effect on the allocation and effective management of the financial and other public resources applied across the State.

3.8.6 The Treasurer of Victoria, the Minister for Finance, the Minister for WorkCover and the Minister for Gaming have responsibility for public sector agencies within the Treasury and Finance portfolio, as outlined in Table 3.8A. These Ministers have collective responsibility for the Department of Treasury and Finance.

TABLE 3.8A
MINISTERIAL RESPONSIBILITY FOR
PUBLIC BODIES WITHIN THE TREASURY AND FINANCE SECTOR

Ministerial portfolio	*Entities subject to audit*
Finance	Emergency Services Superannuation Scheme
	Government Superannuation Office
	State Superannuation Fund
	Parliamentary Contributory Superannuation Fund
	Regulator General, Office of the
	Victorian Managed Insurance Authority
Gaming	Gambling Research Panel
	Tattersall's Club Keno Pty Ltd
	Tattersall’s Gaming Pty Ltd
	Tattersall’s Sweep Pty Ltd
	Victorian Casino and Gaming Authority
Treasurer	Arada Pty Ltd
	Arada Trust
	Chief Electrical Inspector, Office of the
	Gas Release Co. Pty Ltd
	Gas Safety, Office of
	Gas services business Pty Ltd *(a)*
	Gas Transmission Corporation
	Gascor Pty Ltd
	Gascor Holdings No. 1 Pty Ltd and its 3 subsidiaries
	Gascor Holdings No. 2 Pty Ltd and its 3 subsidiaries
	Gascor Holdings No. 3 Pty Ltd and its 3 subsidiaries
	Gascor (TH) Pty Ltd and one subsidiary
	Land Aggregation Program Trust Fund
	Met Train 1 (formerly trading as Bayside Trains) *(a)*
	Met Train 2 (formerly trading as Hillside Trains) *(a)*
	Met Tram 1 (formerly trading as Swanston Trams) *(a)*
	Met Tram 2 (formerly trading as Yarra Trams) *(a)*
	Property Leasing Limited
	Roslin Pty Ltd
	Rural Finance Corporation
	SEMCL No. 1 Unit Trust
	South Eastern Medical Complex Limited
	State Electricity Commission of Victoria and its 2 subsidiaries
.	State Trustees Ltd and its 7 common funds
	STL Financial Services Ltd
	Transport Accident Commission and its 3 subsidiaries
	Treasury Corporation of Victoria
	Tricontinental Holdings Ltd and its 3 subsidiaries
	Vicfleet Pty Ltd

TABLE 3.8A
MINISTERIAL RESPONSIBILITY FOR
PUBLIC BODIES WITHIN THE TREASURY AND FINANCE SECTOR

Ministerial portfolio	*Entities subject to audit*
Treasurer – *continued*	Victorian Energy Networks Corporation
	Victorian Funds Management Corporation and its 5 trusts
	Victorian Power Exchange
	Victorian Trauma Foundation
	Victorian Trauma Foundation Pty Ltd
	V/Line Passenger Corporation
	Western Underground Gas Storage Pty Ltd *(a)*
WorkCover	Victorian WorkCover Authority

(a) A final audit was conducted on this entity during the 1999-2000 audit cycle.

3.8.7 The annual reporting and audit requirements for the majority of entities within the portfolio are set out in the *Financial Management Act* 1994 and the *Audit Act* 1994. In particular, under section 45 of the Financial Management Act, each department and public body must submit its annual financial statements to the Auditor-General within 8 weeks of the end of the financial year. Under the Audit Act, the Auditor-General is then required to audit the financial statements within 4 weeks of their receipt. Finally, within 4 months of the end of the financial year or the next sitting day after the end of the fourth month, the relevant Minister is required to table in each House of the Parliament the annual report of each entity, which includes a report of operations and the audited financial statements.

3.8.8 The reporting and audit requirements relating to the gaming, club keno and lottery sweeps segments of Tattersall's operations are set out in the *Gaming Machine Control Act* 1991, the *Club Keno Act* 1993 and the *Tattersall's Consultations Act* 1958, respectively. Under these Acts, Tattersall's is required to prepare financial statements as soon as practicable following the end of each financial year and to submit these to the Auditor-General for audit. The audited financial statements are then required to be submitted to the Treasurer of Victoria who, in turn, is required to table them in both Houses of the Parliament.

Audit opinions issued

3.8.9 During the 1999-2000 financial audit cycle, clear audit opinions were issued on all financial statements prepared by entities within the portfolio, except for 2 sets of financial statements relating to Tricontinental Corporation Limited and Securities Finance Corporation Limited. These entities' financial statements were subject to audit qualification which related to the inappropriate disclosure of certain transactions between these 2 associated subsidiary companies. "Emphasis of matter" comment was also included in the audit reports of a number of entities to draw attention to certain matters that were considered relevant for the users of the financial statements, but not of such a nature that affected the audit opinion. Table 3.8B outlines these instances.

TABLE 3.8B
AUDIT OPINIONS INCLUDING EMPHASIS OF MATTER COMMENT, TREASURY AND FINANCE PORTFOLIO AGENCIES

Entities	*Reason for emphasis of matter*
Victorian WorkCover	***Inherent uncertainty regarding the valuation of the outstanding claims liability.*** A greater than initially anticipated number of claims were lodged with the Authority under the provisions of the *Accident Compensation (Common Law and Benefits) Act* 2000, relating to certain serious injuries incurred prior to November 1997 which were required to be lodged prior to the statutory deadline of 1 September 2000. Due to the proximity of the statutory deadline to the date of finalisation of the Authority's accounts, the impact of the claims on the Authority's outstanding claims liability and its net loss for the year could not be reliably determined. Further comment on this matter is included later in this Part of the Report.
Property Leasing Limited	***Inherent uncertainty relating to the valuation of financial liabilities.*** The financial liabilities of the company included various bonds valued at $278.2 million, with maturity dates ranging from the year 2011 to 2013. The value of these bonds as at balance date (30 September 2000) was based on the assumption that they would be redeemed at maturity. However, the financial statements highlighted that, if the bonds were redeemed prior to maturity, then the fair value at that time was likely to be different from the value recognised in the financial statements, which would impact on the reported result for that period. Subsequent to the issue of the audit opinion, the company was placed into voluntary liquidation, with the value of the bonds re-assessed by the company at $387.3 million.

Timeliness of financial reporting

3.8.10 As previously mentioned, legislation generally requires the audited financial statements of public sector entities to be completed within 12 weeks of the end of the relevant financial year, that is by 22 September of each year. Table 3.8C illustrates the performance of portfolio agencies in meeting this statutory requirement during the 1999-2000 reporting cycle.

TABLE 3.8C
TIMELINESS OF FINALISATION OF AUDITED FINANCIAL STATEMENTS, TREASURY AND FINANCE PORTFOLIO

	Entities	
Number of weeks after end of financial period	*Number*	*Per cent (cumulative)*
Less than 8 weeks	22	29
8 to 10 weeks	9	40
10 to 12 weeks	13	57
12 to 14 weeks	9	69
14 to 16 weeks	6	77
Over 16 weeks *(a)*	18	100

(a) Includes 4 entities whose financial statements had not been finalised at the date of preparation of this Report.

3.8.11 The table demonstrates that **there is scope for improvement in the timeliness of completion of audited financial statements by entities in this sector, with only 57 per cent of entities meeting the 12 week completion timeframe.**

3.8.12 Schedule A to this Part of the Report shows specific details of the financial statements and the issue of audit opinions.

3.8.13 **Timeliness of reporting is an essential characteristic of an effective accountability process. Accordingly, it is important that avenues are identified and pursued to improve the timeliness of the financial reporting process.**

FINANCIAL STANDING OF THE VICTORIAN WORKCOVER AUTHORITY

Overview of financial position and operating performance

3.8.14 Our *Reports on Ministerial Portfolios* in previous years have provided extensive comment on the financial standing of the WorkCover Fund managed by the Victorian WorkCover Authority. The common issue highlighted in these previous Reports has been the continued funding deficiency in the Fund, mainly due to the increasing growth in the outstanding claims liability.

3.8.15 Table 3.8D sets out the operating performance and financial position of the Victorian WorkCover Authority for the period from 1 July 1995 to 31 December 2000. Over this period, the financial position of the Authority, represented by the proportion of net assets held by the Authority to outstanding claims liability, has substantially deteriorated and the Authority has incurred substantial operating losses. **During the 6-month period to 31 December 2000, the Authority incurred an operating loss of $651 million, bringing the accumulated losses to almost $1.1 billion.**

TABLE 3.8D
VICTORIAN WORKCOVER AUTHORITY,
SUMMARY OF OPERATING PERFORMANCE, FINANCIAL POSITION AND FUNDING LEVELS,
FOR THE PERIOD FROM 1 JULY 1995 TO 31 DECEMBER 2000
($million)

	6 months ended 31 Dec 2000	*Year ended 30 June 2000*	*Year ended 30 June 1999*	*Year ended 30 June 1998*	*Year ended 30 June 1997*	*Year ended 30 June 1996*
Operating performance						
Revenue -						
Premium revenue	785	1 243	1 185	960	914	883
Investment revenue	70	589	329	437	617	286
Other	12	23	14	19	20	3
(Expenditure) -						
Net claims paid	(695)	(1 239)	(1 056)	(955)	(895)	(727)
Movement in outstanding claims liability	(707)	(511)	(433)	(385)	(540)	(340)
Other	(116)	(232)	(215)	(199)	(167)	(122)
Operating (loss)	**(651)**	**(127)**	**(176)**	**(123)**	**(51)**	**(17)**
Financial position						
Outstanding claims liability *(a)*	5 541	4 834	4 323	3 890	3 505	2 965
Net assets	4 467	4 411	4 027	3 771	3 509	3 020
Surplus/(deficiency)	(1 074)	(423)	(296)	(119)	4	55
Funding level (per cent) *(b)*	**80.6**	**91.2**	**93.2**	**96.9**	**100.1**	**101.9**
Average premium rate (per cent) *(c)*	*(d)* **2.2**	**1.9**	**1.9**	**1.8**	**1.8**	*(e)* **1.8**

(a) Represents net present value of estimated future claim payments.
(b) Represents the percentage of the Scheme's net assets in relation to its outstanding claims liability.
(c) Represents the overall average premium rates charged to WorkCover insured employers expressed as a percentage of total remuneration costs of these employers.
(d) Proposed premium rate for the 2000-01 financial year.
(e) Ten per cent surcharge removed from 1996-97 financial year.
Source: Authority's annual audited financial statements and unaudited management accounts for the 6 months to 31 December 2000.

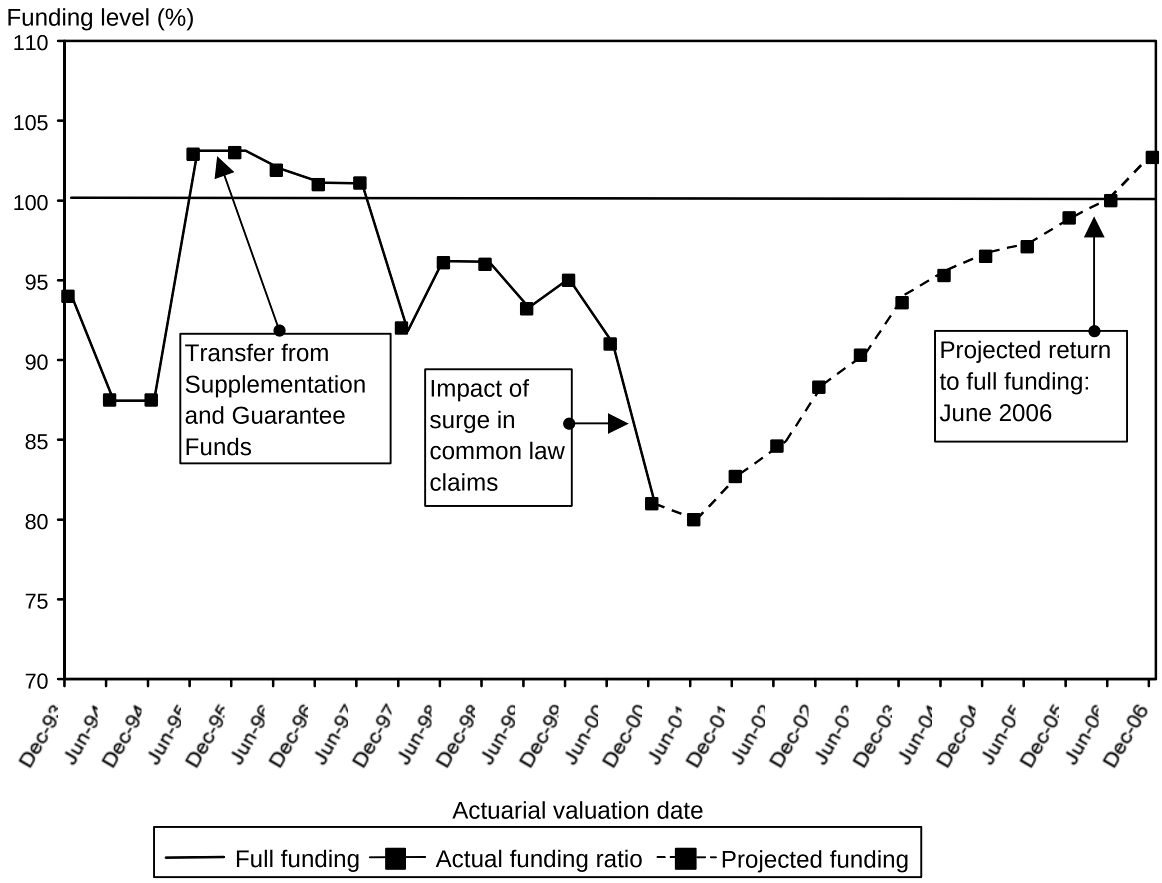
3.8.16 **The increase in the operating loss for the 6 months to 31 December 2000 has arisen due mainly to significant increases in the level of claims, the substantial reduction in investment revenue earned by the WorkCover Authority over the 6-month period, and changes in economic assumptions used in the valuation of the outstanding claims liability including allowance for the impact of the goods and services tax (GST).**

3.8.17 The most significant development impacting on the December 2000 actuarial assessment of the outstanding claims liability has been the enactment, in May 2000, of the *Accident Compensation (Common Law and Benefits)* Act 2000 which introduced revised common law remedies to employees from October 1999. The Act imposed a 1 September 2000 statutory deadline for serious injury claims incurred prior to November 1997, the date at which common law claims were previously disallowed.

3.8.18 A large number of common law applications were received by the Authority in late August 2000 following the legislative change. As at 31 December 2000, the Authority's consulting actuaries estimated that common law liabilities increased by approximately $300 million from that factored into the June 2000 financial statements as a result of this late surge in claims.

3.8.19 Chart 3.8E indicates the ratio of net assets to the outstanding claims liability over the last 7 years and the movement estimated by the Authority for the next 6 years, based on certain premium, economic and other assumptions, and assessments made by the Authority's consulting actuaries.

CHART 3.8E
ASSESSMENT BY CONSULTING ACTUARIES
OF FUNDING LEVELS FOR THE WORKCOVER FUND
FOR THE 13-YEAR PERIOD FROM DECEMBER 1993 TO DECEMBER 2006



Source: Derived from reports issued to the Authority by consulting actuaries.

3.8.20 **During the last 7 years, the Authority has operated at funding levels of less than 100 per cent with the exception of the 1995-96 and 1996-97 financial years when $320 million in surplus assets were transferred from the Supplementation and Guarantee Funds to the WorkCover Fund.**

3.8.21 **The chart also indicates that the Authority's consulting actuaries do not expect the Fund to return to a fully-funded position before 30 June 2006, 3 years later than intended when the amending legislation was enacted in May 2000.**

Key factors impacting on the financial position

3.8.22 The primary influences on the Authority's financial position include the following:

- the significant growth in outstanding claims liability for pre-November 1997 and post-October 1999 common law claims following recent legislative amendments;
- investment performance in line with market outcomes;
- higher premium revenue following an increase in the rate charged to employers; and
- initiatives to be implemented by the Authority over the next 3 years aimed at improving the Fund's financial position.

3.8.23 Each of these aspects is examined in more detail in the following paragraphs.

Significant growth in outstanding claims liability

Understanding the actuarial assessment process

3.8.24 The outstanding claims liability reported in the Authority's financial statements is based on actuarial assessments provided in accordance with actuarial and accounting professional standards.

3.8.25 With the exception of the 1998-99 financial year, 2 consulting actuaries have been engaged by the Authority to undertake an assessment of the liability each half-year, with the higher figure provided by the 2 actuaries recognised in the Authority's financial statements. Authority staff conduct rigorous checks to ensure the integrity of claims data which is relied on by the actuaries in conducting their assessments.

3.8.26 In assessing the current level of the outstanding claims liability, the actuaries take into account projected inflation rates to arrive at expected future payments, which are then discounted using a risk-free rate. Within these calculations, allowance is made by the consulting actuaries for the anticipated direct and indirect costs of settling the claims including the impact of the goods and services tax (GST).

Continuing upward trend in the outstanding claims liability

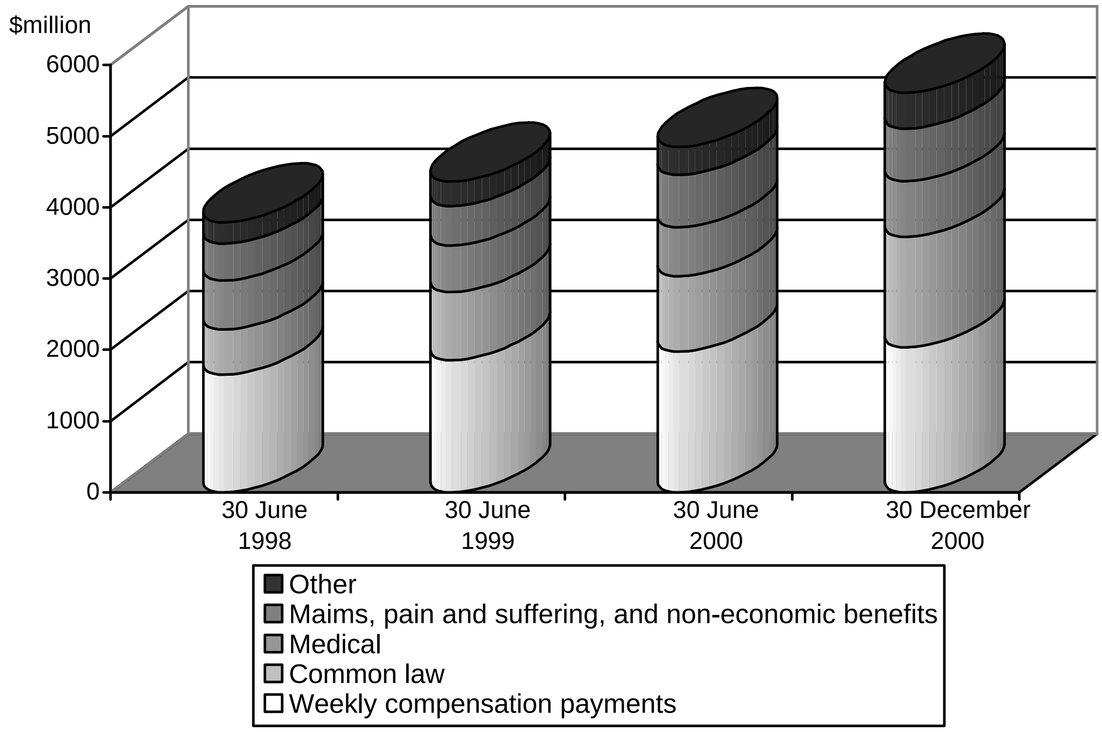
3.8.27 The outstanding claims liability for the Authority, as outlined previously in Table 3.8D, has increased from $2.9 billion at 30 June 1996 to $5.5 billion at 31 December 2000, an increase of 90 per cent over that period, and well in excess of the growth in the value of supporting assets. Of this increase, around 27 per cent or $700 million occurred during the 6-month period to 31 December 2000 as a result of the following factors:

- the late surge in August 2000 (prior to the 1 September cut-off date) for pre-November 1997 common law applications;
- re-assessment of the likely number of new (post-October 1999) common law claims;
- changes in economic assumptions, principally lower long-term discount rates and higher short-term inflationary expectations driven by the impact of the GST;

- higher allowance for claims handling expenses resulting from an increased emphasis on better case management practices; and
- offsets relating to higher recoveries and lower cost for other benefit types.

3.8.28 **Chart 3.8F highlights the substantial growth in the common law component of the outstanding claims liability, an increase of around 138 per cent from $630 million to over $1.5 billion since 30 June 1998, with the majority of the increase taking place during the 2000 calendar year.**

CHART 3.8F
COMPONENTS OF OUTSTANDING CLAIMS LIABILITIES, FOR THE PERIOD FROM 30 JUNE 1998 TO 30 JUNE 2000



Source: Reports by consulting actuaries provided to Authority for financial reporting purposes.

Impact of recent legislative amendments on the outstanding claims liability

3.8.29 Changes to the legislation in November 1997 removed the legal right for seriously injured workers to common law damages in respect of work-related injuries that occurred on or after 12 November 1997. The *Accident Compensation (Common Law and Benefits) Act* 2000 enacted in May 2000, provides for the following:

- restoration of common law rights whereby workers will be able to access common law damages if they satisfy a "Serious Injury Test";
- the establishment of an intensive case review program which makes provision for workers injured between 12 November 1997 (when common law was abolished) and 20 October 1999 (when it was restored); and

- improvements to the level of both the statutory lump sum benefits and weekly payments.

3.8.30 The absence of common law claims experience in light of the latter legislative amendments in May 2000 does not currently permit the consulting actuary to accurately assess the value of the related outstanding claims. In assessing the impact of the legislative amendments, reliance was placed by the actuaries on the deliberations of a government working party in early 2000, which provided recommendations on the manner in which restoration should proceed.

Investment performance

3.8.31 For the 5 year period to 30 June 2000, the value of investments held by the Authority had increased from around $2.7 billion at 30 June 1995 to almost $4.3 billion at 30 June 2000, an increase of around 59 per cent over that period.

3.8.32 **As at 30 June 1996, the level of investments held by the Authority was in line with the outstanding claims liability, however, since then, there has been a widening shortfall between the value of investments and the outstanding claims liability. The rise in investment values has not matched the increase that has taken place in the outstanding claims liability over the same period.**

3.8.33 Over the 5 year period to 30 June 2000, the Authority generated an overall rate of return of 13.5 per cent per annum, well above its target objective to exceed average weekly earnings of around 3 to 4 per cent per annum for that period. The returns achieved were high and were in line with market conditions. However, with the recent equity market downturn, only $69.7 million in revenue was generated for the 6-month period to 31 December 2000, well below the $302.8 million earned in the comparable 6-month period in the prior year.

3.8.34 An important influence of the financial standing of the WorkCover Authority is the considerable level of unrealised gains included in investments held by the Authority, which can be substantially impacted by reversals in equity market conditions. **The Authority will need to continue its efforts to optimise the returns from its investments especially when taking into account the level of funds required by the Authority to meet future claims.**

Higher premiums declared to return WorkCover Fund to full funding

Increased premium rates for the 2000-2001 financial year

3.8.35 The Authority establishes the premium rate on the basis of actuarial advice taking account of the costs of the WorkCover Fund. This process primarily involves the assessment of the industry/employer claims experience. The average premium rate of 2.22 per cent for the 2000-01 financial year, before adding the goods and services tax (GST), represented a 17 per cent increase, on average, in the rate charged in the previous year.

3.8.36 The significant increase in the average premium rate took into account the recommendations of an actuarial report commissioned by the government and released in February 2000 titled *Actuarial Costing of Options for the Working Party on Restoration of Access to Common Law Damages.* The working party also considered the assessments made by the Authority's consulting actuaries, including their calculations of the expected ongoing annual costs of managing the WorkCover Fund.

3.8.37 The key factor contributing to the 2000-01 rate increase was the return to common law and associated changes to benefits. The increased average premium rate was aimed at returning the WorkCover Fund to full funding within a 3 year period, namely, by 30 June 2003, with a safety margin to provide for unforeseen costs. The Authority expects that $1.525 billion in premium revenues will be generated following the setting of the new premium rates (for 1999-2000, $1.243 billion).

3.8.38 **In reporting the outcomes of their examination at 31 December 2000, both consulting actuaries found that the current assessed cost for the WorkCover Fund continued to be less than the average premium rate and that the margin (i.e. the difference between the average premium rate and the current assessed cost) would result in the Authority returning to full funding by around 30 June 2006.**

Inquiry by Economic Development Committee into 2000-01 premium levels

3.8.39 The reaction by employers to significant premium rate increases led to the Legislative Council of the Victorian Parliament's request on 6 September 2000 for the Economic Development Committee to inquire into WorkCover premiums for the 2000-01 financial year. The Committee produced an interim report in November 2000 which outlined the inquiry process and referred to the briefings obtained and the submissions received, with public hearings scheduled for late November 2000. The final report is expected to be tabled in the Parliament in the Autumn 2001 session.

3.8.40 The Authority prepared a submission to the Committee regarding the manner in which the Authority developed the 2000-01 premium rates and included a number of examples to explain why increases greater than expected may have arisen. It appears that a number of factors contributed to instances of increases greater than the 17 per cent expected by many employers, including:

- changes in the cost of workplace accidents (claim rates), which particularly affect premiums for large employers;
- increases in remuneration which leads to higher premiums for a given premium rate (premium rate times remuneration equates with premium payable); and
- changes in industry rates for premiums, particularly affecting small and medium-sized employers.

3.8.41 The concern of employers as to the significance of these increases and the timing of payments was acknowledged and once-off extensions of the due dates were made for payments of the annual premium amount from October to November 2000 and the initial quarterly payment from September to October 2000. The due date for the discounted annual in advance premium of 18 August as provided under the legislation was extended by one week to 25 August 2000.

3.8.42 The Authority will be undertaking a comprehensive review of its experience-rated system, which will also take into account the outcomes of the Economic Development Committee inquiry into changes needed for the determination of future premiums. The review will consider the key issues identified by the Authority in its submission to the Committee.

Comparison by Workplace Relations Ministers' Council of workers' compensation schemes within Australia and New Zealand

3.8.43 A recent and important Commonwealth Government development has been the monitoring by the Workplace Relations Ministers' Council of the performance of occupational health and safety, and workers' compensation programs in Australia and New Zealand. Reports issued by the Council provide a useful insight into the Authority's relative position within Australia in respect of average premium rates charged and funding levels.

3.8.44 Table 3.8G drawn from the Council's Second Report issued in April 2000 provides the latest official information on the Authority's comparative financial standing.

TABLE 3.8G
COMPARISON OF STANDARDISED PREMIUM RATES AND FUNDING LEVELS WITHIN AUSTRALIA, FOR THE 1997-98 AND 1998-99 FINANCIAL YEARS
(per cent)

	Premium rate		*Funding level*	
Jurisdiction	*1998-99*	*1997-98*	*1998-99*	*1997-98*
New South Wales	2.91	2.77	78.0	77.3
Victoria	1.89	1.77	91.4	96.3
Queensland	1.91	1.80	116.1	102.0
Western Australia	2.62	2.33	87.0	99.3
South Australia	2.37	2.34	90.2	83.9

Source: Workplace Relations Ministers' Council Comparative Performance Monitoring – *The Second Report into Australian & New Zealand Occupational Health & Safety and Workers' Compensation Programs*, April 2000 – drawn from Appendices B1 *(Factors Affecting Premium Rates)* and B2 (*Recognition of Liabilities).*

3.8.45 In can be seen from Table 3.8G that, as at 30 June 1999, the Authority's financial standing in terms of the key parameters of premium rate and funding level was comparable with the positions of the other major States of Australia. All States, with the exception of Queensland, have funding levels below 100 per cent and have experienced fluctuations in those levels over the 2 years covered by the Council's Report.

3.8.46 **In the subsequent 18 months since the period covered by the Council's Report, the Authority's relative position has changed significantly with the funding level at 31 December 2000 at 80.6 per cent primarily as a result of increases in common law liabilities and reduced investment returns over the last 6 months.**

The Authority's initiatives to address the deterioration in the WorkCover Fund's financial standing

3.8.47 In response to the significant downturn in the financial standing of the WorkCover Fund, and in line with the recommendations of the consulting actuaries, the Authority is currently implementing a number of initiatives under *Strategy 2000*, aimed at refocusing the Authority's business direction over the 3 years to 30 June 2003.

3.8.48 The Authority has advised that it will focus on the following key operational areas:

- Prevention, which aims at reducing the incidence of work-related injuries, illness and death. This initiative will target "worst" industries and employers, common injury type, work-related fatalities and major hazard facilities. The Authority will seek constructive compliance by employers based on incentive and deterrent measures; and
- Compensation and return to work, which include measures aimed at effective team-based management of common law liabilities. The Authority will give special attention to the key drivers for the successful management of these liabilities, namely, case preparation, risk assessment and consistency in management practices. In-house specialist personnel have been engaged to assist the legal firms which currently represent the Authority in these matters.

3.8.49 In their most recent assessment of the outstanding claims liability, the consulting actuaries did not give direct recognition to the possible benefits arising from the above significant Authority initiatives. However, the actuaries acknowledged the intended focus on improvements in the claims management process and increased the expense allowance for handling claims. **It is expected that future assessments by the actuaries will take account of any tangible outcomes of the *Strategy 2000* initiatives and their impact on assumptions underpinning the actuarial calculations.**

3.8.50 On the basis of their December 2000 revisions to the assessment of the outstanding claims liabilities, the actuaries believe that it will not be before June 2006 that the WorkCover Fund will be fully funded, some 3 years later than previously expected. In their December 2000 assessment of the outstanding claims liability, the actuaries identified the following key factors that would greatly impact on the final date for full funding to be achieved:

- commitment by the Authority to *Strategy 2000* initiatives which centre on an increased emphasis on accident prevention and the development of a more effective claims management process; and
- the ongoing monitoring and further analysis of impairment benefits cost and new common law settlements, for which there is minimal claims experience on which to discern trends for actuarial assessment.

3.8.51 It will be incumbent upon the Authority to maximise the potential benefits to be derived from *Strategy 2000* to effect improvements in the financial standing of the WorkCover Fund. **During the 3-year period covered by this plan, the Authority should regularly monitor its progress against the stated objectives of improved accident prevention, compensation and return to work practices.**

***RESPONSE** by the Chief Executive, Victorian WorkCover Authority*

The Victorian WorkCover Authority (VWA) generally concurs with the content of the Report which correctly attributes recent operating losses to the impact of significant increases in outstanding claims liabilities and changes in economic assumptions, including the impact of the goods and services tax (GST), and reduced investment revenue.

However, we believe that the Report fails to sufficiently emphasise the increase in outstanding claims liability which reflected the growth in pre-November 1997 common law claims.

It is further agreed that, in addition to common law and investment revenue, future performance will also be impacted by premium revenue and VWA initiatives being implemented.

RESPONSE *by the Chief Executive, Victorian WorkCover Authority - continued*

Of these factors, while it is recognised that investment and premium revenue are material issues, we believe the Report should have given greater emphasis to the "critical" financial determinants which are the increase in outstanding claims, and the VWA initiatives. An explanation of these critical factors follows:

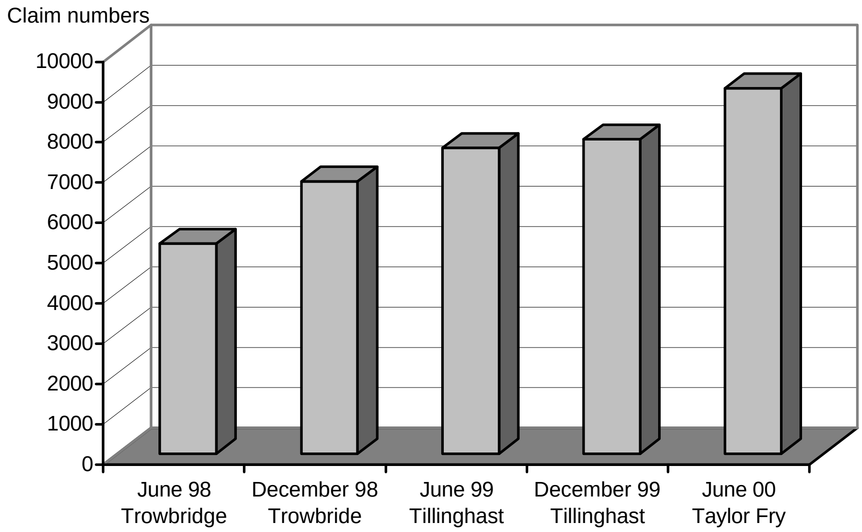
- ***Increase in outstanding claims liability***

  Over the past 3 years, liabilities relating to pre-1997 common law claims are almost double the amounts that were initially projected.

  After access to common law was removed in November 1997, claimants were given until 1 September 2000 to lodge a claim. Up until this time, valuing WorkCover's outstanding liabilities involved estimating the ultimate number of pre-1997 common law claims expected to be received.

  As WorkCover received more and more common law applications, it became clear that the ultimate number assumed in initial valuations was too low. The actuaries, therefore, began to increase this assumption, and this fuelled the rise in liabilities (refer following graph).

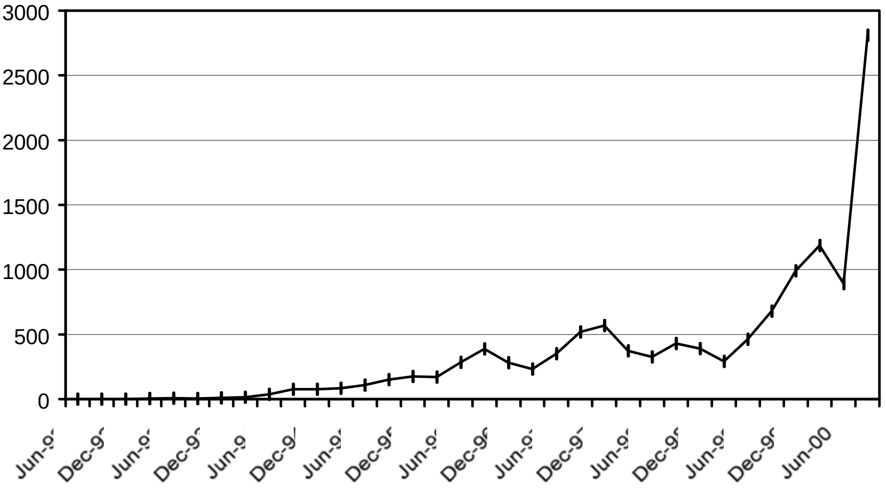
ULTIMATE NUMBER OF COMMON LAW WRITS SETTLED AT SOME COST



An extreme example of this trend occurred in August, immediately before the cut-off date, when WorkCover received nearly 2 000 more old common law applications than expected (refer following graph).

***RESPONSE** by the Chief Executive, Victorian WorkCover Authority - continued*

COMMON LAW NOTIFICATIONS



This surge caused the actuaries to increase their estimates for outstanding common law liabilities by $387 million, leading to the drop in the funding ratio.

However, now that the 1 September cut-off date has passed, the ultimate number of old common law claims is known and outstanding liabilities for these claims should be reasonably stable.

It's important to note that while liabilities for old common law claims have blown out, liabilities for other claims have remained relatively stable, despite the growing workforce.

The flow-on impact of the introduction of the goods and services tax (GST) also significantly contributed to WorkCover's liabilities. The most recent valuation revealed an additional GST liability of $190 million, to cover for greater than expected wage inflation resulting from the GST.

- ***VWA initiatives***

Key directions in our strategy include:

(a) Increase the emphasis on prevention.

Health and Safety has been clearly separated from Compensation and Rehabilitation to sharpen the focus on prevention.

On the prevention side we are focusing on 5 key areas:

1. *High-risk industries;*
2. *Poorly performing employers;*
3. *Common injury types;*
4. *Work related deaths; and*
5. *Major hazard facilities.*

***RESPONSE** by the Chief Executive, Victorian WorkCover Authority - continued*

(b) Develop more effective claims management.

We are shifting the focus from simple claims processing to more sophisticated claims management and rehabilitation encouraging co-ordinated case management by key players such as WorkCover Agents, doctors, allied health providers, and employers.

(c) Implement a new strategic management approach to common law, both old and new common law, focusing on:

Case preparation – Where early identification and preparation are vital for managing common law effectively. Accordingly, we have appointed an experienced team of in-house senior legal counsel to assist with case preparation and litigation policy;

Strategic thinking - Our approach will focus on identifying and managing those cases that have the greatest potential to impact on the system's financial viability. We are improving our liaison with stakeholders, including plaintiff solicitors and the courts, as well as our knowledge and use of databases, to enable better prediction, recording, and monitoring of high-risk claims; and

Consistency – We are also developing comprehensive legal kits and peer review training to ensure a consistent approach and the delivery of benefits to seriously injured workers at the earliest opportunity.

(d) Revitalising the VWA to maximise its capabilities

The VWA has undergone an organisation restructure, has made appointments to improve management and skills, and is reviewing all work processes to ensure alignment to our strategic objectives.

All these initiatives have the potential to significantly reduce the VWA's claim liabilities and improve the financial position.

In respect to other aspects of the Report, I wish to highlight that although investment revenue was reduced during the first half of 2000-01, this was consistent with market conditions and I can confirm the Authority will continue its present investment approach and efforts in optimising returns which has generated an overall return of 13.5 per cent over the last 5 years, notwithstanding market volatility.

I would like to conclude by emphasising that the WorkCover system remains well provisioned and our funds are more than sufficient to meet all claim payments in the foreseeable future. At the present premium level, our actuaries project that the system will become fully-funded over the next 5 to 6 years, an outcome which will improve further when the aforementioned initiatives begin to impact.

MOTOR VEHICLE FLEET MANAGEMENT BY DEPARTMENT OF TREASURY AND FINANCE

3.8.52 The Government, through agencies, operates a motor vehicle fleet of around 8 500 passenger and light commercial vehicles.

3.8.53 The vehicle fleet's financing and management arrangements are set out in a lease agreement entered into with the Commonwealth Bank of Australia (CBA) in July 1997. The agreement allows for fleet management services to be provided by either private sector providers or government agencies.

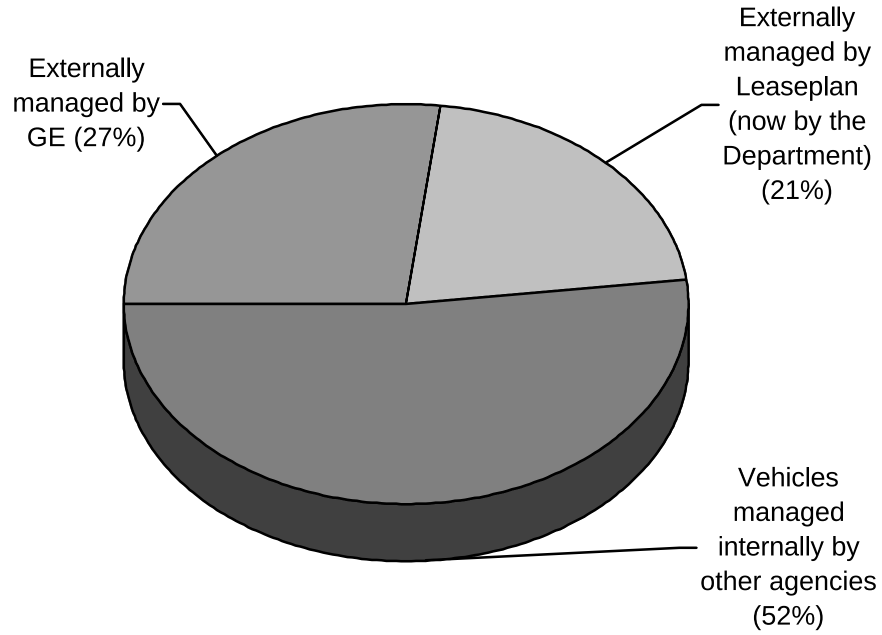
3.8.54 As indicated in our October 1997 *Report on the Government's Annual Financial Statement, 1996-97,* a panel of private sector providers, comprising LeasePlan Australia Ltd. (LeasePlan), Orix Australia Corporation Limited and DAS Fleet, was appointed in June 1997 to provide services to agencies with the Department of Treasury and Finance maintaining overall responsibility for managing the external contracts. GE Capital Fleet Services (GE) was subsequently added to the panel. Of the approved private sector providers, only LeasePlan and GE were successful in winning contracts from agencies.

3.8.55 The external fleet managers were contracted to provide services to enhance agencies' asset management activities and assist in minimising overall leasing costs. The fleet management services included:

- purchase of new and replacement vehicles and liaison with the financier;
- administration of vehicle registration and insurance;
- collection and reporting of asset management and vehicle operating data;
- co-ordination of servicing, maintenance and repair of vehicles; and
- disposal of vehicles through auction houses.

3.8.56 Chart 3.8H shows the proportion of the budget sector fleet managed by external and internal providers as at May 2000.

CHART 3.8H
BUDGET SECTOR MOTOR VEHICLE FLEET, MAY 200



Assumption of fleet management services by the Department of Treasury and Finance

3.8.57 LeasePlan's contract expired in May 2000. LeasePlan's offer to renew the contract at a revised fee was declined by the Department. As a consequence, the Department assumed responsibility for providing fleet management services to those agencies previously contracted to LeasePlan. These services covered 1 790 vehicles or 21 per cent of the budget sector fleet.

3.8.58 **At the time of assuming responsibility for providing fleet management services, the Department had not developed a business case in support of the activity. In particular, the Department had not:**

- **evaluated whether the services could be effectively managed by another private provider or, alternatively, by a budget sector agency;**
- **quantified the costs and benefits associated with assuming fleet management responsibilities; or**
- **developed suitable systems and procedures to provide effective fleet management services.**

Implementation of fleet management system

3.8.59 After assuming the fleet management responsibilities, the Department set about formalising its arrangements with client agencies. As part of this process, the Department submitted proposals to client agencies that set out proposed fees and service level details. This was aimed at providing client agencies with an opportunity to compare service delivery with that of other prospective providers. The proposals were based on the Department maintaining appropriate records regarding the vehicle fleet using a computerised fleet management system known as *Figtree*, which was to be acquired.

3.8.60 At the time of preparing the proposals that set out proposed fees and service level details, the Department had not undertaken a comprehensive costing of its proposed fleet management services, covering both system development and staffing costs. In particular, the Department had not fully costed the modifications that were necessary to the computerised system to be acquired and the supporting systems that were to be integrated, or established firm timeframes in which the system was to be fully implemented. **Therefore, the Department was not in a position to accurately determine the profitability of providing fleet management services to the client agencies at the time service arrangements were entered into.**

3.8.61 At the date of preparation of this Report, the computerised fleet management system had been acquired but was not operational. System modifications were yet to be completed and data conversion tasks remained outstanding. Since assuming fleet management responsibilities, the Department has had to rely on various in-house systems, primarily developed to facilitate management of the CBA financing arrangement, and information from external sources to provide a minimum level of service to client agencies. The Department expects new agencies to have on-line access to the new system after 30 June 2001.

3.8.62 **The Department could not readily identify the costs to date of implementing the new system. In addition, it had not determined the ongoing costs associated with providing fleet management services and, therefore, was not in a position to determine whether it should continue to provide such services in the future.**

RESPONSE *provided by Deputy Secretary, Department of Treasury and Finance*

At the time, in May 2000, the Department of Treasury and Finance considered that the preparation of a business case for assuming fleet management responsibility was neither necessary nor viable. The existing commercial provider, LeasePlan, withdrew from commercial negotiations at short notice. The Department was aware of client agency concerns at the time with the services provided by both LeasePlan and the only other appointed provider with experience in the CBA lease facility, GE Capital Fleet Services.

At the same time, those agencies managing their own vehicles in-house were satisfied with their operating systems and the provision of services to their internal agency clients. Following unsuccessful negotiations to establish a reasonable price structure with both LeasePlan and GE, the Department considered there was no practical alternative but to establish a new in-house operation.

The Department notes audit's comment that a business case analysis should have been carried out. Some analysis of business case options, say 6 months prior to expiry, may have assisted with management of various contract scenarios. However, in the practical situation of an unexpected, sudden termination of negotiations, the Department had no choice but to immediately establish an in-house fleet management operation.

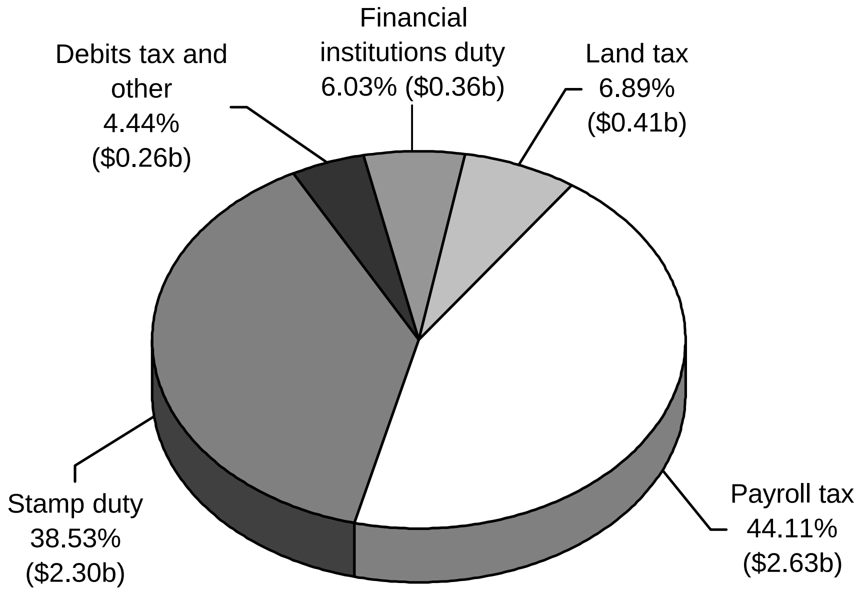
The Department accepts the thrust of audit's comments on the need for improved fleet management costing. The Department is concerned that its charges for fleet management services should cover all costs, including all relevant operating overheads and departmental management overheads. To this end, the Department is currently seeking professional assistance in establishing a pricing model which reflects all costs, while at the same time is competitively neutral in relation to private sector providers. The costs of implementing new fleet management computer systems will be incorporated in the pricing model. Client response to services based on the new price regime will then determine whether the in-house fleet management business can be effectively delivered on a full cost recovery basis.

The Department also intends to commission a review of the costs and benefits of future strategic options for the financing of motor vehicles, e.g. re-negotiation of existing lease facility, replacement lease arrangements, return to government ownership. These strategic options for financing the fleet may also hold implications for optimal fleet management arrangements in the future.

STATE REVENUE OFFICE INFORMATION TECHNOLOGY SYSTEMS

3.8.63 The State Revenue Office (SRO) was established in 1992 to have primary responsibility for the collection of the State's taxes, duties and levies. In meeting this responsibility, the SRO currently collects in excess of $5.9 billion annually, as outlined in Chart 3.8I, which represents around 27 per cent of the total annual revenue of the State.

CHART 3.8I
TAXES, LEVIES AND DUTIES COLLECTED BY THE STATE REVENUE OFFICE, 1999-2000
($billion)



3.8.64 Given its significance to the State, it is vital that the SRO's revenue collection activities are supported by effective management and control systems. In this respect, the SRO has continued to rely largely on 3 software systems originally implemented in the late 1980s and early 1990s, the Corporate Data System (CDS), the Generic Revenue Collection System (GRCS) and the One Stop Shop system. While these systems have served the SRO well over the last decade, a risk exists that these systems may not be adequate to meet future requirements, particularly given the technological developments that have occurred since their initial implementation and proposed changes to the tax system.

Strategic planning to upgrade SRO management information systems

3.8.65 Over the last decade, the SRO has taken a number of actions to ensure its information technology (IT) systems are appropriate to its future operations.

3.8.66 In 1993, the SRO completed an IT strategy, covering the period 1993 to 1997, which defined future requirements for IT standards, processes and systems.

3.8.67 Early in 1998, the SRO approved a new IT Strategic Plan (ITSP) for the years 1997 to 2000. This plan took into account technological advances since the 1993 strategies and established a program for migration from existing systems to new systems capable of meeting the SRO's future needs. As part of the plan, the SRO envisaged that by 2001 a new integrated system would be implemented to replace the existing corporate data and revenue collection systems. It was intended that this new system would also be capable of interfacing with other relevant systems used in both the Victorian and Commonwealth Government sectors.

3.8.68 The revised IT strategic plan outlined certain business outcomes sought by the SRO, namely:

- *"To support the Whole of Government strategy for all Government agencies to be on line by the year 2001.*
- *To support the SRO's business strategy to offer a wide range of compliance options to its customers, ensuring that compliance is simpler and therefore less costly to the consumer.*
- *To ensure that IT systems are flexible to changes in the Tax system.*
- *To minimise the risk and exposure of legacy systems through increasing shortage of skills.*
- *To reduce the overall costs to the business by use of more effective technology and to reduce overall IT costs."*

3.8.69 Around the same time as the finalisation of this strategic plan, a submission by the SRO to the Government's Budget and Economic Review Committee outlined its proposals for the development of new IT systems at an estimated cost of around $30.4 million.

3.8.70 In March 1998, the Government approved total funding for IT developments by the SRO of $27.4 million, comprising:

- $22.4 million to replace core revenue management systems; and
- $5 million to develop systems for electronic service delivery.

3.8.71 The Government expected the $3 million difference between the funds sought and approved would be funded internally by the SRO.

3.8.72 In September 1998, the SRO commissioned Tier Technologies to provide advice on the possibility of "reverse engineering" its existing revenue collection system, which involved using certain aspects of the current system's architecture, programming code and documentation to develop a replacement system. At the same time, the SRO sent an evaluation team to Western Australia to evaluate whether that State's newly installed Revenue Collection Information System (RCIS) would suit its requirements.

3.8.73 Following these actions, the SRO's Information Technology Division reported in November 1998 on the preferred architectural direction of the new system. In forming its opinion, the Division considered a number of options, namely:

- Option 1- Reverse engineering the GRCS and SRO systems;

- Option 2 - Extending and tailoring the Western Australian RCIS using Oracle developer;
- Option 3A- Developing new core systems using RCIS as a basis – piloting using the Java programming language;
- Option 3B- Developing new core systems using components of existing SRO systems- piloting using Java; or
- Option 3C- Developing new core systems using components of existing SRO systems, RCIS and commercial components (mix and match option) – piloting using Java.

3.8.74 The Division concluded that option 3C, an internally developed system capable of supporting e-business functionality, with future enhancements, would best meet the business requirements of SRO.

3.8.75 Implementation of the recommended option would involve both the development of software and the purchase and installation of new hardware appropriate for the operation of these systems. The project would require substantial involvement of SRO staff working in conjunction with a prime contractor appointed to manage certain aspects of the development and implementation phases.

Appointment of contractor

3.8.76 To assist in the project development, 43 companies were approached in early 1998 to express interest in providing consultancy and other services in relation to the development of core system replacement, e-business, telecommunication development and upgrade of the IT infrastructure. Of the 5 companies that subsequently responded, 3 were short-listed and provided with the detailed plans and associated timing for the development of the new IT system. Proposals by the 3 short-listed companies were subsequently evaluated against 6 general criteria, which centred on experience in the industry, general approach to the project, timing and the quality of staff.

3.8.77 In January 1999, the SRO's evaluation team recommended the appointment of Fujitsu as the prime contractor and development director for the project based mainly on their expertise and experience in the field. A contract, subsequently signed by SRO and Fujitsu in May 1999, required Fujitsu to undertake ongoing consultancy and management services, detailed system development and to purchase and install certain system hardware. Under the terms of the contract, Fujitsu was required to provide these services in compliance with dates specified in the implementation plan, which in effect required completion of the project by 30 June 2001.

3.8.78 The contract did not incorporate an overall fixed price for the services to be provided by Fujitsu but rather a set of estimates to be fixed during the life of the project. The contractor was required to notify the SRO of proposed charges on a progressive basis at least 2 months before commencement of each stage of the project. Under the terms of the contract, these price estimates were to be subject to review and written approval by the SRO within 14 days of notification and, once agreed, were fixed for each stage. Fujitsu estimated the total cost of services to be provided under these arrangements at around $14.6 million.

3.8.79 The lack of an overall fixed price for services created a risk that, in the event of significant delays or problems associated with project implementation, charges by the contractor on subsequent stages may exceed the initial cost estimates developed by the SRO.

3.8.80 To date, this risk has not eventuated due mainly to the approval processes for contractor estimates instigated by the SRO. At the date of preparation of this Report, payments to the contractor have totalled $11.3 million with the SRO forecasting that total payments for development will be $15.9 million by completion of the project, 9 per cent above the original estimate of $14.6 million. This increase is mainly attributable to delays in implementation of the project compared with original timeframes as referred to in subsequent paragraphs of this Report.

Changes in the scope and timing of system implementation

3.8.81 In December 1998, a paper was submitted to the SRO executive management recommending that the SRO proceed to pilot an on-line revenue system for completion by June 1999 using a combination of workflow modules, existing systems and commercial components with the pilot using the Java programming language.

3.8.82 During the second quarter of 1999, the SRO and Fujitsu formulated a project agreement, which outlined that the entire new system would be implemented by 30 June 2001 with the associated aim of ceasing use of existing systems and hardware at the same time. The plan divided the project into 5 release stages consisting of project initiation, planning, project development, implementation and completion.

3.8.83 The initial implementation schedule included a phased release strategy and indicative release dates as outlined in Table 3.8J.

TABLE 3.8J
INITIAL IMPLEMENTATION SCHEDULE

Phase	*Indicative release date*
Project initiation, proof of concept and insurance duty	November 1999
Motor car stamp duty	January 2000
Remaining stamps return	June 2000
Payroll tax	August 2000
Land tax and land information	February 2001
One Stop Shop and miscellaneous	June 2001

3.8.84 Since the initial stages of the project, substantial changes have been made to the development strategy and the implementation schedule emanating mainly from a decision by the SRO in October 1999 to move to an Oracle-based approach due to:

- an assessment in August 1999 of the results of a pilot project to confirm that the technology and options previously proposed using the Java programming language remained the most suitable approach for the implementation of new systems;
- concerns that the required Java development software, to be purchased from an overseas vendor, may not be available in time to meet the required deadlines; and

- a conclusion by independent consultants, in October 1999, that the best approach would be to extend and tailor the Western Australian revenue system using an Oracle-based approach in preference to the Java-based option on the basis that:
  - the revised approach would be more practicable given the stringent time and budgetary constraints;
  - there was a lower risk associated with use of the established Oracle development technology compared with the newer, and still under development, Java approach; and
  - Fujitsu had greater experience in dealing with Oracle-based developments.

3.8.85 The changed approach to system development created pressures for the SRO to meet its previously established timeframes, which resulted in decisions to:

- change from a staged release strategy to a merged release strategy to enable major aspects of the development, including payroll tax, land information and land tax components, to still be achieved by the time target of 30 June 2001;
- defer finalisation of certain other components of the system which are now to be implemented as part of system enhancements to be completed in August and December 2001 rather than by the initial 30 June deadline; and
- change the testing program for the new systems whereby the systems integration and acceptance testing phases, usually conducted sequentially, would now be undertaken concurrently.

3.8.86 A major implication of the decision to concurrently undertake systems integration and acceptance testing was an increased likelihood of high error rates. To address this situation, the SRO implemented a stringent monitoring regime of the testing program to ensure that all errors would be appropriately recorded and reported to senior management and any issues arising from these errors would be effectively addressed.

3.8.87 **At the time of our review, 48 per cent of the total systems integration and acceptance testing had been conducted on the payroll tax, land information and land tax components of the system. The number of errors identified, as predicted, has been high and the SRO continues to closely monitor the results of the testing phase of the project.**

Effectiveness of the SRO project management

3.8.88 Audit identified that formal project management arrangements had been implemented by the SRO to monitor the progress of the IT development. At the project's inception an *e-sys steering committee* was formed and it has met on a monthly basis. The committee is now meeting on a fortnightly basis to review status reports and action and risk registers. The *e-sys steering committee* is responsible for reporting on project progress, and for referring major decisions to SRO executive management. Project management has been further enhanced through the engagement of internal audit to conduct quarterly project reviews along with a range of more detailed assessment of specific technical and other aspects of the project. In addition, a formal contingency plan has been put in place to address any matters that may impact on the operations of the SRO should current implementation deadlines not be achieved.

3.8.89 **The SRO has established comprehensive project management procedures and has progressively strengthened these procedures to address emerging issues resulting from changes to the initial scope and implementation milestones of the project. The importance of maintaining effective management processes will assume even greater importance as the project enters its final critical phases to meet implementation deadlines.**

Cost implications of changes to implementation deadlines

3.8.90 As referred to above, the SRO envisages that the entire system will now be fully implemented by December 2001, 6 months later than the original proposal. However, at the date of preparation of this Report the SRO was still working towards a 30 June 2001 first release which would include the payroll tax, land information and land tax components of the system. A further upgrade of those systems is expected in August 2001, which will include some of the initial proposed functionality of the systems that were deferred. Release 2, scheduled for December 2001, will include the Stamp Duties Return module.

3.8.91 The later release of certain system modules will mean that the prime contractor will continue to be engaged for a number of months after June 2001. In accordance with the terms of the arrangement with the contractor, a monthly management fee of $110 000 is payable for each month for which they are engaged.

3.8.92 **At 31 January 2001, the SRO had spent $19.9 million on the project and advised that it estimates total direct costs associated with the project will amount to $30.2 million, compared with the initial cost estimate of $30.4 million.**

3.8.93 This current cost estimate may increase should existing systems and mainframe hardware be required to be operated past 30 June 2001 as a result of delays in meeting revised implementation dates for the new systems. **The SRO has estimated that additional costs associated with operating the mainframe after 30 June would amount to around $50 000 per week.**

Issues concerning use of credit card facilities

3.8.94 One of the impediments to optimising the value that should be captured with the upgrade is the inability of the SRO to offer a credit card payment option. The *Financial Management Act* 1994 Direction 2.10.3.(i) states that*: "… where practicable, accountable officers must ensure that their organisation can accept revenue using credit card, debit card and other electronic media facilities"*. Currently, the SRO has an exemption from complying with the direction. It should be noted that all agencies that provide credit card payment facilities attract a merchant service fee and in the case of the SRO the fees payable, in total, would be substantial.

3.8.95 **In light of the current trends toward e-commerce and the increasing usage by consumers paying by credit card, the appropriateness of current policy exemption may require review. This review should ensure that due consideration is given to the cost implications of introducing payments by credit card and any associated impact this may have on the revenue of the State.**

Conclusion

3.8.96 Over the past 3 years, the SRO has embarked on a comprehensive IT development project involving the key revenue systems of the State of Victoria. While changes have occurred over this time in the scope and timing of the project, these have been largely managed without significant impact to date on either the ultimate completion of key phases or the cost of the project.

3.8.97 **The project is currently in the critical phases of testing and final implementation. The progress made in these final phases and the extent of any significant issues encountered at this stage will ultimately determine the success of the SRO in implementing effective revenue collection systems in line with the stringent timeframes established for the project. Any delays may also impact on both the direct costs of the project and the extent of internal resources utilised by the SRO on the project.**

3.8.98 **Given the importance to the State of these new systems, it will also be of key importance for audit to continue to monitor and report on the progress and ultimate results of the development project.**

***RESPONSE** provided by Commissioner of State Revenue*

At the time of the audit in March of this year, it was anticipated that Release 1 of the project would be completed by 28 June 2001. This date has now slipped to 16 August 2001, a delay of 7 weeks from our projection at the time.

SCHEDULE A
STATUS OF MATTERS RAISED IN PREVIOUS REPORTS

Report	*Subject*	*Status at date of preparation of this Report*
	MATTERS RESOLVED OR ACTION COMMENCED	
VICTORIAN WORKCOVER AUTHORITY		
Ministerial Portfolios, June 2000, pp. 316-20	The WorkCover scheme's continued funding deficiency has been mainly due to the growth in the level of the outstanding claims liability without a matching or improving increase in available net assets.	Further comment in relation to the status of this matter is included in this Part of the Report.
DEPARTMENT OF TREASURY AND FINANCE		
Ministerial Portfolios, May 1996, p. 335.	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 in annual reports to the Parliament.	Consistent with the recommendations of the "Review of Government Purchasing Arrangements" undertaken in 1999-2000 on behalf of the Minister for Finance which is currently being considered by the Government, the Department is examining options to resolve the issues associated with the classification of consultants and contractors.

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS			
FINANCIAL YEAR ENDED 30 JUNE 2000			
Department of Treasury and Finance	19 Oct. 2000	23 Oct. 2000	✓
FINANCE			
Emergency Services Superannuation Scheme	15 Sept. 2000	19 Sept. 2000	✓
Government Superannuation Office	18 Oct. 2000	20 Oct. 2000	✓
Parliamentary Contributory Superannuation Fund	4 Oct. 2000	6 Oct. 2000	✓
Regulator-General, Office of the	29 Sept. 2000	29 Sept. 2000	✓
State Superannuation Fund	18 Oct. 2000	20 Oct. 2000	✓
Victorian Managed Insurance Authority	6 Sept. 2000	11 Sept. 2000	✓
GAMING			
Tattersall's Club Keno Pty Ltd	30 Oct. 2000	31 Oct. 2000	✓
Tattersall’s Gaming Pty Ltd	30 Oct. 2000	31 Oct. 2000	✓
Tattersall’s Sweeps Pty Ltd	30 Oct. 2000	31 Oct. 2000	✓
Victorian Casino and Gaming Authority	29 Aug. 2000	31 Aug. 2000	✓
Chief Electrical Inspector, Office of	18 Aug. 2000	30 Aug. 2000	✓
Gas Release Co. Pty Ltd	31 Aug. 2000	20 Sept. 2000	✓
Gas Safety, Office of	29 Aug. 2000	30 Aug. 2000	✓
Gas Transmission Corporation	23 Aug. 2000	25 Aug. 2000	✓
Gascor Holdings No. 1 Pty Ltd *(a)*	23 Aug. 2000	24 Aug. 2000	✓
Gascor Holdings No. 2 Pty Ltd *(a)*	23 Aug. 2000	24 Aug. 2000	✓
Gascor Holdings No. 3 Pty Ltd *(a)*	23 Aug. 2000	24 Aug. 2000	✓
TREASURER			
Gascor EPL Pty Ltd *(a)*	23 Aug. 2000	24 Aug. 2000	✓
Gascor IEPL Pty Ltd *(a)*	23 Aug. 2000	24 Aug. 2000	✓
Gascor KEPL Pty Ltd *(a)*	23 Aug. 2000	24 Aug. 2000	✓
Gascor MAPL Pty Ltd *(a)*	23 Aug. 2000	24 Aug. 2000	✓
Gascor MGPL Pty Ltd *(a)*	23 Aug. 2000	24 Aug. 2000	✓
Gascor Pty Ltd	21 Sept. 2000	21 Sept. 2000	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS – *continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS - *continued*			
FINANCIAL YEAR ENDED 30 JUNE 2000 – *continued*			
TREASURER – *continued*			
Gascor SAPL Pty Ltd *(a)*	23 Aug. 2000	24 Aug. 2000	✓
Gascor SNPL Pty Ltd *(a)*	23 Aug. 2000	24 Aug. 2000	✓
Gascor (T No.1) Pty Ltd *(a)*	23 Aug. 2000	24 Aug. 2000	✓
Gascor (TH) Pty Ltd *(a)*	23 Aug. 2000	24 Aug. 2000	✓
Gascor WAPL Pty Ltd *(a)*	23 Aug. 2000	24 Aug. 2000	✓
Gascor WPL Pty Ltd *(a)*	23 Aug. 2000	24 Aug. 2000	✓
Gas services business Pty Ltd *(b)*	23 Aug. 2000	28 Aug. 2000	✓
Land Aggregation Program Trust Fund	2 Aug. 2000	2 Aug. 2000	✓
Opalwood Pty Ltd	2 Aug. 2000	7 Aug. 2000	✓
Rural Finance Corporation	2 Aug. 2000	2 Aug. 2000	✓
Southgate Trust	2 Aug. 2000	7 Aug. 2000	✓
State Electricity Commission of Victoria	20 Sept. 2000	21 Sept. 2000	✓
State Trustees Limited	29 Sept. 2000	16 Oct. 2000	✓
State Trustees Common Fund No. 1	20 Sept. 2000	2 Oct. 2000	✓
State Trustees Common Fund No. 2	20 Sept. 2000	2 Oct. 2000	✓
State Trustees Common Fund No. 3	20 Sept. 2000	2 Oct. 2000	✓
State Trustees Common Fund No. 4	20 Sept. 2000	2 Oct. 2000	✓
State Trustees Common Fund No. 5	20 Sept. 2000	2 Oct. 2000	✓
State Trustees Common Fund No. 6	20 Sept. 2000	2 Oct. 2000	✓
State Trustees Common Fund No. 10	20 Sept. 2000	2 Oct. 2000	✓
STL Financial Services Limited	13 Oct. 2000	16 Oct. 2000	✓
TAC Law Pty Ltd	8 Aug. 2000	17 Aug. 2000	✓
Transport Accident Commission	25 Aug. 2000	25 Aug. 2000	✓
Treasury Corporation of Victoria	1 Sept.2000	11 Sept. 2000	✓
Vicfleet Pty Ltd	13 Nov. 2000	14 Nov. 2000	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS - *continued*			
FINANCIAL YEAR ENDED 30 JUNE 2000 – *continued*			
TREASURER - *continued*			
Victorian Energy Networks Corporation	18 Sept. 2000	18 Sept. 2000	✓
Victorian Funds Management Corporation	7 Sept. 2000	7 Sept. 2000	✓
Victorian Power Exchange Pty Ltd	13. Sept. 2000	18 Sept. 2000	✓
VFM Australian Equities Trust	31 Aug. 2000	7 Sept. 2000	✓
VFM Australian Fixed Interest Trust	31 Aug. 2000	7 Sept. 2000	✓
VFM Indexed Bonds Trust	31 Aug. 2000	7 Sept. 2000	✓
VFM International Equities Trust	31 Aug. 2000	7 Sept. 2000	✓
VFM Short Term Money Market Trust	31 Aug. 2000	7 Sept. 2000	✓
V/Line Passenger Corporation	4 Oct. 2000	20 Oct. 2000	✓
WORKCOVER			
Victorian WorkCover Authority	25 Sept. 2000	19 Sept. 2000	✓

Report contained an emphasis of matter comment **-** Due to the proximity of a statutory deadline to lodge certain serious injury claims incurred prior to November 1997 to the date of finalisation of the Authority's accounts, the impact of the claims on the Authority's outstanding claims liability and its net loss for the year could not be reliably determined.

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
OTHER FINANCIAL PERIODS			
TREASURER			
Arada Pty Ltd *(c)* (period 4 Jan. 1999 to 30 Sept. 2000)	22 Nov. 2000	11 Dec. 2000	✓
Arada Trust *(c)* (period 11 Aug. 1999 to 30 June 2000)	22 Nov. 2000	11 Dec. 2000	✓
Faraday Arch Pty Ltd (year ended 30 Sept. 1999)	14 Dec. 2000	14 Dec. 2000	✓
(year ended 30 Sept. 2000)	14 Dec. 2000	14 Dec. 2000	✓
Florida Banner Pty Ltd (year ended 30 Sept. 1999	14 Dec. 2000	14 Dec. 2000	✓
(year ended 30 Sept. 2000	14 Dec. 2000	14 Dec. 2000	✓
Property Leasing Limited *(c)* (year ended 30 Sept. 2000)	22 Nov. 2000	11 Dec. 2000	✓

Report contained an emphasis of matter comment – There was an inherent uncertainty relating to the valuation of certain bonds that were included as part of the liabilities of the company.

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*
COMPLETED AUDITS - *continued*			
OTHER FINANCIAL PERIODS *– continued*			
TREASURER - *continued*			
Met Train 1 (then trading as Bayside Trains) (period 1 Jul. 1999 to 29 Aug. 1999) *(d)*	31 Aug. 2000	31 Aug. 2000	✓
(period 1 Jul. 1999 to 23 Dec. 1999) *(e)*	31 Aug. 2000	31 Aug. 2000	✓
Met Train 2 (then trading as Hillside Trains) (period 1 Jul. 1999 to 29 Aug. 1999) *(d)*	31 Aug. 2000	31 Aug. 2000	✓
(period 1 Jul. 1999 to 23 Dec. 1999) *(e)*	31 Aug. 2000	31 Aug. 2000	✓
Met Tram 1 (then trading as Swanston Trams) (period 1 Jul. 1999 to 29 Aug. 1999) *(d)*	31 Aug. 2000	31 Aug. 2000	✓
(period 1 Jul. 1999 to 23 Dec. 1999) *(e)*	31 Aug. 2000	31 Aug. 2000	✓
Met Tram 2 (then trading as Yarra Trams) (period 1 Jul. 1999 to 29 Aug. 1999) *(d)*	31 Aug. 2000	31 Aug. 2000	✓
(period 1 Jul. 1999 to 23 Dec. 1999) *(e)*	31 Aug. 2000	31 Aug. 2000	✓
Securities Finance Corporation Ltd (year ended 31 Dec. 2000)	26 April 2001	26 April 2001	Qualified opinion
(Reason for qualification: Overstatement of the carrying value of loan liabilities.)			
Tricontinental Corporation Ltd (year ended 31 Dec. 2000)	26 April 2001	26 April 2001	Qualified opinion
(Reason for qualification: Overstatement of the carrying value of receivables.)			
Tricontinental Holdings Ltd (year ended 31 Dec. 2000)	26 April 2001	26 April 2001	✓
Twin Waters Resort Pty Limited (year ended 31 Dec. 2000)	26 April 2001	26 April 2001	✓
V/Line Passenger Corporation (period 1 Jul. 1999 to 29 Aug. 1999) *(d)*	4 Oct. 2000	20 Oct. 2000	✓
Victorian Trauma Foundation (period 14 Dec. 1999 to 30 June 2000)	31 Jul. 2000	14 Dec. 2000	✓
Victorian Trauma Foundation Pty Ltd (period 14 Dec. 1999 to 30 June 2000)	31 July 2000	14 Dec. 2000	✓
Western Underground Gas Storage Pty Ltd (period 26 June 1997 to 27 November 1998) *(d)*	15 May 2000	29 May 2000	✓

SCHEDULE B
COMPLETED/INCOMPLETE AUDITS - *continued*

Entity	*Financial statements signed by entity*	*Auditor-General's report signed*	*Clear opinion issued*

COMPLETED AUDITS - *continued*

OTHER FINANCIAL PERIODS – *continued*

GAMING

Gambling Research Panel (period 10 May 2000 to 30 June 2000) *(f)*	6 Oct. 2000	11 Oct. 2000	✓

INCOMPLETED AUDITS

Roslin Pty Ltd (Financial year ended 30 June 2000)	Audit substantially completed
SEMCL No. 1 Unit Trust (Financial year ended 30 June 2000)	" "
South Eastern Medical Complex Limited (Financial year ended 30 June 2000)	" "
V/Line Passenger Corporation *(e)* *(Period 1 July 2000 to 31 December 2000)*	" "

(a) These represent the "shell companies" of previous gas industry entities.

(b) Company deregistered as at 30 June 2000.

(c) Arada Pty Ltd is the trustee of the Arada Trust which in turn holds all the shares in Property Leasing Limited. The Treasurer of Victoria is the sole beneficiary of the Arada Trust.

(d) Audit requested by the Treasurer of Victoria as at the date of sale of the entity's net assets to the private sector.

(e) Final audit.

(f) Established under the *Gambling Legislation (Responsible Gambling) Act* 2000.

Part 4

Broad scope issues

Part 4

Broad scope issues

KEY FINDINGS

Performance reporting in the budget sector

- Considerable progress has been made by the Government in implementing a new performance management and reporting framework for the budget sector.

  Para. 4.1.14

- The framework is not yet sufficiently developed for audit opinions to be issued regarding the relevance, appropriateness and fair presentation of performance information. ***Para. 4.1.19***

- Requirements for departments to provide Parliament with key information contained in their corporate plans is worthy of consideration.

  Para. 4.1.30

- The output measures incorporated in the Government's Budget Papers may not be the most appropriate indicators of departmental performance.

  Para. 4.1.34

- The outcome of more detailed assessments of each department by this Office subsequent to this Report will inform decisions regarding future audit directions, including the issue of audit opinions on performance information.

  Para. 4.1.43

Outcome of IT audits in departments and selected other agencies

- Information technology (IT) security and administration could be significantly improved at the agencies subject to our review. There is a need for agencies to enhance the strategic oversight of IT development and policy, system security and back-up processes for computerised information and disaster recovery planning.

  Paras 4.2.1 to 4.2.25

Part 4.1

Performance reporting in the budget sector

Trends in performance reporting

4.1.1 In recent years, there has been increasing pressure on governments and public sector managers to provide services in more efficient and effective ways, and to be more accountable for their performance. This has been accompanied by a trend in many jurisdictions towards enhanced performance management and reporting systems, often facilitated through the introduction of legislation or central directives defining the corporate planning and reporting requirements of agencies.

4.1.2 There is increasing recognition of the need for governments and their agencies to account to Parliament and the community for results based on the full cost of outputs. This compares with the mechanisms in place for many years which focused on accounting for cash inputs and explaining variances between actual and budgeted expenses and revenues.

Developments in Victoria

4.1.3 In line with these trends there have been strong calls for improvements in performance management and annual reporting across the Victoria public sector, as reflected in successive reports of Parliament's Public Accounts and Estimates Committee. The Committee has expressed reservations about the quality of annual reporting practices in relation to meeting reader needs, the accuracy of information presented and the relevance of performance measures reported.

4.1.4 In response, there have been a number of developments in recent years aimed at achieving improved financial and performance management reporting including:

- the introduction of accrual output-based budgeting;
- the introduction of accountability requirements under the *Financial Management Act* 1994; and
- enhancements to the performance reporting framework for the budget sector.

Output-based management

4.1.5 As part of the implementation of the former Government's Management Reform Program, Victoria moved from an input to output focus with the introduction in 1998-99 of accrual, output-based budgeting. This has involved defining the services delivered to the community by departments and costing them on the basis of accrued costs rather than cash disbursements. Performance measures for each output and results achieved relating to each measure have, since that time, been included in the Government's annual budget papers.

4.1.6 A primary objective of the change was to focus on and manage the services delivered by departments and to better align resource allocation with the strategic objectives of the Government. The use of output measures was also introduced to facilitate better decision making regarding the allocation of resources and the purchase of outputs in an environment where increased competitiveness in service delivery was fostered.

Accountability requirements of agencies

4.1.7 The key accountability requirements under the *Financial Management Act* 1994, or under the Management Reform Program, have been for all departments and public bodies to:

- establish a corporate and business planning process;
- define measures relating to quantity, quality, timeliness and cost measures for various output groups, as part of the annual budget process;
- prepare audited annual financial statements and a report of operations; and
- table the financial statements and report of operations in Parliament, through their relevant Minister.

4.1.8 As indicated in Part 3.3 of this Report, a number of specific requirements have also been put in place in relation to local government bodies.

Revised budget sector framework

4.1.9 The reforms to date have not been matched by strengthened accountability arrangements which focus on measuring and reporting outcomes achieved. In particular, the output budgeting mechanisms introduced in the 1998-99 financial year have not provided a transparent link between the departmental output measures included in the budget papers and the impact on the community of the services delivered by the Government.

4.1.10 With the aim of strengthening the processes, the Government commenced this year implementing a revised performance reporting framework for the budget sector. The key elements of the framework are:

- definition by the Government of high level desired outcomes and priorities;
- establishment of operational objectives at a departmental level which are consistent with the high level outcomes;

- development of at least one indicator for each departmental objective which demonstrates the extent to which objectives are achieved; and
- establishment of links between departmental outputs, departmental objectives and government desired outcomes.

4.1.11 We understand that there is an intention to strengthen the reporting mechanisms for the non-budget sector at a later stage.

4.1.12 A number of performance audits completed by this Office have examined and reported on the quality of performance information reported by departments. The audit legislation was amended in December 1999 to provide the Auditor-General with a further discretionary mandate. The legislation specifically provides for the following:

> "*The Auditor-General may audit any report of the operations of an authority under section 45 of the Financial Management Act 1994 to determine whether any performance indicators in the report of operations:*
>
> *(a) are relevant to any stated objectives of the authority; and*
>
> *(b) are appropriate for the assessment of the authority's actual performance; and*
>
> *(c) fairly represent the authority's actual performance.*"

4.1.13 These provisions are clearly directed at providing the Auditor-General with discretion to issue audit opinions on performance information reported publicly by departments and public bodies.

Implementation to date

Establishing the framework

4.1.14 **Considerable progress has been made by the Government in implementing the new framework.** As part of the 2000-01 budget process managed by the Department of Treasury and Finance, objectives have been developed by each department and endorsed by the Government's Expenditure Review Committee. Each department has provided information to the Department of Treasury and Finance regarding performance indicators together with targets in respect of each indicator. The objectives were included in the 2001-02 budget papers along with the quantity, quality, timeliness and cost output measures similar to those included in the budget papers in recent years.

4.1.15 The Government, through the Department of Premier and Cabinet, is also in the process of formalising its high level desired outcomes and priorities. Quantifiable performance indicators and targets in relation to the outcomes and priorities are under development and the Government is considering mechanisms for publicly reporting this information and accounting to the community for achievements against these targets.

4.1.16 These developments are to be incorporated within the Government's proposed integrated management cycle to be adopted for the budget sector in the 2001-02 financial year. The cycle is aimed at integrating planning (at a whole-of-government and departmental level), resource allocation, service delivery and accountability.

Audit of performance information

4.1.17 The moves to strengthen the accountability framework within Victoria are positive in that they rightly place the prime responsibility for accounting for achievements with the Government and its agencies. While the responsibility for establishing the framework clearly rests with the Government, the legislative provisions for audit assurance of publicly reported information are important in ensuring the performance information available to the Parliament and the public is relevant, appropriate and accurate.

4.1.18 Experience in many jurisdictions has shown that it is not easy to achieve a sound regime for reporting audited performance information in the short-term. It needs to be approached in an evolutionary way and be subject to continuous improvement. Ongoing input from the Auditor-General and effective communication between departments and his Office are an essential part of this process.

4.1.19 With this in mind, we have examined the implementation of the framework to date and the principles underpinning the proposed framework. **We have formed the view that it has not yet been sufficiently developed to enable audit opinions to be issued regarding the relevance, appropriateness and fair presentation of performance indicators.** We have also identified a number of areas relating to the framework which need to be addressed, to achieve a sound public reporting regime.

4.1.20 The areas we have identified as requiring consideration for enhancement are:

- clarification of the target audience of performance information;
- public disclosure of corporate plans;
- improved content of reports of operations; and
- further clarification of the proposed evaluation framework.

Clarification of target audience

4.1.21 The measurement and reporting of performance can serve a number of purposes including:

- facilitating government or agency accountability to Parliament, the public and other stakeholders regarding the level of achievements of policy objectives;
- assisting government or agency managers in improving their performance and achieving internal accountability; and
- aiding government or funding bodies in decisions regarding the allocation of resources or the purchase of services.

4.1.22 Because of these differing purposes, the nature of performance information required and the level at which performance is reported may vary for different users. Given the potentially high cost to departments and ultimately the Victorian taxpayers of introducing a performance reporting framework, it is important that a reporting regime meets the needs of the target users, while avoiding unnecessary cost. There is also a need for clear links between the various levels of reporting to ensure they are all focused at achieving overall agency and government desired outcomes.

4.1.23 In examining the proposed framework and discussing implications with central agencies and operational departments, we observed a lack of clarity regarding the purpose and target audience of performance information to be developed by agencies as part of the new framework.

4.1.24 The work being undertaken within the Department of Premier and Cabinet to define high level government desired outcomes and performance indicators is clearly focused on accounting to the public for the level of achievement of the Government's policy objectives. However, this is not linked to the resource allocation framework which primarily connects resources to departmental outputs.

4.1.25 At a departmental level, considerable time has been spent in developing output measures to be included in the budget papers and reporting quarterly to the Department of Treasury and Finance on results against each measure. Discussions with a number of departments indicated that this information was seen by them as primarily meeting the needs of the Department of Treasury and Finance and did not necessarily serve the public accountability requirements or link to information utilised for management decision-making. Separate information and reporting processes were often in place for this purpose which departments considered better reflected the nature of their business and customers, and was more clearly linked to their corporate planning processes.

4.1.26 In progressing the implementation of the framework, there is a need to ensure the users of various information are more clearly defined and that linkages between information for various purposes are strengthened. Particular attention needs to be given to ensuring departmental objectives and indicators developed as part of the budget process are closely aligned with the Government's high level objectives and indicators currently under development. The linkages and the need for sound public accountability should be reinforced within the proposed integrated management cycle.

Public disclosure of key corporate planning information

4.1.27 A sound framework for publicly reporting performance should comprise a complete cycle involving initial public disclosure of objectives and targets, periodic measurement of achievements and public reporting of results.

4.1.28 Corporate and business planning processes of individual departments are key components of this cycle. They are important in signalling the future intentions of departments in terms of their objectives, targets and strategies. They also provide direction for service delivery and form a basis against which to report achievements.

4.1.29 Departments are required to establish corporate and business planning processes and this is to be reinforced within the proposed integrated management cycle. However, there is currently no requirement or proposal for these documents, or key information contained in the documents, to be disclosed publicly or tabled in Parliament. While departmental output measures and targets included in budget documents are publicly available, these are not necessary linked to the corporate planning process nor do they clearly disclose departmental intentions regarding the outcomes expected from their operations.

4.1.30 The introduction of requirements for departments to provide Parliament with key information contained in their corporate plans, including strategies and targets, is worthy of consideration to ensure a complete public accountability cycle is in place in relation to departmental operational performance.

Content of reports of operations

4.1.31 The audit legislation provides the Auditor-General with the power to audit the performance indicators contained in the report of operations included in departmental annual reports.

4.1.32 In accordance with directives issued by the Minister for Finance, departments (and public bodies) annual reports of operations are to include the following information:

- the objectives, functions, powers and duties of the agency;
- the nature and range of services provided by the agency;
- the administrative structure of the agency;
- information regarding the financial results for the year;
- the operational and budgetary objectives of the agency for the financial year and performance against those objectives;
- in the case of departments, a comparison of the output targets specified in the State Budget with actual performance against those targets; and
- a summary of changes or factors which have affected the achievement of the operational objectives for the year.

4.1.33 We understand that the directive is to be amended to also require the objectives and performance indicators to be included in the report of operations. In essence, the performance information included in the budget documents will provide the framework for the management and reporting of performance in departmental annual reports for the 2001-02 financial year.

4.1.34 We have concerns regarding the suitability of output measures developed as part of the budget process as appropriate indicators of departmental achievements in that:

- The 2000-01 Budget Papers contain over 300 outputs with numerous measures for each output. At present, the mass of detail in the Budget Papers tends to obscure the key performance issues and the volume of information does not enable easy assessments of performance;
- There is inconsistency in the interpretation of what constitutes an output measure. A small number of quality measures, for example, are more outcome focused in that they relate to the impact of services on the community, such as *"the percent of year 3 students reaching national benchmarks in reading"* while other quality measures are more process related such as the *"achievement of milestone targets for grants processing"*. The nature of most measures do not readily enable an assessment of the efficiency and effectiveness of each department's operations. For example, many of the measures do not clearly link costs to the quantity of particular outputs produced and they do not provide information regarding the outcome of services;
- The measures included in the budget papers are directed at reporting on a relatively short-term basis by including information relating to the previous year, current year and forthcoming year. Given the nature of the activities of some departments, reporting trends over longer timeframes would also be appropriate; and
- The measures do not enable an assessment of the ongoing capacity of departmental assets to support the delivery of services.

4.1.35 These weaknesses raise questions regarding the cost-effectiveness of auditing all the performance information currently required to be reported and suggest that **a review of the current directive relating to the report of operations is warranted.** In undertaking such a review there needs to be a focus on presenting key efficiency and effectiveness measures in a form that is readily understood by the users. Consideration should also be given to strengthening the link between the report of operations and the corporate plans of departments.

4.1.36 In developing a revised directive on the performance reporting content of annual reports, the Department of Treasury and Finance should consult with individual agencies and public bodies, the Public Accounts and Estimates Committee and our Office.

4.1.37 To ensure publicly reported information on government and departmental achievements meet the information needs of key users, consultation with stakeholders, including service users, should also form an integral part of confirming the suitability of the specific performance indicators established for each department.

Output review framework

4.1.38 As part of the revised performance reporting framework, the Department of Treasury and Finance is establishing a process to systematically review, over a 3 to 5 year period, all outputs provided by departments. This will involve output evaluations, which will focus on the effectiveness of the outputs delivered, and price reviews, which will focus on the price paid by the Government for the output.

4.1.39 The stated aim of the output evaluations is to assess the extent to which departmental objectives and desired government outcomes have been achieved through the delivery of outputs and whether the objectives and measures remain relevant. The outcomes of the evaluations and price reviews is aimed as assisting the Government's Expenditure Review Committee in making budget decisions.

4.1.40 While the establishment of effective evaluation mechanisms is an important component of performance management at both a departmental and central agency level, we consider that the processes proposed within the Department of Treasury and Finance requires further clarification in terms of:

- the scope of the evaluations particularly in relation to assisting departments in improving service delivery;
- the methodologies to be adopted in the evaluations;
- linkages with any evaluation mechanisms established within departments as part of their ongoing performance review processes; and
- the disclosure of the results of evaluations and any role the evaluations may play in regard to public accountability.

Proposed future audit approach

4.1.41 As indicated previously, we do not consider the revised budget sector performance management framework has yet been sufficiently developed to enable audit opinions to be issued. With the aim of enhancing the quality of performance management and reporting across the public sector, our Office will therefore initially be undertaking a number of audits within departments and public bodies. As a first step, **we intend to conduct a more detailed assessment of the standard of each department's performance management reporting arrangements and to provide the results of these assessments to the Parliament later in 2001.** Departments will then be able to consider the outcome of these assessments as part of preparing for reporting on their performance for the 2001-02 financial year.

4.1.42 The assessments will examine the quality of departmental performance reporting for public accountability purposes. They will focus on the clarity and measurability of departmental objectives, the relevance and appropriateness of performance indicators and the linkages between the high level government accountability framework, departmental corporate plans and the budget process. In addition, the preparedness of departments to report on their performance in the 2001-02 financial year, including the adequacy of underlying performance information systems, will be examined.

4.1.43 The outcome of the assessments will inform future decisions by our Office regarding the most appropriate timing of the issue of any audit opinions regarding the relevance, appropriateness and fair presentation of performance information included in departmental annual reports.

***RESPONSE** provided by Secretary, Department of Treasury and Finance*

The work undertaken by the Department of Premier and Cabinet and the Department of Treasury and Finance (DTF) is closely aligned. The objectives of departments were developed in consultation with Ministers to ensure alignment with the developing government outcomes.

DTF, in consultation with departments, has developed the MRP Evaluation Framework as a formal assessment of the implementation of accrual output management. Departments have assessed their implementation including the level of accountability for output delivery and output performance reporting against the framework, and have developed strategies to further implement output accountability and reporting internally. The progress against these strategies are reported to the Government and DTF quarterly.

DTF has fully adopted outputs as the focus of its own internal management reporting.

The output measures are considered an appropriate level of disclosure for the assessment of departmental performance. The users of output information are many and varied. Any reduction in the volume of measures may impact on the accountability and transparency of departmental service delivery and may adversely impact on individual users.

In some instances, it is appropriate to have result-oriented performance measures attached to an output. This is appropriate where the relevant measurement of the quality of the output is the achievement of given results (i.e. School Education).

Output reporting is necessarily short-term; it reports what has been delivered. The introduction of departmental objectives, performance indicators and the new Output Review Framework will promote a longer-term focus on effectiveness and impact.

Departments have fully costed their outputs on an accrual basis. The measures relate to the delivery of the output, not to the system that facilitates such delivery. Currently, the price paid by government is based on that full costing.

The Output Review Framework will be trialled during 2001-02. The clarifications requested by the Auditor-General are included in the Output Review Guidelines to be published in June 2001.

***RESPONSE** provided by Secretary, Department of Premier and Cabinet*

The Report identifies areas for enhancement in the provision of performance information, and suggests that the Department of Premier and Cabinet's (DPC's) work to define high level outcomes and performance indicators does not link in to the resource allocation framework connecting resources to departmental outputs.

With regard to performance information generally, there area number of key documents currently being developed or awaiting approval which will answer many of the points raised. In particular, work on a new set of broad, high level performance indicators is currently being undertaken. These documents are not yet settled and, therefore, have not as yet been examined by your Office. Once available, they will provide valuable input into the Report.

***RESPONSE** provided by Secretary, Department of Premier and Cabinet - continued*

In terms of ensuring that resource allocation and departmental outputs are correctly integrated into performance information, DPC and the Department of Treasury and Finance (DTF) already have a process in place to facilitate this. DPC and DTF in conjunction with the other departments have been working closely together to ensure the alignment between the broad outcomes of government (and their measurement) and the output structure used for resource allocation and reporting. That alignment is primarily occurring through the development of objectives and key performance indicators for departments. These will form the bridge between the output structure and the whole-of-government outcomes.

The key measures of progress for the outcomes (which are in the final stages of development) have all been checked to ensure they can be measured and reported on at the outcome level and at the output level.

Part 4.2

Outcome of IT audits of government departments and selected other agencies

4.2.1 A number of information technology (IT) reviews of government departments and selected other agencies were undertaken as an integral part of the financial audit process for the 1999-2000 financial year. The purpose of these reviews was to assess the strength of IT controls within the computer environments relevant to the production of annual financial information by agencies.

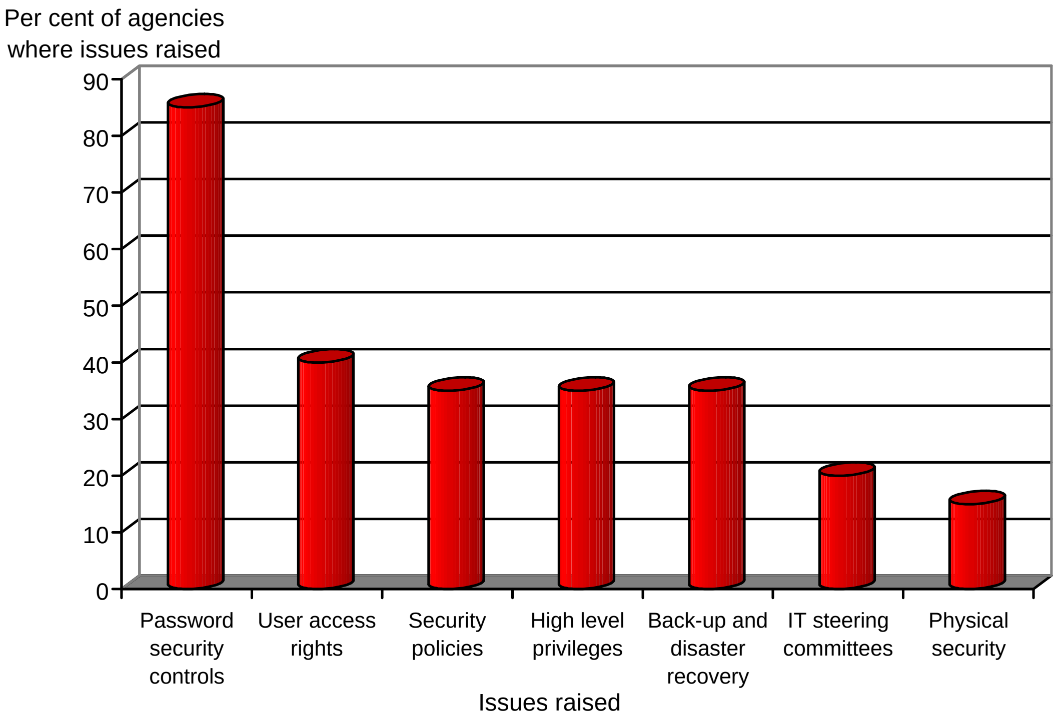
4.2.2 Twenty State Government IT environments were examined. They covered all government departments and major water and local government authorities, hospitals and other public sector agencies. This Part of the Report summarises the common issues identified during our IT reviews.

Conclusion

4.2.3 Overall, we concluded that various aspects of IT security and administration could be significantly improved at the agencies subject to our review. These aspects, which are summarised in Chart 4.2A, illustrate the need for agencies to enhance:

- **the strategic oversight of IT development and policy;**
- **system security including password controls and other access controls; and**
- **back-up processes for computerised information and disaster recovery planning.**

CHART 4.2A
IT REVIEWS – SUMMARY OF ISSUES IDENTIFIED



Source: Victorian Auditor-General's Office 2001.

4.2.4 Detailed comments on the above issues follow.

Need for improvements to password security controls

4.2.5 Password security controls and password configuration settings in most organisations subject to our review were found to be in need of improvement to address a number of issues, ranging from minor in some organisations to significant in others. Specific deficiencies in password controls included:

- user accounts having no password;
- easy to guess passwords;
- users not being required to periodically change their passwords at both application systems and operating system levels;
- passwords not required to comply to a minimum length or configuration;
- "generic" or shared user accounts where staff are sharing passwords;
- inadequate controls to limit the number of unsuccessful log-on (access) attempts to systems; and
- lack of controls to prevent users from re-using or recycling old passwords.

4.2.6 Password security controls are typically the primary form of restricting access to an organisation's computer systems and IT resources and in various cases are the sole control restricting access to a particular system or computer. Therefore, it is critical that organisations implement strong controls to safeguard their systems and data.

4.2.7 We have made various recommendations to strengthening the control over password access and security to the respective organisations where the deficiencies were identified.

Need for improvement in managing user access rights

4.2.8 Formal procedures had not been established in around 40 per cent of organisations to ensure the timely removal of IT access rights for former employees. In certain cases, this had resulted in former employees/users still recorded as having access to critical systems long after their employment had ceased.

4.2.9 Without formal procedures in this area, there is an increased risk of system administrators failing to remove, where required, user accounts with security access clearance to critical systems. The importance of maintaining control over this area is further increased because dormant user accounts can be used, particularly by "hackers", as an initial entry point for gaining unauthorised access into systems.

4.2.10 We have recommended formal procedures be instigated for the removal of user accounts from application systems and operating systems as soon as staff departures occur.

Inadequate information security policies

4.2.11 Around 35 per cent of the organisations reviewed had either inadequate policies in relation to information security or, in certain instances, entirely lacked a formal and promulgated information security policy.

4.2.12 An information technology security policy should document the framework for establishing and maintaining information security throughout an organisation. This policy should stress the importance of information security within the organisation, describe IT security standards and compliance requirements, and formally allocate responsibility for information security management.

4.2.13 In the absence of appropriate security policies, the risk of implementing inappropriate and inadequate computer security controls is increased. In addition, in the event of any misuse or abuse involving information technology, the organisation has a reduced chance of successfully prosecuting or appropriately dealing with the responsible individual.

4.2.14 Recommendations were made to relevant organisations to either develop formal policies or, alternatively, to enhance existing policies in critical areas not previously addressed.

Inappropriate system access privileges

4.2.15 In over 30 per cent of organisations assessed, we found instances of users with access to high-level operating system privileges or security clearances that exceeded the recommended levels necessary to perform their day-to-day tasks. This included users being allocated *super-user* access rights on the organisation's computer system(s).

4.2.16 High level security access rights at the operating system level allow users to read, modify or delete sensitive data and/or system configurations, run any program and, in many instances, assume the identity of any other user of the system. As such, access to high-level security privileges should be heavily restricted and controlled.

4.2.17 Recommendations were made to remove excessive numbers of *super users* or to tighten the levels of security access granted to various staff or user accounts.

Need for enhanced IT disaster recovery and business continuity plans and off-site back-up

4.2.18 Of the 20 government organisations reviewed, around 30 per cent required improvements to be made to their business continuity or IT disaster recovery plans to effectively support their financial operations and systems. In addition, 15 per cent of organisations reviewed had either inadequate off-site storage facilities or were yet to implement such facilities for storing back-up media containing critical data.

4.2.19 Without effective and tested recovery plans, an organisation may experience considerable difficulties in recovery of their systems and critical business information, in the event of a disaster or system interruption. We have made various recommendations to ensure these risks are addressed.

Insufficient use of formal IT steering committees

4.2.20 Of the agencies subject to our IT review, 20 per cent had not established an effective IT Steering Committee (or Management Committee) to oversee the overall direction and activities of their IT divisions or the utilisation of their IT resources.

4.2.21 Without effective IT Steering Committees, there is a heightened risk that IT activities will not be consistent with the overall objectives or strategies of the organisation. The absence of an IT steering committee function may also lead to a failure to appropriately control major IT projects and resources.

4.2.22 At each organisation where this issue was identified, we recommended to management that their IT functions and operations be overseen by an appropriate committee comprising senior executives from across the entire sphere of the organisation's operations.

Inadequate physical computer security controls

4.2.23 Our review found that physical computer security controls over computing facilities required improvements at 15 per cent of organisations examined. Areas requiring improvement differed between organisations but can be generally related to:

- physical access restrictions over computing facilities;
- fire detection and prevention controls and devices; and
- power regulating devices and back-up power sources.

4.2.24 The potential for damage to computer facilities exists through fire, flood, loss of power, or unauthorised entry. Damage to computer hardware may cause loss of critical data and severe interruption to an organisation's operations. Adequate physical security controls over computer facilities should therefore be in place to prevent or reduce the potential for physical damage.

4.2.25 Recommendations were made to relevant organisations to implement improvements to the effectiveness of physical computer security controls to reduce the risk of loss or unauthorised access to IT facilities.

***RESPONSE** provided by the Secretary, Department of Treasury and Finance*

Password security

The Department of Treasury and Finance has a requirement for all users to input a password to access any of its environments including Oracle Financials, Novell Local Area Network (whether accessed via a desktop PC within the Department's precinct or via remote dial-up access) and Lotus Notes.

Those systems that provide first point of entry to the Department's data require users to change their passwords every 30 days, and also have requirements for users to have passwords of minimum length. In the case of access to the Oracle systems, users must have at least one numerical in the first 6 characters.

Unfortunately the use of "generic" accounts is unavoidable in some instances, though as a general rule the Department does not usually establish these accounts. The Department ensures that if generic accounts must be established that they are only used in low risk situations.

Unsuccessful logins to the Local Area Network are strictly monitored, and users' accounts are locked out after 3 unsuccessful attempts to login; this is also the case for logins to the Oracle Financials system.

Both Novell and UNIX passwords are required to be different by at least 3 characters each time a user is required to change their password. Novell security has been set-up such that users are unable to re-use the same password for at least 12 months.

Management of user accounts

Each month a "Stale Users" report is produced for accounts on the Oracle Financials system and Novell Local Area Network. These accounts are investigated to see the status of the user, i.e. on maternity leave, long service leave, annual leave, left employment of the Department. User accounts are dealt with accordingly.

***RESPONSE** provided by the Secretary, Department of Treasury and Finance - continued*

Security policies

The Department has a formal security policy.

Systems access privileges

All Oracle Financials users who are granted "super-user" access require such privileges to perform their day-to-day work. Such users include the supervisors for each module as well as support staff so that they can re-create any functionality problems that occur on the system for the purposes of trouble-shooting.

Unisys, as the Department's IT service provider, has "super-user" account privileges on the Local Area Network and under Oracle in order to perform tasks as required under its support arrangement with the Department.

IT disaster recovery, business continuity plans and off-site back-up storage

The Department is currently looking at means of providing sufficient Disaster Recovery Planning to make contingencies for a number of potential situations. These discussions are taking place in partnership with Unisys which provide support services for the hardware located in the computer room in the Treasury precinct.

IT Services has recently commissioned a report from Unisys which looks at the possibility of using existing development hardware to restore production services in the case of any major hardware failure, in order to facilitate business continuity for the duration of any hardware failure for the Oracle systems. The finer details of the report are currently being looked at for feasibility and logistics, and will be responded to over the next month.

At present, all back-ups taken on equipment in the Treasury computer room are re-located off-site during the next business day following their creation. This covers all Oracle and Local Area Network servers. Back-up tapes are only returned to the Treasury computer room when required for daily backups or when required to restore files on request. In addition, the final back-ups for each month are retained off-site indefinitely.

IT Steering Committee

The Department currently has in place an IT Steering Committee to oversee the implementation of the Department's IT Strategic Plan for the coming 3 years. A number of projects have been identified through the Strategic Plan for implementation over the coming years. All projects to be implemented over the coming 12 months have been allocated project sponsors from the IT Steering Committee, and will be monitored via the OASIS reporting mechanism used within the Department.

Reviews of the IT Strategic Plan will take place once a year to ensure the relevance of the targeted projects.

Physical computer room security

All Department computer servers and central network equipment are located within a secured facility within the Treasury precinct. Access to the facility is controlled as a separate zone within the building's proximity card security system and a security camera monitors the only entrance.

Unisys is responsible for the security of the Department's computing equipment and must approve who is authorised to access the computer facility. The appropriate checks are made with Unisys before proximity cards are updated for user access to the computer room.

RESPONSE *provided by the Secretary, Department of Treasury and Finance - continued*

Physical computer room security *- continued*

A physical log book is maintained to record details of visitors to the room including the name of the visitor, time of arrival, purpose, Unisys contact and the time of departure. In most cases, a Unisys employee will remain onhand to supervise any works undertaken by visitors in the computer room.

The computer room itself has its own independent fire detection and retarding system that is connected to the Metropolitan Fire Brigade. The room also has independent air-conditioning units that regulate the temperature so that equipment does not overheat. Dedicated 3-phase wiring is installed to ensure enough power is available to all equipment and a battery powered Uninterrupted Power Supply is also attached to the network to protect equipment from power fluctuations and short-term power failures.