VICTORIA

Auditor General
of Victoria

REPORT ON
PUBLIC SECTOR AGENCIES

Results of special reviews and 30 June 2003 financial statement audits

November 2003

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AUDITOR GENERAL
VICTORIA

The Hon. Monica Gould MP
President
Legislative Council
Parliament House
MELBOURNE

The Hon. Judy Maddigan MP
Speaker
Legislative Assembly
Parliament House
MELBOURNE

I am pleased to forward this report to you for presentation to each House of Parliament, pursuant to section 16 of the *Audit Act* 1994.

The report sets out the results of financial statement audits conducted on public sector agencies with 30 June 2003 balance dates and the results of a number of special reviews undertaken up to the date of its preparation. It also comments on the status of matters raised in 2 previous performance audit reports tabled during the 2001-02 financial year.

Yours faithfully

J.W. CAMERON
Auditor-General

26 November 2003

Contents

Part 1

Executive summary

INTRODUCTION

This report draws together the results of our financial statement audits for public sector agencies with 30 June 2003 balance dates. The report also outlines the results of a number of special reviews. It is organised into 2 parts, namely:

- *Summary of audit results and cross-sector issues* – presenting an overall summary of the results of June 2003 audits. It also includes the significant factors that have impacted on financial reporting during the cycle, or are likely to impact on future financial reporting; and
- *Results of financial audits and special reviews, by sector* – outlining the results of the financial audits of reporting entities within Parliament and each major sector of government activity, together with the results of certain special reviews.

The Report provides greater coverage of the results of financial audits than included in previous reports. This coverage is provided to increase the information available to Parliament on the effectiveness of financial reporting, the financial results of key sectors and the adequacy of financial policies and systems used by agencies. We will also continue to include the results of special reviews in future reports on public sector agencies.

OVERALL RESULTS OF FINANCIAL AUDITS

Audit opinions

We issued 428 clear audit opinions and 13 qualified audit opinions on the financial statements of State and local government agencies with 30 June 2003 balance dates. We also issued 75 clear audit opinions and 4 qualified audit opinions on performance statements of municipal councils. The major reasons for qualified audit opinions were:

- Inappropriate disclosure of grants revenue within financial statements;
- Failure to consolidate organisations that were regarded as "controlled entities" within financial statements;
- Prior year comparative balances included in financial reports of newly acquired companies had not been previously audited; and
- For performance statements, failure of certain councils to include within their corporate plans, appropriate business plans, performance measures and/or targets as required under the *Local Government Act* 1989. The councils were therefore not able to report against such measures and/or targets.

The number of qualified audit opinions reduced significantly in 2002-03, reflecting the positive action by agencies to resolve a number of the issues previously identified.

At the date of preparation of this report, we had not issued audit opinions on 12 agencies with 30 June 2003 balance dates as completed financial statements had not been received.

Timeliness of financial reporting

A significant improvement was observed in the timeliness of financial statement completion by public sector agencies, with 66 per cent of State agencies meeting the 12-week statutory reporting target (40 per cent in 2002) and 95 per cent of local government agencies meeting the 3-month statutory reporting target for that sector (76 per cent in 2002). The results were however mixed at a sector level, with some sectors continuing to have difficulties in meeting the statutory reporting target.

Scope exists for further improvement in the timeliness of reporting, particularly considering recent research that suggests that best practice organisations have reduced statutory financial statement preparation times to around 10 to 15 elapsed days from balance day. This compares with the current statutory requirement for State agencies to submit financial statements to my Office within 8 weeks (56 days) from balance date.

We recommended:

- **The earlier completion of major asset and liability valuations (such as major non-current physical asset and actuarial valuations), and key account reconciliations;**
- **For departments, the earlier completion of the appropriation certification process by the Department of Treasury and Finance; and**
- **The introduction of earlier/interim account "close-offs" by agencies. International better practice indicates that an early "close-off" achieves significant time and resource savings at year-end. This process assists in the earlier identification and resolution of any major contentious accounting and reporting issues.**

Paras 2.24 to 2.33

Quality of financial reporting

We observed improvement in the quality of financial reporting by public sector agencies. However, there was further scope for agencies to improve the financial statement preparation process.

We recommended agencies strengthen their year-end planning processes, the capability of their finance functions and the quality assurance processes over the preparation of the financial statements.

Paras 2.37 to 2.39

Adequacy of control environment

Our audit process confirmed that the systems of internal control maintained by agencies impacting on the preparation of financial reports operated adequately during the year. However, various improvement opportunities were identified. Among the more significant issues requiring attention were:

- slow progress in the development of integrated risk management frameworks;
- deficiencies in information technology environments and systems;
- inadequate reconciliation and review procedures relating to key accounting systems; and
- need for improved asset valuation and management practices.

Our more significant recommendations for addressing these issues were that agencies should:

- **adopt formal risk management approaches that are appropriate to the agencies' level of risks;**
- **develop fraud prevention and detection strategies, including appropriate treatment plans, to minimise the risk of fraudulent activity;**
- **ensure that audit committees are established and operate in accordance with better practice and, where applicable, relevant Ministerial Directions;**
- **assess their business continuity preparedness, including IT, and develop or review appropriate business continuity plans;**
- **develop an appropriate IT strategic plan that outlines the high level IT objectives and strategies of the agency over the medium to long term;**
- **regularly review and update their password security policies over critical business systems;**
- **focus attention on ensuring the accuracy and integrity of information held on supplier master files, and the timely completion of appropriate accounts payable review and reconciliation procedures;**
- **further strengthen controls over their payroll environment, with particular attention to be given to ensuring the accuracy of information held in computerised employee master files; and**
- **encourage employees to utilise their annual leave entitlements on a more timely basis.**

Paras 2.40 to 2.105

Developments in financial reporting

Over the past 18 months there have been 2 significant developments that will impact on the future direction of financial reporting by the public sector. First, the proposed harmonisation of the Government Finance Statistics (GFS) and the Australian Generally Accepted Accounting Principles (GAAP) reporting frameworks and, second, the adoption of international accounting standards by all reporting entities for reporting periods commencing on or after 1 January 2005.

Both these developments will have major ramifications for public sector agencies, which must be carefully managed to ensure an understanding of, and compliance with, the new requirements. We are supportive of initial steps taken by the Department of Treasury and Finance to establish a leadership role within the Victorian public sector in relation to these developments. However, it is important that the implementation strategies be closely monitored to ensure that agencies, particularly non-departmental and smaller agencies, gain an adequate and timely understanding of the major changes and their implications.

We recommended that agencies:

- **identify the likely effects of the changes on financial budgeting, workloads, report presentation and relationships with stakeholders;**
- **conduct a gap analysis to identify new information needs and changes to systems and processes that may be required;**
- **develop a training strategy to ensure a sound understanding of the new requirements underpinning the changes; and**
- **consider how their boards, audit and other governance bodies are kept abreast of the developments.**

Paras 2.107 to 2.120

The following pages present a summary of the other major findings and recommendations.

OTHER MAJOR FINDINGS AND RECOMMENDATIONS BY SECTOR

EDUCATION AND TRAINING

Application of the capital assets charge

The capital assets charge paid by the Department of Education and Training in 2002-03 was consistent with that approved by the Minister for Finance. However, its downward revision by $78.5 million to ease departmental budgetary pressures brings into question whether the intended objectives of the charge (from both financial and asset management perspectives) are being achieved.

We recommended that the operation of the capital assets charge be reviewed with a view to assessing its effectiveness in meeting its intended objectives.

Paras 3.2.18 to 3.2.22

Status of recommendations - Teacher work force planning performance audit, *2001*

The Department of Education and Training has made progress in implementing the recommendations made in the 2001 performance audit report on *Teacher work force planning*.

There is still a need for the Department to take further action in the following areas:

- improving the extent of information on retirement intentions of teachers and on former teachers' future intentions to return to teaching;
- implementing proposed enhancements to the Human Resources Management System that directly support work force planning activities;
- establishing a consolidated source of work force information for school Principals;
- developing additional initiatives to increase teacher supply; and
- reviewing the operations of the Teacher Supply and Demand Reference Group and its decision-making power, and encouraging the co-ordination of research.

Paras 3.2.25 to 3.2.75

HUMAN SERVICES

Financial viability of public hospitals

The overall financial position of public hospitals further deteriorated during 2002-03, with 15 hospitals showing signs of financial difficulty and a further 22 hospitals having unfavourable results.

We recommended that the Department of Human Services work closely with the respective hospitals to identify the reasons for financial difficulties currently faced, review its current funding strategy and develop ongoing strategies to improve the financial performance of these hospitals in the future.

Paras 3.3.14 to 3.3.35

Although the parliamentary appropriation arrangements currently operating in Victoria are based on the full cost of service delivery, including depreciation, the grants provided to individual public hospitals do not cover the cost of depreciation. By not providing the funding equivalent of the cost of depreciation to each hospital, the service capacity of hospitals may not be maintained.

We recommended that the Department of Human Services, in conjunction with the Department of Treasury and Finance, re-assess the current method of funding for public hospitals. This re-assessment should address the need to ensure that depreciation funding is provided to hospitals to effectively maintain existing hospital infrastructure.

Paras 3.3.27 to 3.3.31

INFRASTRUCTURE

Application of parliamentary appropriations

The Department of Infrastructure received appropriation funding of $207 million ahead of service delivery, which was transferred into 2 trust accounts and remained unspent at 30 June 2003. This practice is inconsistent with the purchaser/provider principle embodied in the current parliamentary appropriation framework.

We recommended that any amounts standing to the credit of trust accounts within the Trust Fund at the end of the financial year, which represent funds drawn-down from the Consolidated Fund for services not yet delivered, should be repaid to the Consolidated Fund.

Paras 3.4.20 to 3.4.24

INNOVATION, INDUSTRY AND REGIONAL DEVELOPMENT

Underspend of parliamentary appropriations

Over the past 3 years, the value of appropriations applied by the Department has, on average, been around 24 per cent below the available parliamentary authority, equivalent to $107.8 million.

We recommended that the Department further assess the underlying reasons for the above financial outcomes and the implications for the preparation and management of future departmental budgets.

Paras 3.5.16 to 3.5.19

Australian Grand Prix events

The net operating cost in 2002-03 of staging the Formula One and Motor Cycle Grand Prix events totalled $19.4 million ($16.2 million in 2001-02). This follows the trend established since the State first hosted these events. However, it is less than the previously estimated annual economic benefit to the State from staging these events.

Paras 3.5.20 to 3.5.24

Federation Square

The revised estimated cost of Federation Square to the State, at 30 September 2003, was $481.7 million. This represents an increase of $8.4 million from the estimate reported in May 2003**.**

Paras 3.5.25 to 3.5.30

While the confirmed funding will be sufficient to meet the currently estimated cost of Federation Square, any significant escalation in costs may compromise the funding position of Federation Square Management Pty Ltd.

Paras 3.5.31 to 3.5.33

The financial position of Federation Square Management Pty Ltd is finely balanced and rests on a number of key assumptions over the 2003-04 financial year, which may be subject to variation and are not completely within the control of the company.

We recommended that the company continue to closely monitor its budget and funding position.

Paras 3.5.34 to 3.5.38

JUSTICE

Lack of funding agreements

There are currently no formal funding agreements in place between the Department of Justice and other portfolio agencies which receive annual grants totalling more than $1.3 billion.

To improve accountability arrangements, we recommended that the Department formalise funding agreements with all agencies in receipt of annual grant funding.

Paras 3.6.18 to 3.6.21

Need for clarification of funding arrangements

The current funding practices adopted by the Victorian Electoral Commission are not consistent with legislative requirements.

We recommended that the Commission:

- **review its current practices, in conjunction with the Department of Justice, to ensure that practices comply with requirements for revenue collection and the receipt of appropriations; and**
- **enter into a formal funding agreement with the Department to facilitate reconciliation between amounts recorded in its financial records and corresponding amounts recorded in the Department's records.**

Paras 3.6.28 to 3.6.34

PRIMARY INDUSTRIES

Melbourne Market Authority – Investment in Fresh Chain Ltd

The Melbourne Market Authority invested $13.8 million in, and is the majority (95 per cent) shareholder of, Fresh Chain Ltd (Fresh Chain) - a company incorporated in May 2001. However, due to the poor financial performance of the company, its directors resolved to cease all operations and close the business on 30 June 2003. At the time of preparation of this report, the Melbourne Market Authority was endeavouring to sell the Fresh Chain business.

Paras 3.8.14 to 3.8.19

SUSTAINABILITY AND ENVIRONMENT

Completeness of Crown land records

Over many years we have had concerns about the inability of the Department to confirm the completeness of its records of Crown land managed by external departments and agencies. While the Department has commenced a review of its records, little progress had been made to date.

We recommended that the Department continue to pursue its review of the accuracy of its records of Crown land, in co-operation with other agencies managing Crown land.

Paras 3.9.23 to 3.9.26

Resolution of Seal Rocks litigation

The resolution of the Seal Rocks Life Centre dispute involved the payment of $42.9 million to the former operators of the Centre. In addition, the Department incurred around $13 million in legal and other costs over the 3-year period of this dispute.

We recommended that the Department, in consultation with other stakeholders, undertake an ex-post review of the management of the original agreement and subsequent legal resolution, with the aim of identifying areas for future attention/improvement that could, in turn, reduce the risk of similar issues arising in the future.

Paras 3.9.27 to 3.9.29

Water sector – overview of financial operations

An overall loss of $24 million (2001-02, $18 million) was recorded by rural water authorities. This was mainly attributable to the level of depreciation costs not being fully recovered through the current pricing levels.

Paras 3.9.30 to 3.9.33

Asset valuation in the water sector

The cost method of valuing assets is acceptable under existing accounting standards. However, the impact of the current situation (whereby some water sector agencies value their assets at cost while others record them at valuation), reduces comparability between agencies operating in the same sector.

We recommended that steps be taken by the water authorities, in conjunction with central agencies, to ensure that an appropriate and consistent asset valuation basis is established across the water sector.

Paras 3.9.34 to 3.9.41

SUSTAINABILITY AND ENVIRONMENT - *continued*

Processes for approval of revenue waivers

A metropolitan water authority was not able to adequately demonstrate that an appropriate basis existed for its waiver of fees and charges totalling $243 000.

We recommended that the water authority review and update its current policy and guidance relating to debt relief and waivers to ensure consistency in the treatment, processing and consideration of all customers requests for financial relief.

Paras 3.9.42 to 3.9.45

Central Gippsland Region Water Authority - Waste management operations

The Central Gippsland Region Water Authority has operated an industrial waste business on its Dutson Downs site since the mid 1950's. The Authority is currently proposing development of a soil treatment and recycling facility on this site.

An Environment Improvement Plan had not been submitted to the EPA for approval by the date specified in the Authority's licence to accept waste.

The Authority's emergency event management strategy was at a preliminary stage of development despite the length of time that the site had been operating.

Given the likelihood that scientific standards and community expectations will continue to evolve, the Department should continually reassess the suitability of the Dutson Downs site for the management of industrial waste.

The Authority nominated its Dutson Downs property as a site for a significant soil recycling facility after a preliminary assessment but prior to undertaking a detailed business case and completing full environmental assessments. A subsequent environmental study, undertaken by a consultant engaged by Major Projects Victoria in conjunction with the Authority, has determined that the establishment of the proposed facility would have an insignificant effect on the surrounding environment.

A number of financial and business risks arise from the proposed soil recycling facility, including those associated with technical expertise, the levels of proposed revenue and operating costs and public and environmental safety.

Detailed recommendations to address the key issues identified are included in Part 3.9 of this report.

Paras 3.9.49 to 3.9.285

SUSTAINABILITY AND ENVIRONMENT - *continued*

Catchment management in Victoria

A number of strategies deal with specific issues affecting the State's water catchments such as salinity, river health and pest management. However, there is no integrated Statewide catchment management strategy.

We identified a range of weaknesses within Catchment Management Authorities over:

- acquittal of expenditure from grants received for specific purposes;
- financial management knowledge and experience of Authority Boards;
- the quality and accuracy of financial and performance reports provided to Boards;
- the adequacy of internal audit processes; and
- project management and reporting.

Detailed recommendations to address the key issues identified are included in Part 3.9 of this report.

Paras 3.9.286 to 3.9.454

TREASURY AND FINANCE

Timing of triennial valuations for superannuation funds

The current timing of triennial reviews of public sector superannuation fund liability valuations and funding positions creates a potential risk that results may differ from those used to calculate liabilities as disclosed in annual financial statements.

We recommended that the Government Superannuation Office and the Emergency Services Superannuation Scheme time future triennial actuarial reviews to allow incorporation of results in financial statements for the year to which the reviews relate.

Paras 3.10.24 to 3.10.26

TREASURY AND FINANCE *- continued*

Applicability of APRA guidelines for State insurances

In the absence of clear guidelines for the government sector, the 3 State insurance bodies currently adopt different philosophies and practices for prudential margins, risk-free discount rates and capital adequacy reserves.

We recommended that an appropriate and consistent liability valuation regime be implemented for the State's insurance bodies. In developing this regime, consideration should be given to the Australian Prudential Regulatory Authority guidelines, developments in international financial reporting standards and the recommendations of the HIH Royal Commission.

Paras 3.10.27 to 3.10.31

Status of recommendations - Management of major injury claims by the Transport Accident Commission performance audit, 2001

The Transport Accident Commission has made significant progress in implementing the recommendations made in our 2001 performance audit report.

Paras 3.10.45 to 3.10.91

The Transport Accident Commission has recently revised and enhanced its communication materials for claimants outlining entitlements under the scheme. The provision of relevant information to claimants is monitored as part of the file review process for all new and existing claimants. Our follow-up review has indicated that there is further room for improvement in the provision of timely information to claimants.

We recommended that a formal assessment of the timeliness with which the re-written information is provided to claimants be undertaken as part of the normal Major Injury Division file audit program.

Paras 3.10.81 to 3.10.84

LOCAL GOVERNMENT

Financial results

The combined net operating result for all municipal councils and related sector agencies for 2002-03 was $334.4 million. However, after excluding certain non-recurring revenues and expenditures, the sector generated an overall "underlying operating deficit" of $15.1 million.

We recommended that individual councils consider the use of key indicators of short to medium financial health, including projected trends in the councils' future operating results, "current" ratios and the cash position.

Paras 3.12.12 to 3.12.25

Valuation of infrastructure audits

Those municipal councils which have not yet revalued their infrastructure assets to fair value face a significant challenge in meeting the 30 June 2005 timetable established by accounting standards, given the typically long lead times required to plan, execute and report on asset valuations.

We recommended that councils:

- **finalise plans for the progressive revaluation of their assets, and establish a systematic approach to annually reviewing the carrying value of their assets to ensure the currency of these values; and**
- **maximise the utility of asset valuations, by ensuring that sufficient and appropriate instructions are provided to valuers, including specification of the form and content of valuation reports.**

Paras 3.12.54 to 3.12.64

Debt collection

There is evidence that at least 10 per cent of parking and related fines are never collected. This represents an annual revenue leakage of around $10 million.

We recommended that municipal councils with significant unpaid fine debtors consider whether taking a more pro-active approach to the recovery process would provide a net benefit.

Paras 3.12.65 to 3.12.71

LOCAL GOVERNMENT - *continued*

Unfunded superannuation liability

Liabilities of local government agencies increased by $133.8 million in 2002-03 as a result of a call for additional funding made by the Local Authorities Superannuation Fund. This arose from a shortfall in the net assets of the defined benefit plan that the Fund administers on behalf of local government agencies and other local authorities.

We recommended that municipal councils which have yet to pay their share of the unfunded superannuation shortfall develop payment and funding strategies, and regularly review these strategies, in light of the current and future earning rates of the Fund.

Paras 3.12.72 to 3.12.76

Operation of audit committees

While almost all municipal councils have operational audit committees, there were indications that not all committees were fully effective.

We recommended that:

- **all committees assess the extent to which weaknesses outlined in our report might apply to them and what impact they may have on the committees' overall effectiveness; and**
- **all councils review the relationship between the external auditor and their audit committee to ensure that the committee is best placed to achieve its objectives.**

Paras 3.12.87 to 3.12.98

Information security

By far, the most common control weaknesses identified by audit related to access controls over operating systems and end-user applications.

We recommended that all agencies review their information security regularly against an updated risk and threat assessment. This should include a review of the effectiveness of the operation of the controls established by management.

Paras 3.12.107 to 3.12.109

LOCAL GOVERNMENT *- continued*

Operation of internal audit functions

Twelve municipal councils either had no internal audit or a limited internal audit function operating throughout the past financial year. It was not apparent within these councils what other monitoring and review mechanisms had been established to inform management and the councils on the effectiveness of their systems of internal control.

We recommended that all councils periodically assess their monitoring and review activities to satisfy themselves that they are obtaining sufficient, appropriate and timely information on the effectiveness of internal control processes.

Paras 3.12.114 to 3.12.116

Part 2

Summary of audit results and cross-sector issues

2.1 This part of the report outlines the Auditor-General's mandate to audit the financial and other accountability statements of public sector entities, the approach we take to conducting the audits and the legislative framework established for financial reporting.

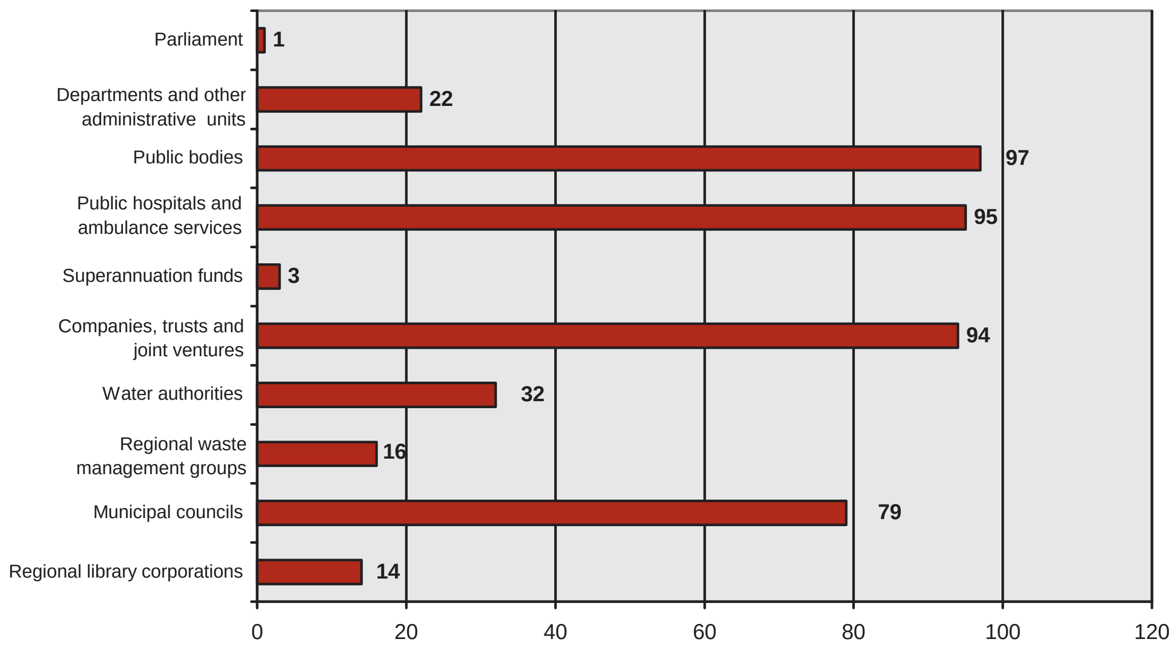
2.2 The significant factors impacting on financial reporting during the 2002-03 reporting cycle and an overall summary of the results of the financial statement audits of entities with 30 June balance dates are also included. The report further includes a number of emerging developments that are likely to have a substantial impact on financial reporting and auditing within the Victorian public sector in future years.

FINANCIAL AUDIT PROCESS

2.3 The *Audit Act* 1994 provides the authority for the Auditor-General to undertake the audit of the annual financial statements prepared by public sector entities. The *Local Government Act* 1989 requires the Auditor-General to audit performance statements prepared by municipal councils.

2.4 As at 30 June 2003, around 590 public sector agencies came within the Auditor-General's mandate. Figure 2A provides the profile of the 453 reporting entities that had 30 June 2003 balance dates.

FIGURE 2A
TYPE AND NUMBER OF AUDITED ENTITIES WITH 30 JUNE 2003 BALANCE DATES
(number)



Source: Victorian Auditor-General's Office.

Audit approach

2.5 Financial audits are conducted in accordance with the Australian Auditing Standards issued by Australian Accounting Bodies and use a risk-based methodology. The audits assess key organisational risks and associated management controls. The resultant strategy details the approach taken by audit to the risks identified. The audit strategy typically involves:

- evaluating and testing internal control structures, including controls operating over key accounting applications and systems;
- additional substantive testing to sufficiently mitigate audit risks; and
- assessing whether the information and disclosures made in the audited financial statements or statements of performance are in accordance with the relevant legislative, professional and other reporting requirements.

2.6 The financial audit does not examine all transactions but provides the users of the statements with reasonable assurance that they are free from material error. While the strategies address the risk of fraud resulting in a material error in financial statements, they are not designed to detect all incidents of fraud.

2.7 The management of each entity is responsible for keeping proper accounts and records, and maintaining adequate systems of internal control to support the presentation of the financial statements and, in the case of local government entities, performance statements. Management also has the primary responsibility for the prevention, detection and investigation of fraud and other irregularities.

2.8 The financial statements of each entity are prepared within the framework of Australian Accounting Standards and other mandatory professional reporting requirements, and the financial reporting requirements of the *Financial Management Act* 1994 and, for local government entities, the *Local Government Act* 1989.

2.9 The audit opinion on an entity's financial statements is the result of our audit. This opinion indicates whether the financial statements present fairly the financial position of the entity at the reporting date, and its financial performance and cash flows for the period under review. The main purpose of our audit opinion is to add credibility to the financial statements and, in the case of municipal councils, the performance statements prepared by the respective councils.

2.10 Professional guidance on the issue of audit opinions on financial reports is contained in Australian Auditing Standard AUS 702: *The Audit Report on a General Purpose Financial Report*. In accordance with AUS 702, the following audit opinions may be issued:

- ***Unqualified audit opinion (Clear audit opinion)*** - issued when the financial report is presented fairly in accordance with Australian Accounting Standards and relevant statutory requirements;

- ***Unqualified audit opinion with emphasis of matter*** - an emphasis of matter is included in certain limited circumstances to emphasise a specific matter that is not of such a nature that it affects the audit opinion on the financial report; and
- ***Qualified opinions*** – issued in 3 circumstances, namely:
  - ***"Except for" opinion*** - expressed when the auditor concludes that an unqualified audit opinion is inappropriate because of:
    - a disagreement with management (including inherent uncertainty not adequately disclosed); or
    - a conflict between applicable financial reporting frameworks, e.g. between accounting standards and relevant legislative requirements; or
    - a limitation on the scope of the audit; and
    - the effects or possible effects of the above are not of such a magnitude or so pervasive or fundamental as to require the expression of an "*adverse opinion*" or an "*inability to form an opinion*";
  - "***Adverse opinion"*** – expressed when the effects of a disagreement with management or a conflict between applicable financial reporting frameworks is of such a magnitude or is so pervasive or fundamental that the financial report taken as a whole is, in the auditor's opinion, misleading or of little use to the addressee of the audit report; and
  - ***"Inability to form an opinion"*** - expressed when a scope limitation exists and:
    - sufficient appropriate audit evidence to resolve the uncertainty resulting from the limitation cannot reasonably be obtained; and
    - the possible effects of the adjustments that might have been required, had the uncertainty been resolved, are of such a magnitude or so pervasive or fundamental that the auditor is unable to express an opinion on the financial report taken as a whole.

Financial reporting framework

2.11 The annual reporting and audit requirements for departments and other public sector agencies are set out in the *Financial Management Act* 1994 and the *Audit Act* 1994. Section 45 of the Financial Management Act requires departments and public bodies to submit annual financial statements to the Auditor-General within 8 weeks of the end of the financial year. The Auditor-General is required to audit the financial statements within 4 weeks of their receipt.

2.12 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 Parliament the annual report of each entity, including the audited financial statements.

2.13 For local government, the annual reporting and audit requirements are set out in the *Local Government Act* 1989 and the *Audit Act* 1994. Section 126 of the *Local Government Act* requires each municipal council and regional library corporation to submit its annual report, including a report of operations and audited financial statements, to the Minister for Local Government within 3 months of the end of the financial year. The annual report is also required to include an audited performance statement. The Auditor-General is required to audit the financial statements within 4 weeks of their receipt.

MAJOR DEVELOPMENTS IMPACTING ON 2002-03 FINANCIAL REPORTING

2.14 **The single most significant development impacting on our financial audit program during 2002-03 was the machinery of government changes made following the November 2002 State election.**

2.15 In December 2002, the Government announced a restructure of a number of departments. These changes included:

- disaggregation of the former Department of Natural Resources and Environment into 2 new departments: the Department of Sustainability and Environment and the Department of Primary Industries; and
- establishment of the new Department for Victorian Communities to undertake responsibilities and functions previously performed by other departments (such as local government; the Commonwealth Games, sport and recreation; the Community Support Fund; youth affairs; multicultural affairs, etc.).

2.16 Significant challenges were placed on the new/restructured departments to implement the changes, including the amalgamation or establishment of corporate services functions and accounting systems. A major task was the transfer of assets and liabilities and the associated financial records.

2.17 The audit impact of these changes was that:

- additional audit work was required to ensure the appropriate reporting of transactions and balances, particularly those balances transferred between departments; and
- some delays were experienced by departments, particularly the newly established departments, in preparing and completing financial statements.

2.18 **Notwithstanding the significant challenges arising from the restructure, appropriate processes were generally established by departments to facilitate the completion of the financial statements. However, as discussed below, delays in the finalisation of asset and liability transfers contributed to delays in preparing some departmental financial statements.**

***RESPONSE** provided by the Secretary, Department of Treasury and Finance*

As indicated in the Report, the December 2002 Machinery of Government changes did impact on the finalisation of financial statements of affected departments.

The complexities involved in transferring of functions between departments and ensuring that all components are appropriately recorded and accounted for was critical to the success of the transfer. Given these complexities, all departments, assisted by the Department of Treasury and Finance (DTF) completed this process and received clear unqualified audit opinions.

RESULTS OF AUDITS

Nature of audit opinions issued - Financial statements

2.19 At the date of preparation of this report, 428 clear audit opinions had been issued on the financial statements of public sector agencies with 30 June 2003 balance dates, with qualified audit opinions issued on 13 financial statements. The incidence of qualified audit opinions reduced significantly when compared with 22 qualified opinions that were issued in the previous year. This reflects the positive effect of action taken by entities to resolve a number of the contentious issues resulting in previous qualifications. Appendix A of this report provides information in respect of each agency regarding the timing of the finalisation of financial reports and audit opinions, and the nature of the audit opinions issued.

2.20 The major reasons for the issue of qualified audit opinions in 2002-03 were:

- Inappropriate disclosure of grants within financial statements. These grants, which were non-reciprocal in nature, were not disclosed in accordance with Australian Accounting Standard AAS 15: *Revenue* which requires that they be treated as income in the accounts of the recipient in the year of receipt (3 hospitals/health services);
- Failure to consolidate organisations that were regarded as “controlled entities” in accordance with Australian Accounting Standard AAS 24: *Consolidated Financial Reports* (3 hospitals);
- Failure to revalue non-current physical assets in accordance with the requirements of Australian Accounting Standard AASB 1041: *Revaluation of Non-Current Assets* which requires regular revaluations of non-current assets (one health care group);
- Inappropriate recognition of certain debtors (one hospital);
- Failure to undertake condition assessments for a significant proportion of infrastructure assets (one council);
- Prior year comparative balances included in financial reports had not been previously audited (3 newly acquired companies within the infrastructure portfolio); and
- Incorrect recognition of an expense and an associated liability (one agency in the Victorian Communities portfolio).

2.21 In addition to the above, an "emphasis of matter" comment was included in the audit report of one entity to draw attention to significant uncertainty as to whether it would continue to exist as a separate entity in the future.

Nature of audit opinions issued - Local government performance statements

2.22 At the date of preparation of this report, 75 clear audit opinions had been issued on the performance statements prepared by municipal councils with 4 performance statements subject to audit qualification. The reasons for the qualified audit opinions related to the failure of the relevant councils to include within their corporate plans, appropriate business plans, performance measures and/or targets as required under the *Local Government Act* 1989. In one case, the results reported in respect of certain performance measures were not supported by sufficient or appropriate evidence.

2.23 The incidence of qualified audit opinions on municipal council performance statements reduced significantly in the year when compared with the 9 qualified opinions issued in the previous year.

Timeliness of reporting

2.24 The audit of the financial statements of public sector entities is required to be completed within 12 weeks of the end of the financial year. Figure 2B illustrates the performance of agencies (not including local government entities) with 30 June 2003 balance dates in meeting this requirement.

FIGURE 2B
TIMELINESS OF FINANCIAL STATEMENT COMPLETION, ALL DEPARTMENTS AND PUBLIC SECTOR AGENCIES (EXCLUDING LOCAL GOVERNMENT ENTITIES) WITH 30 JUNE BALANCE DATES

Finalisation of audited financial statements (no. of weeks after end of financial period)	*2002-03*		*2001-02*	
	Number of entities	*Per cent (cumulative)*	*Number of entities*	*Per cent (cumulative)*
Less than 8 weeks	26	7	35	10
8 to 10 weeks	56	23	37	21
10 to 12 weeks	152	66	65	40
12 to 14 weeks	66	85	130	78
14 to 16 weeks	22	91	32	88
More than 16 weeks *(a)*	30	100	41	100
Total	**352**	**-**	**340**	**-**

(a) Includes entities whose financial statements had not been finalised at the date of preparation of this report.

2.25 **Figure 2B shows that there has been a substantial improvement from 2001-02 (40 per cent) to 2002-03 (66 per cent) in the number of entities meeting the 12-week reporting time frame. However, there remains substantial scope for further improvement in the timeliness of completion of audited financial statements. The audited financial statements of 8 per cent of entities took more than 16 weeks to complete from year-end (12 per cent in 2001-02).**

2.26 Figure 2C illustrates the performance of agencies within each of the major sectors/portfolios in meeting the 12-week time frame, for both the 2001-02 and 2002-03 reporting cycles.

FIGURE 2C
TIMELINESS OF FINANCIAL STATEMENT COMPLETION BY SECTOR (EXCLUDING LOCAL GOVERNMENT)

	2002-03		*2001-02*	
Sector	***Number of statements finalised within 12 weeks***	***Per cent***	***Number of statements finalised within 12 weeks***	***Per cent***
Parliament	2	100	1	50
Education and Training	3	43	-	-
Human Services	81	71	39	35
Infrastructure	7	32	8	57
Innovation, Industry and Regional Development	3	30	-	-
Justice	20	67	12	44
Premier and Cabinet	8	73	6	55
Primary Industries	5	36	1	8
Sustainability and Development	40	56	24	33
Treasury and Finance	58	91	41	61
Victorian Communities *(a)*	7	88	5	71
Total	**234**	**66**	**137**	**40**

(a) Excludes local government bodies, which are separately discussed below.

2.27 Figure 2C shows an improvement across all sectors, except for the infrastructure sector, which experienced a substantial deterioration in the timeliness of financial reporting. This deterioration was mainly attributed to the impact of machinery of government changes, public transport restructuring, and a number of other significant/contentious accounting issues, which required attention towards the end of the financial year.

2.28 A detailed analysis of the specific issues impacting on each of the sectors is provided later in this report. However, **the major factors contributing to the overall improvement in timeliness of financial statement completion in 2002-03 were:**

- earlier discussions with our staff on contentious issues, resulting in the more timely identification and resolution of significant issues;

- a substantially unchanged reporting framework with only minor changes in accounting standards;
- improved use of the guidance in model accounts contributing to the improved quality of draft financial statements; and
- a more active role taken by certain departments to monitor progress by agencies within their portfolio in meeting their reporting timelines.

2.29 However, many of the issues contributing to delays in the completion of departmental financial statements could have been resolved earlier in the financial reporting process. For example:

- issues surrounding the transfer of assets and liabilities between departments remained unresolved until October 2003, over 9 months after the implementation of machinery of government changes;
- the appropriation certification process, which confirms the major revenue source for departments, was not finalised until after the date departments are required to submit financial statements for audit; and
- certain departments appeared unaware of specific details and disclosure requirements concerning major lease and other arrangements established on their behalf by central agencies.

2.30 Timeliness of reporting is an essential characteristic of an effective accountability process. Recent research undertaken by the Australian National Audit Office, as cited in its Report No. 23, 2002-03 *Audits of the Financial Statements of Commonwealth Entities for the Period ended 30 June 2002*, indicates that best practice organisations have reduced financial statement preparation times to 10 to 15 elapsed days from balance date. This compares with the current statutory requirement for State agencies to submit financial statements to my Office within 8 weeks (56 days) from balance date.

2.31 **In the context of these trends, and the Victorian public sector experience to date, it is important that avenues are actively identified and pursued to improve the timeliness of the financial reporting process.**

Recommendations

2.32 **We recommend:**

- **The earlier completion of major asset and liability valuations (such as major non-current physical asset and actuarial valuations), and key account reconciliations;**
- **For departments, the earlier completion of the appropriation certification process by the Department of Treasury and Finance; and**
- **The introduction of earlier/interim account "close-offs" by entities. International better practice indicates that an early "close-off" achieves significant time and resource savings at year-end. This process assists in the earlier identification and resolution of any major contentious accounting and reporting issues.**

2.33 We will continue to work closely with entities and central agencies, to facilitate continuous improvement to the timeliness of financial reporting.

***RESPONSE** provided by the Secretary, Department of Treasury and Finance*

Para. 2.25

As indicated in figure 2C, this Report indicates that there was a significant improvement in the timeliness of Financial Statement completion in 2002-03.

This improvement indicates that departments and their portfolio entities have developed the necessary systems and hold the required expertise to complete this task in a timely manner. In addition, this process is facilitated by the development and application of various Model accounts, such as the "Model Financial Report for Victorian Government Departments", which is issued by DTF.

Paras. 2.31 and 2.32

DTF, in conjunction with the Auditor-General, is actively working to further increase the timeliness of financial reporting. This will be achieved through a variety of mechanisms which include, but are not limited to the timely completion of:

- *valuations;*
- *reconciliations; and*
- *formal interim "close-offs".*

Local government

2.34 Figure 2D illustrates the overall timeliness of entities within the local government sector in the completion of audited financial statements and, where applicable, performance statements during the 2001-02 and 2002-03 reporting cycles.

FIGURE 2D
TIMELINESS OF AUDITED FINANCIAL STATEMENT AND, WHERE APPLICABLE, PERFORMANCE STATEMENT COMPLETION WITHIN THE LOCAL GOVERNMENT SECTOR

Finalisation of audited statements (no. of months after end of financial period)	*2002-03*		*2001-02*	
	Number of entities	*Per cent (cumulative)*	*Number of entities*	*Per cent (cumulative)*
Less than and up to 3 months	96	95	75	76
3 to 4 months	2	97	17	93
Over 4 months	3	100	7	100
Total	**101**	**-**	**99**	**-**

2.35 **Figure 2D indicates there has been a significant improvement in the timeliness of completion of audited financial statements and, where applicable, performance statements by local government entities. Ninety-five per cent of local government entities completed their 2002-03 statements within the statutory 3-month period, compared with 76 per cent in 2001-02.**

2.36 The major factors contributing to this improvement in timeliness were similar to those previously mentioned for other public sector entities.

Quality of financial reporting

2.37 **The overall quality of financial statements submitted for audit has improved over recent years**. The development and refinement of model financial reports produced by the various "industry sectors", such as the water sector, has been a major contributor to this improvement. These model accounts have facilitated increased awareness across agencies of the relevant disclosure and reporting requirements, together with greater consistency of reporting within the relevant sectors. **However, there continues to be scope for various agencies to improve the financial statement preparation process.**

Recommendations

2.38 **We recommend that entities strengthen their:**

- **year-end planning**, including the establishment of clear timelines for the preparation and availability for audit of key reconciliations and other supporting information;
- **finance function capability**, ensuring the availability of sufficient and appropriately skilled resources to facilitate the timely preparation of draft financial statements; and
- **quality assurance processes**, ensuring that the draft financial statements submitted for audit are complete, free of material errors and internally consistent.

2.39 Where financial reporting processes were assessed as requiring improvement, recommendations were made to the respective agencies for enhancing the efficiency of such processes.

Adequacy of control environment

2.40 While the principal purpose of financial statement audits is to add credibility to the financial accountability process (the audit opinion), the audit also assesses the adequacy of the management control environment that includes controls over:

- compliance with legislation;
- payroll, payments, revenue, assets and liabilities; and
- information technology.

2.41 While deficiencies in the internal control environment may not result in the issue of an audit qualification, they are referred to the agency for appropriate remedial action. In this regard, our observations arising from the financial statement audit process, including those relating to the adequacy of the internal control environment are summarised later in this report. A high level summary of these observations and recommendations is provided below.

2.42 **Our 2002-03 financial audits confirmed that public sector entities had maintained relatively effective systems of internal control over the financial and information technology systems impacting on the preparation of their financial reports. Opportunities were identified, however, for some agencies to further improve the effectiveness of their management and internal control processes.** Among the more significant issues identified were:

- slow progress in the development of integrated risk management frameworks;
- deficiencies in information technology environments, including concerns on long-term strategic planning and computer security;
- inadequate reconciliation and review procedures relating to key accounting systems, including payroll, accounts payable and receivables systems;
- poor controls over critical data held in IT master files of key accounting systems; and
- need for improved asset valuation and management practices.

2.43 Many of these issues are not new and represent matters that we have raised with agencies over many years. **While the responsiveness of individual agencies to addressing specific issues has been mixed, we have observed an increasing awareness across the public sector of the need for sound risk and financial management practices. In turn, this is helping focus greater attention to the issues raised - given their potential impact on the accuracy and integrity of financial and other information being produced by major accounting and support systems.**

2.44 In this environment, we expect that continuing attention will be given by agency management and audit committees to ensuring the timely resolution of the matters raised by audit. The need for agency attention will be further reinforced by the implementation across the public sector, as from 2003-04, of the Government's Financial Management Compliance Framework (further comment on this framework is provided later in this part of the report).

2.45 Figure 2E provides a further summary of the control and management issues identified, which were common to a number of entities. While the frequency of occurrence varied, where the issues are considered to be of particular significance, further comment is provided following Figure 2E.

FIGURE 2E
COMMON AUDIT ISSUES IDENTIFIED AND REPORTED DURING THE 2002-03 FINANCIAL AUDIT CYCLE

Subject area	*Issues identified*
Governance and risk management	• Slow progress in the development of integrated risk management frameworks. • Lack of formalised fraud prevention strategies. • Absence of, or ineffective, audit committees and internal audit functions.
Financial management and reporting	• Further deterioration in the financial standing of certain public hospitals/health services *(a).* • Concerns with the financial viability of certain municipal councils *(a).*

FIGURE 2E - *continued*
COMMON AUDIT ISSUES IDENTIFIED AND REPORTED DURING THE 2002-03 FINANCIAL AUDIT CYCLE

Subject area	*Issues identified*
Information technology (IT) control environment	• Business continuity and disaster recovery plans either not developed or formalised, and associated procedures not tested. • Inadequate IT change management procedures over systems and applications. • Absence of current formalised IT strategic plans. • Insufficient security management policies and procedures. • Inadequate security controls governing access over IT systems and financial applications.
Revenue and accounts receivable	• Absence of formal debt collection policies and procedures. • Inadequate controls over the issue of credit notes. • Debtor ledgers not reconciled with general ledger and lack of independent review of debtor's reconciliations.
Expenditure and accounts payable	• Need to amend errors in standing data held on masterfiles, including instances of duplicated supplier details. • Inadequate procedures for updating of masterfile information. • Lack of independent review over payables reports and reconciliations with general ledger.
Payroll and related employee benefits	• Concerns with the accuracy of information held on employee masterfiles. • Lack of independent review over payroll reports and reconciliations with general ledger. • Accumulation of excess annual leave entitlements.
Asset management	• Better management practices not followed in relation to plant and equipment items, including the conduct of regular stocktakes and the re-assessment of asset condition/asset lives. • Annual re-assessments of property valuations not undertaken. • Asset registers not accurately maintained. • Lack of formal review of appropriateness of capitalisation thresholds and depreciation rates.

(a) Detailed comment on these issues is provided in the Human Services and Local Government sections of this report.

Governance and risk management

Progress in developing risk management frameworks

2.46 Our March 2003 report *Managing risk across the public sector* outlined the results of a performance audit undertaken to assess the current status of risk management within the Victorian public sector, including whether:

- public sector agencies have established appropriate risk management strategies, which are effectively implemented and strategically managed; and
- risk management is effectively integrated into the governance and management structures of government agencies.

2.47 The audit covered 61 agencies across all ministerial portfolios, including departments, statutory authorities, education institutions, health service agencies, water authorities and other small agencies. It concluded that most of the selected agencies were addressing risk management in some way, but risk management had not yet been established as a mature business discipline. It also found that around one-third of the organisations reviewed did not explicitly identify and assess their key risks, and that organisations did not always report risk information to their key internal and external stakeholders.

2.48 **Our 2002-03 financial audit round confirmed the conclusions drawn from this earlier review. We found that there was general recognition and support across the public sector for the need to implement appropriate risk management frameworks as an integral part of agency governance structures. However, there remained some agencies that were yet to introduce such frameworks.**

Recommendations

2.49 **We recommend that:**

- **all public sector agencies should adopt formal risk management approaches that are appropriate to the agencies' level of risks; and**
- **audit committees play a key role in assessing and monitoring the effectiveness of the risk management process.**

Fraud prevention and detection

2.50 Fraud is one of many risks faced by agencies requiring careful management to minimise potential loss. Development of an appropriate policy to address fraud prevention is likely to provide an effective tool for minimising opportunities to engage in fraud. The establishment of sound fraud control procedures as an integral part of each agency's risk management strategies will assist in the effective management of this risk.

2.51 Australian Auditing Standard AUS 210: *The Auditor's Responsibility to Consider Fraud and Error in an Audit of a Financial Report* requires auditors, as part of the financial audit process, to assess the risk of material misstatement resulting from fraud and error. However, ultimate responsibility for the prevention and detection of fraud and error remains with agency management.

2.52 In assessing the potential for fraud and error, and establishing appropriate management arrangements, each agency should consider:

- conduct of an environmental scan to determine the internal and external influences impacting on the occurrence of fraud and error;
- development and implementation of an agency-wide fraud prevention and detection strategy;
- assignment of responsibilities for co-ordination and monitoring compliance with the agency strategy;

- supporting the agency strategy with appropriate communication policies, response procedures and training programs; and
- the potential for fraud and error arising from the introduction of new technologies.

2.53 **During the 2002-03 financial audit round, we identified many instances where agencies had not yet established formal fraud prevention and detection strategies as part of the wider risk management processes.**

Recommendation

2.54 **We recommend that agencies develop fraud prevention and detection strategies, including appropriate treatment plans to minimise the risk of fraudulent activity.**

Audit committees

2.55 The existence of an effective audit committee plays an important role in assisting boards or accountable officers to fulfil their governance responsibilities. The essential features of an effective audit committee include:

- membership comprising independent, non-executive (board) members who possess the necessary skills in finance, management and industry;
- the committee formally meeting and reporting to the board (or accountable officer) on a regular basis; and
- reports of the committee to the board providing a summary of the committee's work and results, including formal resolutions, recommendations requiring action and/or approval, and information pertaining to the external and internal audit process.

2.56 Specific responsibilities of the audit committee may include:

- considering the appropriateness of an entity's accounting policies and principles;
- recommending to the board (or accountable officer) whether financial statements should be signed;
- ensuring the entity has in place, effective internal control and risk management procedures;
- liaising with external auditors, and investigating audit issues and findings;
- overseeing the activities of internal audit, including monitoring management's responsiveness to internal audit findings and recommendations; and
- receiving from management, reports on all suspected and actual frauds, thefts, and legislative breaches.

2.57 The 2002-03 financial audit cycle identified a number of instances where agencies had either not established audit committees, or where the effectiveness of audit committee operations could be enhanced. Among the issues identified were the need for greater independent/external representation on committees, lack of appropriate experience and knowledge of some committee members, need to maintain appropriate records of committee meetings and resolutions, and the need to broaden committee charters beyond a narrow financial focus.

Recommendation

2.58 **We recommend that agencies give greater attention to ensuring that audit committees are established and operate in accordance with better practice.**

Information technology (IT) control environment

2.59 Our previous reports have commented on the outcomes of information technology (IT) reviews, undertaken as part of the annual financial audit process. As part of the 30 June 2003 and 31 December 2002 financial statement audits, we conducted IT reviews across agencies that use significant IT systems. A summary of the key findings arising from these reviews follows.

2.60 The IT reviews assessed the adequacy and effectiveness of controls within the computer environments, focusing on systems that produce financial reporting information. The scope of each review is dependent on the size and nature of the organisation, the risks inherent in their specific computer environment and the results of any prior period reviews.

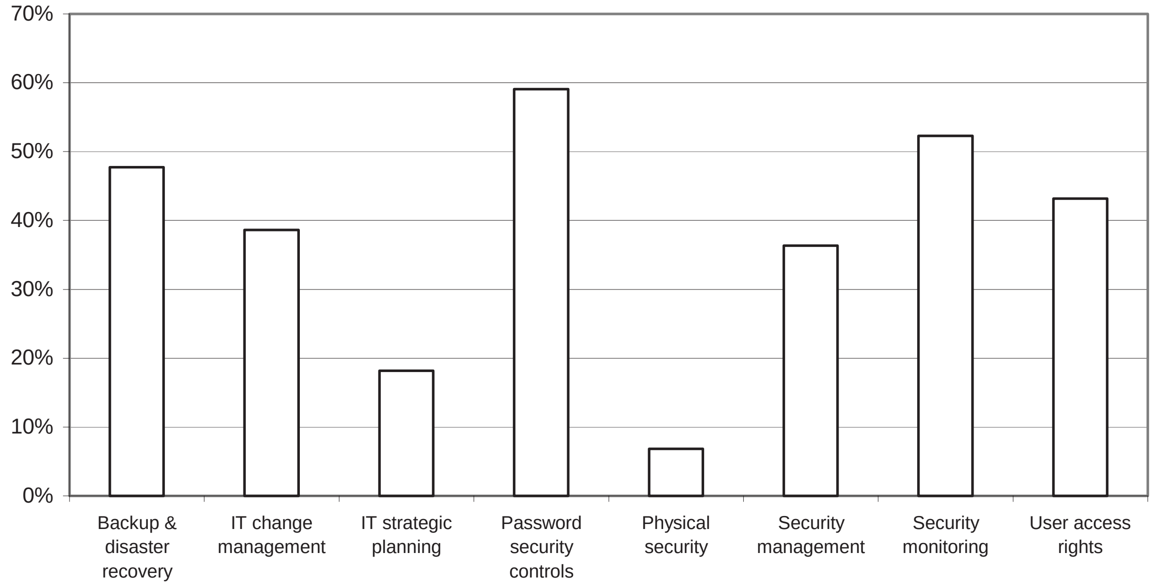
2.61 Elements of control over specific financial systems such as IT security, change management and recovery capability, as well as organisation-wide IT governance, were addressed as part of these reviews. These controls are critical in ensuring the confidentiality and integrity of organisational systems and data, particularly given the greater use of the internet to deliver services within government.

2.62 **We found that, during 2002-03, many of the agencies subject to review had addressed key weaknesses in controls or practices that were identified in the previous year. However, there remained a continuing need for agencies to examine and review controls across all critical aspects of their IT operations.**

2.63 **In particular, we found a need for agencies to develop and maintain comprehensive policies and procedures for the management of their computer environments and the use of IT resources. For example, many agencies had not adequately addressed key areas of security management, including security arrangements operating over specific financial systems, as well as business continuity planning.**

2.64 Figure 2F summarises key issues raised by my Office across 44 agencies in 2002-03.

FIGURE 2F
IT REVIEWS – SUMMARY OF ISSUES IDENTIFIED
(percentage of agencies where issues raised)



2.65 Further comment on certain of the issues identified follows. Specific recommendations have been made to the relevant agencies.

Business continuity and disaster recovery planning

2.66 With increasing dependence on information technology, the ability of agencies to recover their IT systems in a timely manner following a major system interruption or disaster is becoming increasingly important. To manage the associated risks, agencies should have in place formal business continuity and IT disaster recovery plans, which detail the necessary steps for recovering their systems within identified timeframes. Features of good business continuity and disaster recovery planning include:

- identification of key business process, whether IT or not, that would impact on the agency’s ability to continue to operate, and strategies to continue client services;
- formal assessments of the business impact of a loss of key IT systems;
- identifying the provision of alternative processing sites (where this is assessed as necessary to recover systems and data within critical time frames), and manual processes to provide limited operational capability during interim periods until system recovery occurs;
- periodic and formal testing of disaster recovery plans; and
- regular updating of plans to reflect changes to IT systems and business processes.

2.67 While all the agencies reviewed during the recent audit cycle had implemented procedures to regularly back-up key financial data, we found that many still required improvements in business continuity and disaster recovery planning. More specifically, 21 of the agencies reviewed (48 per cent) were found to require improvements in this area, with many yet to develop formal procedures for their critical business processes and systems. Other issues identified included the lack of formal testing of plans, as well as instances where plans were not updated to reflect the agencies current IT infrastructure, staff responsibilities and systems.

Recommendation

2.68 **We recommend that agencies assess their business continuity preparedness, including IT, and develop or review and test appropriate business continuity plans.**

IT change management

2.69 Information technology changes in the form of upgrades or modifications to financial applications or systems are a source of risk that should be managed in a controlled and structured manner. Agencies should have in place policies and procedures for:

- formal project planning for major system implementations or upgrades;
- approval of all requests for changes to systems and application software;
- testing of changes utilising separate test systems or environments;
- segregation of duties within the software development and maintenance process;
- appropriate formal training to users following systems changes; and
- communication of change processes.

2.70 While the majority of agencies reviewed during the period were found to have established sound change management practices, 17 agencies (39 per cent) were assessed as having weaknesses requiring attention, including:

- inadequate documentation of change management procedures;
- inadequate testing practices and insufficient project implementation documentation;
- lack of management approval of IT changes; and
- poor segregation of incompatible duties within the development process.

Recommendation

2.71 **We recommend that agencies develop appropriate change management policies and procedures for IT systems changes.**

IT strategic planning

2.72 Formal IT strategic planning assists in ensuring that IT activities are consistent with the overall objectives and business needs of the organisation. Agencies should have in place processes to assist in strategically managing their IT resources, including:

- the development of a formal IT strategic plan linked to the agencies' business objectives;
- regular monitoring of IT activities against the objectives set out in the IT strategic plan; and
- establishment of a formal IT steering committee with appropriate senior management representation.

2.73 Issues relating to IT strategic planning were identified in 8 of the agencies reviewed (18 per cent), the majority of which related to failure of agencies to maintain a current formal IT strategic plan. We also noted that the majority of these agencies (71 per cent) lacked other key IT policies and procedures, such as those addressing business continuity and IT security.

Recommendation

2.74 **We recommend that agencies develop an appropriate IT strategic plan that outlines the high level IT objectives and strategies of the agency over the medium to long term.**

Password security controls

2.75 Password security controls are one of the primary means of restricting access to information systems. It is, therefore, critical that good practices are applied in the development and enforcement of agency policies for the use of passwords. Failing to do so increases the risk of unauthorised access to IT systems and resources.

2.76 Improvements to password security were identified in most agencies reviewed (26 agencies, or 59 per cent). The impact of residual weaknesses varied in each case, and included:

- no requirements for users to periodically change their passwords;
- instances where passwords were not required for users to access critical systems;
- instances of generic or shared user accounts; and
- inconsistent application of password policies.

2.77 We also noted that limitations within some financial systems meant that good password practices could not be enforced.

Recommendation

2.78 We recommend that agencies regularly review and update their password security policies. Where systems limitations do not enable good password protection, appropriate policies should be implemented to ensure that the selection of passwords by users is sufficiently complex and passwords are manually changed on a regular basis.

Security management

2.79 Information security management protects an organisation's key information and data. Agencies need to have in place a framework to initiate and control the implementation of information security.

2.80 We observed a number of good practices during our reviews, including:

- development of security policies and procedures in accordance with recognised standards;
- establishment of formal information security forums to discuss key security issues and concerns, with representation across the agency;
- implementation of independent reviews of security over specific systems and security management; and
- communication of information security requirements to staff through internal staff awareness and induction programs.

2.81 We noted that the awareness of security-related issues across agencies had increased over the past 2 years. However, improvements to information security management policies and procedures were still identified at 16 agencies (36 per cent). These issues included:

- the absence of formal policies and procedures in relation to information security;
- pre-existing policies and procedures had not been updated to reflect current risks, or had not yet been endorsed by management; and
- policies and procedures did not address all relevant security issues.

Recommendation

2.82 We recommend that agencies review their security management policies and procedures so that they reflect best practice.

Security monitoring

2.83 To assist in protecting agency computer systems against security threats, formalised procedures should be implemented to regularly log and monitor security-related activity across the organisation. Monitoring contributes significantly to the ability of organisations to detect and respond to unauthorised activity within key information systems and applications.

2.84 While some of the agencies reviewed had implemented sound practices in security monitoring, 23 of the agencies (52 per cent) we examined require improvement in areas including:

- monitoring of failed access attempts to key systems and applications; and
- monitoring of privileged user access.

Recommendation

2.85 **We recommend that agencies institute appropriate procedures to monitor security related activity.**

Managing user access rights

2.86 The process for managing the registration, modification and removal of user access privileges to systems, including financial applications, is critical from a security perspective. If these tasks are not adequately controlled, there is an increased risk of unauthorised users gaining access to systems.

2.87 In 19 of the agencies reviewed (43 per cent), the management of user access rights in relation to specific systems was found to require improvement. Some of the major concerns included:

- no documented policies and procedures for managing user registration and removal;
- the lack of periodic review of users with access to specific information systems; and
- users with access levels in excess of their job requirements.

Recommendations

2.88 **We recommend that agencies:**

- **develop appropriate policies and procedures for managing user access rights; and**
- **periodically review levels of user access.**

Expenditure and accounts payable

2.89 In 2002-03, approximately $13 billion was spent on the purchase of goods and services across government. Given the significant and emerging technological developments impacting on this important activity, it is important that effective control environments are established by agencies which ensure that:

- only authorised payments are made, particularly where there is devolved responsibility for aspects of the purchasing and accounts payable functions;
- there is compliance with legislative requirements, government policy and other relevant procedures;
- any potential financial savings are realised through the use of innovative purchasing strategies;

- sound systems are in place to gather cost information in a form conducive to further analysis and effective management; and
- internal policies have been developed to minimise the potential for fraudulent activity.

2.90 **Our examination of agency purchasing and accounts payable functions during the 2002-03 financial audit cycle did not reveal any significant internal control deficiencies. We found that agencies had established appropriate policies and procedures for the ordering, receipt and payment of suppliers.** However, we did identify a number of recurring instances of less significant internal control deficiencies, including:

- need to eliminate duplicate suppliers from data held on master files;
- inadequate procedures for the updating of master file information;
- lack of independent review of payables reports and reconciliations with the general ledger; and
- inadequate procedures relating to the usage of credit cards by agency staff, including a lack of authorisation and monitoring of credit card transactions.

2.91 Where agencies fail to maintain an effective control environment over purchasing and accounts payable, the following major risks are increased:

- unauthorised or duplicate payments may be made;
- the accuracy or completeness of financial records may be impaired; or
- non-compliance with legislation, such as GST, may occur.

2.92 Specific recommendations have been made to the relevant agencies for improvements to their purchasing and accounts payables procedures.

Recommendation

2.93 **We recommend that agencies focus attention on ensuring the accuracy and integrity of information held on supplier master files, and the timely completion of appropriate accounts payable review and reconciliation procedures.**

2.94 As part of our 2003-04 work program, we intend to examine in greater detail the management of purchasing and accounts payable across the public sector, with the results of this work to be reported to Parliament during the 2004 Autumn Session.

Payroll and related employee benefits

2.95 Employee-related costs represent one of the largest items of expenditure, totalling approximately $10 billion in 2002-03. These costs are mainly for employee salaries, wages and related items.

2.96 Our March 2003 report to Parliament, *Control and compliance audits (Payroll management and Administration of the goods and services tax)*, outlined the results of a study conducted by my Office earlier this year, which assessed the effectiveness of payroll policies and procedures across 17 public sector agencies.

2.97 The main conclusion drawn from the study was that the agencies, comprising all departments and a small number of other agencies, had "… sound policies and practices in place to control the payroll function". However, opportunities were identified to further strengthen payroll management through regular cost-benefits analysis of potential alternatives, a more systematic approach to assessing processing risk, provision of additional policy and procedural guidance, introduction of additional control processes, and a greater emphasis on independent monitoring and review of payroll information.

2.98 The results of our examination of payroll controls during the 2002-03 financial audit cycle were consistent with the earlier report findings. **We found that payroll controls were generally adequate, but a number of recurring concerns had been identified across agencies, including:**

- **concerns associated with the accuracy of information on electronic employee master files;**
- **lack of independent review of payroll reports and reconciliations with the general ledger; and**
- **accumulation of excess annual leave entitlements.**

2.99 Failure by agencies to maintain an effective control environment over payroll functions increases the risk of:

- inaccurate or inappropriate payments to employees;
- potential for fraud or misappropriation of funds; and
- increased employee costs, due to excessive retention of annual leave entitlements arising from increasing hourly rates of pay and decreased productivity.

Recommendation

2.100 **We recommend that to minimise the impact of these potential risks:**

- **agencies further strengthen the controls over their payroll environment, with particular attention to be given to ensuring the accuracy of information held in computerised employee master files; and**
- **employees be encouraged to utilise their annual leave entitlements on a more timely basis.**

Asset management

2.101 A major responsibility of agencies is the management of the physical assets they control, which may include land, buildings, roads, infrastructure systems, plant and equipment and cultural assets. Agencies are required to manage their assets efficiently and effectively, in accordance with various Government asset management policies, guidelines and directives. For financial reporting purposes, agencies are also required to account for these assets in accordance with Australian Accounting Standards, which establish requirements for such matters as the assessment of asset useful lives and the revaluation of assets.

2.102 In the context of the current reporting framework, accounting for property, plant and equipment can be extremely challenging for agencies. In confirming the existence and valuation of assets controlled by agencies, our audit procedures are designed to detect significant control deficiencies and accounting/financial reporting errors. The main audit procedures are:

- review of compliance with agency policies and procedures, including capitalisation thresholds, asset disposals, asset stocktakes, depreciation and valuation;
- verification of significant asset additions and disposals to supporting documentation including contracts, invoices/progress claims, etc.;
- evaluation of physical stocktake results to confirm existence and ownership;
- for infrastructure assets, consideration of appropriateness (and consistent application) of valuation methodologies; and
- examination of asset revaluations and annual interim reassessment of valuations with reference to movements in market prices.

2.103 **During the 2002-03 financial audit cycle, we found that agencies had generally complied with the requirements of Australian Accounting Standards. However, we identified a number of concerns over the internal controls and management practices in some agencies.** Some of the more common issues reported were:

- failure by certain agencies to obtain current "fair values" for property assets through the conduct of formal revaluations or annual (interim) reassessments, as required by the accounting standards;
- absence of formal asset policies in relation to the conduct of physical stocktakes and the disposal of surplus or obsolete items;
- inaccurate assessments of asset useful lives, resulting in items with "nil" written-down values but still in use within agencies; and
- inadequate procedures for the timely transfer of completed projects from capital works in progress to asset accounts, resulting in inaccurate depreciation charges in the year.

2.104 Specific recommendations have been made to the relevant agencies on these issues.

Recommendation

2.105 **We recommend that agencies review the adequacy of existing policies and procedures dealing with asset capitalisation thresholds, depreciation charging, re-valuation processes and project management.**

EMERGING ISSUES FOR 2003-04

2.106 This section discusses a number of recent developments requiring attention that will impact on public sector financial reporting and accountability over future financial periods.

Harmonisation of accounting standards

GAAP/GFS convergence

2.107 The Financial Reporting Council, which is responsible for the broad oversight of the accounting standard setting process in Australia, announced in December 2002 that the Australian Accounting Standards Board (AASB) would examine the harmonisation of Government Finance Statistics (GFS) and the Australian Generally Accepted Accounting Principles (GAAP) reporting frameworks.

2.108 GFS is the reporting framework promulgated by the International Monetary Fund to allow economic analysis of the public sector. To date, GFS is mainly used by central agencies to report at the whole-of-government or General Government Sector levels. Differences between the GFS and GAAP frameworks, in the classification and treatment of certain transactions, can yield quite different results in terms of the reported operating performance and net worth of governments.

2.109 The objective of the convergence process is to explore the potential to develop an Australian Accounting Standard that will provide for the preparation of financial reports that are comparable between jurisdictions and which are also directly comparable with the relevant budget statements. The AASB has agreed that the convergence process will be implemented in 3 phases, with the first phase focusing on general purpose financial reporting by State, Territory and Commonwealth governments, the second phase concentrating on reporting by entities within the General Government Sector and the third phase dealing with general purpose financial reporting by other public sector agencies.

2.110 The AASB has advised its intention to issue an issues paper in the near future reflecting the convergence process.

Adoption of international financial reporting standards by 2005

2.111 In July 2002, the Financial Reporting Council also announced that the AASB would work towards the adoption of international accounting standards for reporting periods commencing on or after 1 January 2005. The decision was made in response to increased demand for high quality, internationally comparable financial reports.

2.112 The AASB will issue Australian standards through the development of Australian equivalents of the international standards. These standards will adopt the content and wording of the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB). The Australian standards will be sector neutral and will, therefore, also apply to the public sector and incorporate any standards issued by the International Federation of Accountants (IFAC) Public Sector Committee. Changes in wording will be limited to accommodating the Australian legislative environment and any broader requirements for the public sector and the not-for-profit sector, which is currently not covered by the scope of the IASB standards.

2.113 The AASB plans to retain or develop additional standards, when required, to cater for domestic issues.

2.114 The move to adopting international accounting standards represents the largest change to accounting in Australia for many years. While Australia has been harmonising its accounting standards with the international standards since 1997, the adoption of the IFRS will significantly impact on the financial reporting landscape in Australia because:

- differences still remain between the harmonised Australian standards and the international standards;
- the current Australian standards do not address a number of issues, such as the recognition and measurement of financial instruments, intangible assets, investment property and accounting for post-employment benefits; and
- there will be further changes to the international standards before 2005, which will also need to be incorporated into the Australian equivalents.

What are the key impacts of adoption of international standards?

2.115 The new IFRS equivalent standards will apply to all reporting entities, including the public sector and not-for-profit entities. In particular, reporting entities will be required to prepare their financial reports for reporting periods beginning on or after 1 January 2005, including prior year comparatives, in accordance with the new standards. This means that the new standards must be reflected in financial reports for periods:

- ending on 31 December 2005 with comparatives for 31 December 2004; or
- ending on 30 June 2006 with comparatives for 30 June 2005.

What has been the central agencies' response to these changes?

2.116 The adoption of IFRS in public sector reporting and the possible harmonisation of GFS and GAAP have wide-ranging implications for public sector entities. The Department of Treasury and Finance has established a project team with responsibility for the identification of the significant issues for Victoria arising from these changes, and the development of appropriate communication and implementation strategies. This will be done in conjunction with relevant senior financial staff of the affected departments and agencies, and with the co-operation of our Office.

2.117 The Department is also a member of a working party, together with other Australian jurisdictions which has been exploring the issues involved in the harmonisation of GAAP and GFS, and has made a number of recommendations to the AASB on ways to progress harmonisation. The project team will also prepare for the implementation of the standard arising from this harmonisation process.

2.118 **We are supportive of these initial steps taken by the Department of Treasury and Finance to establish a leadership role within the Victorian public sector. However, it is important that the implementation strategies be closely monitored to ensure that agencies, particularly non-departmental and the smaller agencies, gain an adequate and timely understanding of the major changes and their implications.**

What should individual agencies be doing now?

2.119 Surveys within the accounting profession have consistently indicated a lack of detailed understanding of the implications of the changes and the action entities needed to take to achieve compliance.

Recommendation

2.120 **While there is an awareness of the new standards, we recommend that agencies consider:**

- **the likely effects of the changes on financial budgeting, workloads, report presentation and relationships with stakeholders;**
- **the conduct of a gap analysis to identify any new information needs and any changes to systems and processes that may be required to ensure the necessary information is collected and internal reporting is aligned with the new requirements;**
- **development of a training strategy to ensure a sound understanding of the new requirements underpinning the change to IFRS; and**
- **how the board, audit committees and other governance committees are kept abreast of the developments.**

RESPONSE *provided by the Secretary, Department of Treasury and Finance*

DTF is aware of the significant task ahead involving the harmonisation of accounting standards and, as noted in the report, has already established a project team. DTF is currently undertaking a strategic analysis of these significant accounting changes and the impact they will have on Victoria. In addition, DTF is also evaluating the most appropriate implementation approach to ensure these changes to accounting standards are implemented in a timely and efficient manner whilst maximising the integrity of financial reporting in Victoria.

Financial management compliance framework

2.121 Following a major development and consultative process over the past 2 years, the Minister for Finance in early July 2003 issued a revised package of Ministerial Directions and introduced a new Financial Management Compliance Framework.

2.122 The revised Ministerial Directions are operative from 1 July 2003 and include many changes in the financial management obligations of public sector agencies. These include the introduction of strengthened requirements in the area of financial management governance and oversight - a development that my Office has strongly supported. All Victorian public sector agencies which are subject to the *Financial Management Act* 1994 are required to comply with all new Ministerial Directions as from 1 July 2003. An exemption from full compliance with the Directions included in Part 2 (Financial Management Governance and Oversight) of the package is provided until 1 January 2004. This exemption only applies if agencies are "*… in good faith complying with each of those Directions to the greatest extent reasonably possible*".

2.123 A significant element of the new reforms is the introduction of complementary Financial Management Compliance Framework, which will provide a mechanism through which the Government can monitor and review compliance with its legislative and regulatory financial management structure.

2.124 The compliance reporting regime commences in 2004-05, in relation to compliance achieved during 2002-03, and is mandatory for all entities forming part of the economic entity of the State of Victoria, as identified in the Government's Annual Financial Report. It does not include local government entities, universities and denominational hospitals.

2.125 The Department of Treasury and Finance has fostered awareness of the changes across the public sector, through the conduct of statewide workshops and the development of an internet-based knowledge base.

Recommendation

2.126 **Given the major changes to the financial management obligations of Victorian public sector agencies, we recommend all agencies develop a clear understanding of the changes and their implications at the earliest possible opportunity so that the necessary strategies are established to ensure agency compliance with the new requirements.**

***RESPONSE** provided by the Secretary, Department of Treasury and Finance*

As identified in the report, a major initiative of the Government has been the development and implementation of the Financial Management Compliance Framework (the Framework).

RESPONSE *provided by the Secretary, Department of Treasury and Finance - continued*

In July 2003, the Minister for Finance, officially launched the Framework to Victorian Public Sector (VPS) entities. The launch was consistent with the Government's ongoing commitment to responsible financial management. The Framework provides a mechanism by which the Government can effectively monitor and review compliance with the Standing Directions and is operative for reporting periods commencing 1 July 2003.

The Framework provides assurance that VPS entities have implemented appropriate systems to ensure effective, efficient and responsible financial management of public resources. A key component is an annual certification by VPS entities that they are complying with its provisions and in particular the provisions of the Standing Directions.

The Framework is based on leading practice Australian Standard AS3806 'Compliance Programs' which sets out objective benchmarks for corporations in designing, implementing and maintaining effective compliance programs. It consists of five key elements (culture and commitment, systems and procedures, resourcing and responsibilities, reporting and maintenance).

Prior to the launch of the Framework, DTF implemented a wide ranging Communication Strategy to inform and educate all relevant stakeholders about the requirements of the Framework and continues to maintain a web based knowledge centre, incorporating an Issues Management System, enabling VPS entities to contact DTF and /or other departments with any issues they may have encountered.

Standing Directions of the Minister for Finance

In June 2003, the Minister for Finance issued a revised set of Standing Directions of the Minister for Finance (the Directions). The new Directions prescribe best practice, high-level requirements for modern financial management and allow entities to tailor the various financial procedures and practices to suit their own organisational requirements. Furthermore, a number of the Directions have been strengthened, ensuring that VPS entities continue to practice leading edge financial management.

In relation to the Report, the Directions cover specific issues including:

- *Risk Management (Ministerial Direction 2.3);*
- *IT control environment (Ministerial Direction 3.2);*
- *Revenue and accounts receivable (Ministerial Directions 3.1.3 and 3.4);*
- *Payroll and related employee benefits (Ministerial Direction 3.4.7); and*
- *Asset Management (Ministerial Direction 3.4.9).*

Although the Report identifies some areas of significance, it does indicate that there has been increasing awareness across the public sector of the need for sound risk and financial management practices. DTF would emphasise that the government has in place appropriate mechanisms and frameworks to strengthen financial management practices, and agrees with the Auditor-General, that the public sector has maintained effective systems of internal control over the financial and information technology systems impacting on the preparation of financial reports.

Impact of recent Audit Act 1994 amendments

2.127 In June 2003, Parliament passed a wide range of amendments to the *Audit Act* 1994, focusing on the strengthening of the legislative framework for the Auditor-General. An important aspect of these amendments was the expansion of the definition of an "authority" subject to the Auditor-General's mandate to encompass entities controlled by the State or other authorities. For the purposes of the Act, the definition of control was linked to the meaning set out in the relevant accounting standards.

2.128 While previously the State had to fully own companies before they could be subject to audit by the Auditor-General, under these amendments all entities deemed to be controlled either by the State or another authority become subject to my mandate. Under transitional provisions, these amendments do not take effect for entities falling within the widened definition until the end of the term of appointment of an entity's existing auditor.

2.129 The amendments are welcomed and will facilitate strengthened accountability arrangements for controlled entities that are less than 100 per cent owned by, or on behalf of, the State. During the coming year, we will work closely with the relevant public sector entities to give effect to the legislative amendments by establishing the necessary audit arrangements.

Part 3

Summary of audit results and special reviews – by sector

INTRODUCTION

This part of the report outlines the results of our audits of the financial and other accountability statements of entities with 30 June 2003 balance dates, for Parliament and each of the major sectors of government activity.

Comment is also included on the more significant matters identified during the audit process, together with the results of a number of special reviews into matters of public interest.

Each section is similarly structured to include a brief overview of the responsibilities and activities of the respective sector/portfolio, together with commentary on the:

- nature of audit opinions issued on entities' financial statements and, in the case of municipal councils, performance statements;
- timeliness of financial statement completion by portfolio entities;
- adequacy of the control environments and systems of internal control operating within portfolio entities;
- other issues of significance identified during the audit process; and
- the results of any recently completed special reviews.

Part 3.1

Parliament

OVERVIEW

3.1.1 The Parliament of Victoria comprises the Crown (represented by the Governor), and 2 Houses, namely, the Legislative Council and the Legislative Assembly, which collectively form the legislature.

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

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

3.1.4 The Victorian Auditor-General is an independent Officer of the Parliament appointed under the State's Constitution. The financial reporting requirements of the Victorian Auditor-General's Office are set out in section 7B of the *Audit Act* 1994. The financial statements of the Office must comply with section 49 of the Financial Management Act.

RESULTS OF FINANCIAL AUDITS

Timeliness of reporting

3.1.5 Figure 3.1A outlines the performance of Parliament and the Office of the Auditor-General in meeting the reporting timetable for 2002-03.

FIGURE 3.1A
TIMELINESS OF FINANCIAL STATEMENT COMPLETION

Finalisation of audited financial statements (no. of weeks after end of financial period)	*2002-03*		*2001-02*	
	Number	*Per cent (cumulative)*	*Number*	*Per cent (cumulative)*
Less than 8 weeks	-	-	-	-
8 to 10 weeks	2	100	-	-
10 to 12 weeks	-	-	1	50
12 to 14 weeks	-	-	1	100
Total	**2**	**-**	**2**	**-**

(a) The Victorian Auditor-General's Office was audited by a private sector auditor.

Adequacy of control environment

3.1.6 A report by the Auditor-General on Parliament's information technology upgrade was tabled in Parliament in September 2003. The report resulted from a review requested by the Speaker of the Legislative Assembly.

3.1.7 The report identified major issues associated with the management and oversight of the information technology project and the outcomes achieved from the project. The report also identified that, in part, the issues associated with the IT project were indicative of the need for improvement to the overall administrative framework and processes operating within Parliament.

3.1.8 Our financial audit confirmed many of the matters identified in that report and identified a range of additional control issues associated with the financial management of Parliament.

3.1.9 Parliament responded positively to the audit findings and is developing strategies aimed at addressing the issues identified. We will monitor Parliament's progress in implementing these strategies as part of the 2003-04 financial audit.

Part 3.2

Education and Training

PORTFOLIO OVERVIEW

3.2.1 The Education and Training portfolio comprises the Department of Education and Training, and other entities that provide, purchase and regulate education and training services for Victorians of all ages. These education and training services are delivered through schools, TAFE institutes, registered training organisations, adult education institutions, adult and community education providers,and higher education institutions. The Minister for Education and the Minister for Education Services have responsibility for the Department and specific responsibility for individual entities within the portfolio.

3.2.2 The majority of entities within the portfolio, including universities and TAFE institutes, have 31 December balance dates and are not covered in this report. The outcomes of these financial audits will be reported to Parliament during the 2004 Autumn Session.

3.2.3 Figure 3.2A provides the profile of portfolio entities with 30 June 2003 balance dates, for which we have audit responsibility.

FIGURE 3.2A
TYPE AND NUMBER OF AUDITED AGENCIES WITHIN THE EDUCATION PORTFOLIO, AT 30 JUNE 2003
(number)

Reporting entity	*Number*
Department	1
Public bodies *(a)*	6
Total	**7**

(a) Public bodies include statutory authorities such as the Adult, Community and Further Education Board and the Victorian Learning and Employment Skills Commission.

Source: Victorian Auditor-General's Office.

3.2.4 The Department's major responsibilities include:

- provision of primary and secondary education in government schools, and the regulation and funding of non-government schools in Victoria;
- planning, regulation, resourcing and purchasing of training and further education, apprenticeships and traineeships, and adult and community education, to meet the skill needs of individuals and industry; and
- planning, co-ordination and monitoring the provision of higher education in Victoria.

3.2.5 The activities of other portfolio entities with 30 June 2003 balance dates mainly relate to:

- the development of curriculum and the assessment of schools across all year levels;
- the provision of post-compulsory education and training in Victoria, including the accreditation of training qualifications and courses; and
- the regulation of the teaching profession.

3.2.6 Some of the key financial statistics associated with portfolio responsibilities include:

- parliamentary appropriations of $5.5 billion applied towards the provision of education and training outputs - representing around 23 per cent of total parliamentary appropriations applied across all portfolios;
- local fundraising activities by schools provided around $382 million in additional school revenues; and
- management of around 114 000 school buildings valued at $3.9 billion, located on 6 300 hectares of land which is valued at around $3.2 billion.

RESULTS OF FINANCIAL AUDITS

Audit opinions issued

3.2.7 Clear audit opinions were issued on the financial statements of all portfolio entities with 30 June 2003 balance dates.

3.2.8 The financial statements of a number of entities with 31 December 2002 balance dates, which were recorded as outstanding in our May 2003 *Report on Public Sector Agencies*, have since been finalised. Clear opinions were issued on all these financial statements, except for those of RMIT Union. These financial statements were qualified due to major deficiencies identified in the Academic Management System (AMS) used by the Royal Melbourne Institute of Technology, upon which the Union relies to produce elements of its financial statements. The deficiencies meant that the accounting records of the Union produced by AMS were not sufficiently accurate to enable an opinion to be formed on Union revenues and amounts receivable. A comprehensive report on the AMS system was included in our February 2003 *Report on Public Sector Agencies*.

3.2.9 "Emphasis of matter" comments were included in the audit reports of Monash Ed Pty Ltd and Monash Learningfast Pty Ltd, to draw attention to significant uncertainty as to whether these entities will continue as going concerns. An "emphasis of matter" comment was also included in the audit report of Monash Commercial Pty Ltd in relation to the uncertainty as to whether its controlled entity, Monash Learningfast Pty Ltd, will continue as a going concern.

Timeliness of reporting

3.2.10 Figure 3.2B outlines the performance of portfolio entities in meeting statutory reporting requirements during 2002-03.

FIGURE 3.2B
TIMELINESS OF FINANCIAL STATEMENT COMPLETION, EDUCATION PORTFOLIO *(a)*

Finalisation of the audited financial statements (no. of weeks after end of financial period)	*2002-03*		*2001-02*	
	Number	*Per cent (cumulative)*	*Number*	*Per cent (cumulative)*
Less than 8 weeks	-	-	-	-
8 to 10 weeks	-	-	-	-
10 to 12 weeks	3	43	-	-
12 to 14 weeks	2	71	4	67
14 to 16 weeks	1	86	1	83
More than 16 weeks *(b)*	1	100	1	100
Total	**7**	**-**	**6**	**-**

(a) Includes all audited financial statements as at 31 October 2003.
(b) Includes the financial statements of one entity that had not been finalised at the date of preparation of this report.
Source: Victorian Auditor-General's Office.

3.2.11 Figure 3.2B shows that, **while the timeliness of reporting by portfolio entities improved in 2002-03, only 3 entities (or 43 per cent) met the statutory 12-week completion timeframe (nil in 2002-03).** Appendix A to this report shows specific details of the financial statements and the audit opinions issued.

3.2.12 The key factors contributing to the failure by some agencies to meet the 12-week timeframe were:

- in the case of the Department:
  - delays experienced in obtaining approval from the Minister for Finance to vary the capital assets charge payable in the year (further comment is provided later in the report); and
  - delays in finalising certification of annual appropriation revenue; and
- a general lack of urgency by entities in preparing draft financial statements and in resolving financial issues identified during the audit process.

Quality of financial reporting

3.2.13 We found that the overall quality of financial reporting by entities within the portfolio was satisfactory during the 2002-03 financial audit cycle. Minor improvement opportunities identified during the audit processes were generally incorporated into the final financial reports.

Adequacy of control environment

3.2.14 A key responsibility of the management of each entity is to establish and maintain a sound control environment and an adequate system of internal controls to ensure that:

- the entity's financial records and other information completely and accurately reflected its activities;
- its assets are safeguarded; and
- irregularities are prevented, and detected and corrected should they occur.

3.2.15 Our 2002-03 financial audit process confirmed that the overall control environments within portfolio entities, and the associated systems of internal control subject to audit examination, were generally satisfactory. However, we did identify a number of opportunities to enhance the Department's information technology control environment, through:

- improved procedures to manage the registration, modification and removal of user access rights to information systems;
- reduction in the number of users with privileged security access rights;
- enhanced password security controls; and
- introduction of logging utilities to help detect unauthorised activity within information systems.

3.2.16 The matters raised were referred to the Department. We will review remedial action taken by the Department as part of our 2003-04 audit cycle.

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

The Department is pleased to note that the Auditor-General's finding that the overall control environments established within the portfolio were generally satisfactory. The relevant portfolio entities have noted the recommendations by the Auditor-General to further enhance the control environment and are taking steps to implement the suggested improvements.

Other issues of significance

3.2.17 Comments follow on a number of other issues of significance arising from the 2002-03 financial audit process.

Application of the capital assets charge

3.2.18 The capital assets charge is imposed annually by the Department of Treasury and Finance on all line departments, based on the written-down value of their non-current physical assets, with the aim of:

- attributing to departmental outputs the opportunity cost of capital used in service delivery;
- facilitating the full costing of outputs; and

- providing incentives to these agencies for the timely identification and disposal of under-utilised or surplus assets.

3.2.19 Under current Department of Treasury and Finance policy, departments are required to annually pay into the Consolidated Fund the capital assets charge, based on 8 per cent of the monthly written-down value of controlled non-current physical assets held.

3.2.20 As part of the 2002-03 budget process, the Department of Education and Training had estimated that it would incur a capital assets charge of $565.2 million for 2002-03. However, due to an increase in the actual value of the Department's assets (arising from the revaluation of land and buildings), the capital asset charge should have been $644 million for the year - an additional $78.5 million above the amount originally estimated. **As the Department was unable to absorb the additional expense within its budget, it obtained approval from the Minister for Finance to pay the charge based on the budgeted estimate of controlled non-current physical assets, rather than the actual value of those assets held during the year.**

3.2.21 **While the capital assets charge paid by the Department was consistent with that approved by the Minister for Finance, its downward revision to ease departmental budgetary pressures brings into question whether the intended objectives of the charge (from both financial and asset management perspectives) are being achieved.**

Recommendation

3.2.22 **We recommend that the operation of the capital assets charge be reviewed with a view to assessing its effectiveness in meeting its intended objectives.**

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

The Department notes the recommendation regarding the calculation and payment of the capital assets charge and is currently discussing these issues with the Department of Treasury and Finance.

Issues arising from school audits

3.2.23 The financial activities of State-run primary, secondary and special schools are consolidated into the Department's financial statements. The Department engages accounting firms to perform audits of government schools to ensure they adhere to required standards and procedures. During 2002-03, these audits identified that:

- 15 per cent of school councils did not formally approve the total school budget, indicating that these councils need to play a more active and effective governance role;
- 21 per cent of schools failed to obtain a satisfactory police check for locally-paid employees;
- 16 per cent of schools did not record their purchased assets in the asset register; and
- 16 per cent of schools did not have formal investment policies in place, incorporating such things as risk management, periods of investment, and authorisation requirements.

3.2.24 These observations raise concerns about the standard of financial and personnel management within schools. We have been advised by the Department that the issues arising from school audits are to be followed-up by departmental regional directors at meetings to be held with the respective school principals. Furthermore, we were advised that discussions have been held on a number of the financial management related issues with the schools' Business Managers Group, to be followed-up with additional training in the future.

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

It is pleasing to note that the report acknowledges the steps the Department has already taken to improve the financial and personnel management environments in schools.

STATUS OF RECOMMENDATIONS MADE IN THE PERFORMANCE AUDIT REPORT ON TEACHER WORK FORCE PLANNING

Introduction

3.2.25 The availability of appropriately trained and qualified teachers is a pre-requisite for quality schooling. Teacher work force planning is, therefore, of vital interest to government and to the community. Matching the demand for teachers with an appropriate supply is a critical aspect of teacher work force planning.

3.2.26 In February 2003, there were over 1 500 government primary and secondary schools with almost 46 500 teachers and over 500 000 students in Victoria.

Performance audit 2001

3.2.27 In 2001, the Office undertook a performance audit of *Teacher work force planning* that examined how effectively the Department of Education and Training (the Department) planned and managed its requirements for teachers. Specifically, the audit assessed:

- whether the Department undertook appropriate work force planning activities;
- how well the Department undertook teacher work force planning;
- how well schools planned for, and managed, their teacher requirements;
- the effectiveness of initiatives to ensure that the required numbers and types of teachers are available; and
- the effectiveness of linkages between key stakeholders involved in teacher work force planning.

3.2.28 As part of the audit we assessed work force planning within the Department and also visited 119 schools to examine their work force planning activities.

3.2.29 The Office's report on the performance audit was tabled in Parliament in November 2001. Recommendations in the report were directed at 4 key areas:

- work force planning undertaken centrally, i.e. within the Department;
- work force planning within schools;
- initiatives to address teacher work force requirements; and

- co-ordination between key stakeholders.

Outline of our approach to the follow-up review

3.2.30 We recently reviewed the Department's progress in actioning the recommendations made in the performance audit report. Given that 2 years have passed since the performance audit, we expected to see significant progress towards implementing the recommendations made in the report. It is however, too early to conduct a follow-up audit. We therefore undertook additional investigations limited to assessing the accuracy of the information provided by the Department about their actions on the recommendations.

3.2.31 To assist our review, we provided the Department with a schedule of the recommendations that we made in our November 2001 report, along with the Department's published responses. We asked the Department to review that material and to forward to us details of:

- recommendations which have been acted upon and progress in implementation;
- improvements that have occurred as a result of the actions taken; and
- recommendations that have not been acted upon and the reasons for the inaction.

3.2.32 We reviewed the information provided and visited the Department to discuss progress. We also consulted with external stakeholders to obtain their perspectives on the action taken by the Department to address the report's recommendations.

Agency progress with audit recommendations

Work force planning undertaken centrally

3.2.33 The ability to effectively match the demand for teachers with an appropriate supply is the desired outcome of teacher work force planning. Our recommendations about work force planning undertaken by the Department focused upon improving the quality of data used for planning and broadening the scope to include the non-government sector. We also recommended improvements to the Department's computerised Human Resources Management System.

Improving data and projections about the teacher work force

3.2.34 Our 2001 audit recommended that the Department should:

- continue to adopt a teacher work force planning model that caters specifically to Victoria, while continuing to contribute to national planning activities;
- include both government and non-government sectors in its work force projections;
- improve the quality and availability of work force data by consolidating some existing surveys, extending survey coverage to include non-government sectors and expanding its use of data from the Australian Bureau of Statistics; and
- seek information on retirement intentions of teachers and on teaching intentions of former teachers.

Departmental actions

3.2.35 The Department has continued to use a Victorian-based teacher work force planning model and has broadened the scope of information in its annual *Teacher Supply and Demand Report* to include information on non-government schools. The non-government sector accounts for over 30 per cent of all primary and secondary schools within the State and the inclusion of the sector into work force projections has improved the Department's ability to forecast teacher supply and demand. The Department has worked closely with the Catholic Education Office to obtain data on that sector's teacher work force.

3.2.36 The Department has expanded the range of questions in its *Teacher Recruitment* Survey, which is now completed on-line. The expanded questions now ask Principals about whether they have used the range of available recruitment tools.

3.2.37 In its response to our 2001 audit, the Department advised that to incorporate more accurate and reliable non-government work force data into teacher supply and demand analysis, it would need to negotiate formal arrangements with both the Catholic Education Office and the Association of Independent Schools of Victoria. During our follow-up, the Department advised that formal negotiations have not taken place, although there have been exchanges of data between the Catholic Education Office and the Department. We believe that the Department should negotiate formal arrangements with both of these agencies to provide for a more active role in data collection and reporting. The potential for these requirements to be addressed in funding agreements with non-government schools, should be explored.

3.2.38 Although the Department considers that the usefulness of local level data from the Australian Bureau of Statistics are limited by their high sampling variability, it advised that information such as the Bureau's *Schools Australia* data are used regularly by the Department, and sources such as the OECD are used as data and statistical methodologies become available.

3.2.39 The Department does not collect information on former teachers' future intentions to return to teaching, but advised that:

- It will survey government teachers who resign or intend to leave teaching, during final term 2003 or first term 2004, as part of a national data collection exercise being undertaken with the Commonwealth. The survey will aim to capture factors that affect teachers' decisions to leave the profession.

  We consider that this survey has the potential to provide valuable information on the intentions of teachers in government schools; and
- It would refer the collection of data on former teachers' future intentions to return to teaching to the Victorian Institute of Teaching. The Institute was established in 2001 following the introduction of a requirement for all teachers to be registered. Its establishment means that, for the first time, the potential pool of government and non-government teachers within Victoria will be able to be quantified.

We consider that the Institute is well-placed to collect information on the retirement intentions of teachers in government and non-government schools and on former teachers' future intentions as well as other information of use to the Department in work force planning. The Department should establish protocols with the Institute for data collection and sharing with the aim of obtaining a range of State-wide data on teachers from 2004.

3.2.40 The Department advised that its *Recruitment On-line* tool, which enables prospective teachers to advertise their personal profiles to Principals in Victorian government schools via a website, provides the Department with an indication of teacher availability. We recognise that this tool has the potential to provide an indication of intentions to the Department but is limited by the extent to which teachers choose to use the tool. We also understand that the Department is seeking to enhance the tool to enable Principals to make offers directly to applicants through *Recruitment On-line*.

Upgrade of the Human Resources Management System

3.2.41 In 2001 we recommended that the Department should:

- develop a business case to consider the upgrade of its Human Resources Management System; and
- adopt a work force planning management reporting model that reflects the relevant roles and responsibilities of each level of management, i.e. the executive management and ministerial level, the central divisional level, the regional level and the school level.

Departmental actions

3.2.42 During 2002, the Department developed a business case for upgrading its Human Resources Management System, and funding has been provided to develop a performance management component and an e-recruitment function. The business case also included a proposal to extend the system's functionality to include on-line web-based access by the Department's staff and managers for:

- recording teacher qualifications and skills;
- work force analysis and budget planning tools for managers; and
- a management information system and decision-making tools.

3.2.43 We support the Department's intention to improve the work force planning and reporting aspects of its Human Resources Management System. We were advised that funding for the proposed upgrades and extensions has not yet been approved.

Work force planning within schools

3.2.44 Decisions about the recruitment of staff are taken at the school level. This requires effective and efficient local work force planning to minimise staff shortages and to plan for the recruitment of teachers with the appropriate skills, experience and qualifications. In 2001, our recommendations focused upon improving the tools that the Department makes available to schools, encouraging longer-term work force planning, and consolidating the information provided to schools for planning purposes.

Improving tools available to schools and encouraging longer-term work force planning

3.2.45 We recommended that the Department should:

- improve work force planning through better linking of planning tools;
- reinforce with Principals that a documented work force plan should be prepared annually, and that it should cover at least 3 years;
- increase the use of the Human Resources Management System for work force planning;
- provide professional development opportunities for schools on work force planning;
- establish a consolidated source of information for work force planning; and
- increase schools' awareness of the Department's enrolment projections and their limitations for work force planning purposes.

Departmental actions

3.2.46 The Department has linked planning tools to improve work force planning by schools. For example, major elements of schools' work force planning are now incorporated in the on-line School Global Budget Planner. The Planner is a school-specific tool that enables modelling based on various staffing and budgeting scenarios, and covers a period of 3 forward years. The Planner links an individual school's staffing information from the Human Resources Management System with its budget, and is automatically updated when changes occur to either the school's staffing profile, or to its budget.

3.2.47 Our consultations with key stakeholders during this follow-up review confirmed that the new Planner greatly assists the ability of schools to plan staffing within budget constraints. They also advised that it is being used widely in schools.

3.2.48 While the link between the Planner and the Human Resources Management System aids administrative efficiency and helps eliminate inconsistencies in data, the other proposed upgrades to the System (outlined previously), would greatly assist Principals in undertaking more detailed planning about their future work force requirements.

3.2.49 The Department is providing support to schools for work force planning in the form of information and training provided with the School Global Budget Planner. We were advised that all government schools will receive training on the Planner from regional office staff in Term 4, 2003. The Department has also made an on-line help facility available to Principals to assist them with the Planner.

3.2.50 Despite the above developments, we consider that are still important elements of work force information that remain difficult for many Principals to access. To remedy this we consider that the Department should set up a consolidated source of information on work force planning (such as a web-site) which could include:

- highlights of the Department's annual *Teacher Supply and Demand Report* with a link to the full report;
- other reports on the teacher labour market, including summaries of results of Departmental surveys; and
- reports showing the progress of implementation of teacher supply initiatives.

Initiatives to address teacher work force requirements

3.2.51 The Department, in co-operation with schools and universities, has an important responsibility for initiatives to influence the supply and distribution of teachers. Our recommendations in 2001 focused upon addressing aspects of the Department's 2 existing teacher recruitment programs, as well as giving consideration to the adoption of additional initiatives.

Addressing existing teacher recruitment programs

3.2.52 We recommended that the Department should:

- upgrade the Teaching Scholarship Scheme by better targeting, improved marketing and enhanced administration of key aspects of the Scheme such as the application process; and
- increase and monitor participation in the Teacher Graduate Recruitment Program by highlighting the benefits of the Program to schools and providing Principals with improved labour market information.

Departmental actions

3.2.53 The Teaching Scholarship Scheme is designed to attract the "brightest and best" teacher graduates to teach in Victorian government schools, particularly in curriculum and geographic areas with recruitment difficulties. Since our 2001 audit, the Department has improved the promotion and administration of the Scheme and the targeting of Scholarships awarded. The Department advised that the number of scholarships awarded in 2002 was 248 (28 more than the target number), compared with 167 in 2001. According to the report on the Scheme for 2002, 79 per cent of scholarships awarded during the year were awarded in schools identified as having staffing difficulties. This is a significant improvement on 2001 when only 63 per cent of scholarships awarded went to schools identified as having staffing difficulties.

3.2.54 Marketing of the Scheme to universities now highlights the qualifications needed for teachers in hard-to-fill subject vacancies, and the Scheme is advertised in brochures for people interested in a career in these subject areas, namely Languages other than English, Mathematics, Science and Information Technology. In addition, the Department's fortnightly magazine *Education Times* has featured articles about scholarship holders to encourage schools to participate in the Scheme.

3.2.55 The administration of the Scheme has been simplified: vacancies can now be posted on-line (through the Human Resources Management System), applications can be made on-line via the web and Principals can search the on-line database and select preferred candidates for short-listing.

3.2.56 In our interviews with stakeholders, it was suggested that the Scheme could be improved by varying the level of scholarship payments to reflect the relative difficulty that each school has in filling vacancies. The Department indicated that an evaluation of the Scheme would commence early in 2004. Given that the Scheme has now been operating since 2000, we support such an evaluation.

3.2.57 The Department's other major teacher supply initiative is the Teacher Graduate Recruitment Program. The Program commenced in 2001 and allows Principals to nominate vacancies to be filled only by graduate recruits currently not working in government schools. The main aim of the Program is to enable Principals to adjust staffing profiles and lower their overall staffing costs. The Program is targeted at recent graduates and not at hard-to-fill subjects or schools with recruitment difficulties.

3.2.58 We found that the promotion and administration of the Program has improved in a similar way to the improvements described above relating to the Teaching Scholarship Scheme. The number of graduates employed through the Program has risen from 180 in 2001 to over 500 in 2003.

3.2.59 Reports on the take-up of the Program are provided to the Teacher Supply and Demand Steering Committee, an internal Committee of the Department that examines teacher supply and demand issues and develops proposals for teacher supply initiatives. We consider that these reports could be enhanced by including analysis of the data presented and graphs depicting the main trends, similar to the annual reports of the Teaching Scholarship Scheme.

3.2.60 The Department advised that the above initiatives have been effective in boosting the supply of teachers in the subject areas and geographic areas of shortage. The Department's Teacher Recruitment Survey shows that the number of schools with difficult to fill vacancies declined by 17 per cent from 2002 to 2003.

Additional initiatives to increase teacher supply

3.2.61 In 2001 we recommended that the Department should:

- consider additional initiatives designed to increase teacher supply into schools with staffing difficulties and subject areas which are difficult to staff; and
- determine whether sufficient justification exists to introduce initiatives to increase the pool of casual relief teachers in areas of greatest need.

Departmental actions

3.2.62 The Department's most recent forecast indicates that the extent of unmet demand between 2004 and 2006, after allowing for the supply of new graduates, is between 480 and 580 teachers. This represents a significant reduction on the 2002 forecast results of 600 to 900 teachers.

3.2.63 We also found that the Department has not put in place additional initiatives to increase teacher supply. However, it advised that it is considering a number of initiatives aimed at increasing teacher supply in schools in remote regions and in hard-to-fill subject areas.

3.2.64 We found that the Department has not put in place initiatives to increase the pool of casual relief teachers. Data from the Department's Casual Relief Teacher Recruitment Census show that the proportion of schools reporting difficulties in hiring casual relief teachers fell from 44 per cent in 2001 to 37 per cent in 2002. The Department advised that its preliminary estimates for 2003 show a further drop to 30 per cent. In light of this, the Department considers that there is insufficient justification to introduce new initiatives to increase the pool of casual relief teachers. We consider there is a need to closely monitor these numbers.

Co-ordination between key stakeholders

3.2.65 A number of key stakeholders have the responsibility for making decisions that impact on the size of the teacher work force, namely:

- the Commonwealth Government funds teaching places at universities;
- universities decide the distribution of student places across faculties;
- the State government is the major employer of teachers; and
- schools make decisions on the recruitment of staff.

3.2.66 Because of the number of stakeholders involved, effective communication and decision-making mechanisms are essential.

3.2.67 To facilitate communication between different parties, the Department has established a Teacher Supply and Demand Reference Group comprising representatives of each of these stakeholders. The recommendations in our November 2001 report focused upon improving the operations of the Reference Group and the flow of information both within, and beyond, the Reference Group. We also recommended that the Reference Group conduct co-operative research projects.

Improving the operations of the Reference Group

3.2.68 We recommended that the Department should:

- review the operations of the Reference Group to ensure that it continues to meet the needs of its members;
- improve the decision-making power of the Reference Group, so that members can address teacher supply and demand issues within their own organisations;

- identify the information needs of the constituencies of the Reference Group and determine the most appropriate means of communicating information to these interested parties; and
- explore the potential to conduct co-operative research projects.

Departmental actions

3.2.69 The Teacher Supply and Demand Reference Group was reconstituted in March 2002. However, we found that the reconstituted Group comprises similar membership to that of the previous group with the addition of 2 Deans of university education faculties. The Group’s terms of reference were widened to include consideration of non-government schools and the co-ordination of the conduct of research projects to assist in the long-term planning of teacher supply and demand. While these changes are consistent with our recommendations, we could find no evidence of a review of the operations of the previous Reference Group to ensure appropriate terms of reference were developed, or that constituents’ needs were considered in reconstituting the body.

3.2.70 The Department advised that the Reference Group consults widely with its constituent groups about their information needs. The Department conducted a consultation session with the Deans of university education faculties to canvas their information needs. The Department considers that these consultations have resulted in strengthened decision-making processes, and that the content of its Teacher Supply and Demand Report addresses the identified needs of constituents.

3.2.71 Although the terms of reference of the Reference Group now include co-ordinating the conduct of appropriate research projects to assist in the long-term planning of teacher supply and demand needs across schools, co-ordinated research projects have not occurred. We found little evidence that the Reference Group sought agreement amongst members on standard methodology, definitions or data sources for research projects.

3.2.72 While various members of the Reference Group represent the views of their constituents, we consider that there is sufficient common agreement between parties for them to adopt a more co-ordinated and cost-effective approach to researching work force issues. Co-operative research projects overseen by the Reference Group could provide the community and prospective entrants to the teaching profession with an agreed view of the state of teacher demand and supply.

3.2.73 The Department advised that it is a member of a national education body, the Teacher Quality and Educational Leadership Taskforce, that co-ordinates research on teacher work force issues. The Taskforce, which comprises representatives from all State and Territory government education departments, the Victorian Catholic Education Office and the Association of Independent Schools of Queensland, is currently considering undertaking major studies about teacher attrition rates and the attraction of teachers from non-teaching professions.

Summary of agency progress

3.2.74 The Department has made progress in implementing the recommendations made in the 2001 performance audit report on *Teacher work force planning*.

3.2.75 There is still the need for the Department to take further action in the following areas:

- improving the extent of information on retirement intentions of teachers and on former teachers' future intentions to return to teaching;
- implementing proposed enhancements to the Human Resources Management System that directly support work force planning activities;
- establishing a consolidated source of work force information for school Principals;
- developing additional initiatives to increase teacher supply; and
- reviewing the operations of the Teacher Supply and Demand Reference Group and its decision-making power, and encouraging the co-ordination of research.

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

The Department sees the findings and conclusions of the Status of recommendations: Teacher work force planning *as independent confirmation that its teacher supply and demand initiatives, such as the improved marketing and targeting of the Teaching Scholarship Scheme, have had a positive impact in addressing both difficult to fill subject areas and difficult to staff geographic locations.*

Based on a comparison of 2002 and 2003 Teacher Recruitment Census results, a 17 per cent reduction in schools reporting difficult to fill vacancies is a significant outcome as acknowledged by this report. The nearly 30 per cent reduction in schools with difficult to fill vacancies, where no appointment had been made at the time of the census, suggests the Department has been successful in tackling teacher supply issues in the more difficult to staff schools.

In relation to specific report recommendations, the Department will:

- *Explore the potential to link teacher workforce data collection and reporting from the non-government sector to future funding arrangements;*
- *Improve access by schools to sources of information such as the Teacher Supply and Demand Report;*
- *Continue to pursue additional initiatives to boost teacher supply in difficult to fill subject and geographic areas subject to budgetary constraints. (As the report acknowledges, a range of proposals in this regard are currently under consideration); and*
- *Review the operations of the Teacher Supply and Demand Reference Group.*

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

There remains however, a limited number of areas where the Department would like to make supplementary comments:

- *Firstly, the supply of new graduates in recent times has never met school demand yet the teacher labour market has been found to be in balance. This was the conclusion of both the 2001 Auditor General's report on teacher workforce planning and the recent Ministerial Council of Education, Employment and Training and Youth Affairs report entitled "Demand and Supply of Primary and Secondary Teachers in Australia" which was prepared as at December 2002. Clearly, other sources of supply have been and will continue to be important in meeting any shortfalls in the supply of university graduates;*
- *Based on recent data from the Victorian Institute of Teaching, the potential Victorian teacher labour market is approximately 90,000. While the Department acknowledges it needs to closely monitor the impact of an ageing workforce, the forecast level of unmet demand is manageable given the total size of the teacher labour market and the capacity to meet this demand from non-university graduate sources; and*
- *While the Department is in agreement with the audit recommendation that it is timely to review the terms of reference of the Teacher Supply and Demand Reference Group, the Department does not accept this Group is necessarily the most appropriate vehicle to conduct co-ordinated research across the government, independent and catholic school sectors.*

The Department believes that issues of research on teacher workforce issues are more cost effectively dealt with on a national rather than State basis as many issues facing State and Territory educational jurisdictions are similar. As such, the Department has been influential in sponsoring a number of major research proposals through the Teacher Quality and Educational Leadership Taskforce which formally reports to the Ministerial Council of Education, Employment and Training and Youth Affairs.

On a final note, the then Secretary of the Department of Education and Training in his formal response to the Teacher Workforce Planning November 2001 performance audit report stated, inter alia, that "The recommendations contained in the report will provide a framework for the Department to improve current strategies and develop future initiatives ...". The Department wishes to again reiterate the highly influential part played by this report in guiding the Department's approach to teacher supply and demand.

Part 3.3

Human Services

PORTFOLIO OVERVIEW

3.3.1 The Human Services portfolio comprises the Department of Human Services and 112 other agencies with 30 June balance dates, including public hospitals, ambulance services and registration boards for health professionals.

3.3.2 The Minister for Health, the Minister for Community Services, the Minister for Aged Care and the Minister for Housing have responsibility for the Department of Human Services and specific responsibility for individual entities within the portfolio.

3.3.3 Figure 3.3A provides a profile of portfolio entities with a 30 June 2003 balance date, for which we have audit responsibility.

FIGURE 3.3A
TYPE AND NUMBER OF AUDITED AGENCIES WITHIN THE HUMAN SERVICES PORTFOLIO, AT 30 JUNE 2003
(number)

Reporting entity	*Number*
Department of Human Services	1
Public bodies *(a)*	16
Public hospitals	95
Companies, trusts and joint ventures	1
Total	**113**

(a) Public bodies include statutory authorities such as Victorian Health Promotion Foundation, the Dental Practice Board of Victoria and the Nurses Board of Victoria.

Source: Victorian Auditor-General's Office.

3.3.4 The main responsibilities of the Department of Human Services include the funding and delivery of public health services, public housing, accommodation and support for senior Victorians and for people with disabilities, and other community services.

3.3.5 In meeting these responsibilities during 2002-03, the Department:

- received annual parliamentary appropriations of $7 billion and special appropriations of $1 billion;
- incurred expenditure of $8.6 billion, comprising $6.9 billion in grants to public hospitals and other health care agencies, $1.1 billion in departmental operating costs and $0.6 billion for the provision and management of public housing;
- managed assets with a value of $11.6 billion; and
- directly employed 11 000 people while funding the employment of a further 80 000 people in the wider human services sector.

3.3.6 Responsibilities of other agencies within the sector include:

- public hospitals – providing a range of acute inpatient, non-admitted and emergency, mental health, aged care, community health and public health services to the community;
- ambulance services – providing emergency services through the Metropolitan Ambulance Service, Rural Ambulance Victoria, and the Alexandra and District Ambulance Service; and
- registration boards – responsible for the registration of a range of health professionals such as medical practitioners, nurses, optometrists, pharmacists, physiotherapists, Chinese medicine practitioners, dental practitioners, chiropractors, osteopaths and podiatrists.

RESULTS OF FINANCIAL AUDITS

Audit opinions issued

3.3.7 Clear audit opinions were issued on the financial statements of 103 agencies in the sector with 30 June 2003 balance dates. The financial statements of a further 7 agencies were subject to audit qualifications, as outlined in Figure 3.3B. The financial statements of the remaining 3 agencies, as outlined in Appendix A to this report, had not been finalised at the date of this report.

FIGURE 3.3B
HUMAN SERVICES PORTFOLIO,
QUALIFIED AUDIT OPINIONS

Entities	*Reason for qualification*
Bendigo Health Care Group	Non-compliance with AASB 1041: *Revaluation of Non-Current Assets* requirement for the annual re-assessment of the fair value of assets held.
Cohuna District Hospital	Failure to consolidate the financial statements of a controlled entity, Cohuna District Hospital Nursing Home Foundation.
Mercy Public Hospitals Inc.	Failure to consolidate the financial statements of the controlled entities, Werribee District Hospital Charitable Foundations No.1 and No. 2.
Northeast Health Wangaratta	Non-compliance with AAS 15: *Revenue* requirement for the recognition of grant revenues.
St. Vincent's Hospital (Melbourne) Limited	Understatement of receivables arising from financing arrangements for the redevelopment of the Hospital.
The Queen Elizabeth Centre	Failure to consolidate the financial statements of a controlled entity, The Queen Elizabeth Centre Foundation.
Wodonga Regional Health Service	Non-compliance with AAS 15: *Revenue* with requirement for the recognition of grant revenues.

Source: Victorian Auditor-General's Office.

3.3.8 Prior year qualifications for Kyneton District Health Service (for non-revaluation of non-current assets), Omeo District Hospital and Orbost Regional Health (incorrect recognition of grant revenue) were removed for the year ended 30 June 2003 following resolution of the issues giving rise to these qualifications.

Timeliness of reporting

3.3.9 Figure 3.3C outlines the performance of portfolio entities in meeting statutory reporting requirements during the 2002-03 reporting cycle.

FIGURE 3.3C
TIMELINESS OF FINANCIAL STATEMENT COMPLETION, HUMAN SERVICES PORTFOLIO *(a)*

Finalisation of audited financial statements (no. of weeks after end of financial period)	*2002-03*		*2001-02*	
	Number	*Per cent (cumulative)*	*Number*	*Per cent (cumulative)*
Less than 8 weeks	6	5	2	2
8 to 10 weeks	5	10	10	11
10 to 12 weeks	70	70	27	35
12 to 14 weeks	22	91	49	78
14 to 16 weeks	4	95	12	88
More than 16 *weeks (b)*	6	100	13	100
Total	**113**	**-**	**113**	**-**

(a) Includes all audited financial statements as at 31 October 2003.
(b) Includes the financial statements of 3 agencies that had not been completed at the date of preparation of this report.
Source: Victorian Auditor-General's Office.

3.3.10 As indicated above, there has been substantial improvement in the overall timeliness of completion of audited financial statements by entities in this sector, with **70 per cent of entities meeting the statutory 12-week completion timeframe (35 per cent in 2001-02).** Appendix A to this report shows specific details of the financial statements and audit opinions issued.

3.3.11 The key factors contributing to the improvement included:

- the Department introducing a process to monitor progress by agencies with subsequent oversight by the Department's audit committee; and
- a more stable accounting policy environment and earlier resolution of accounting and disclosure issues.

3.3.12 Major reasons for certain agencies not meeting the deadline included delays in:

- finalising the revaluation of non-current assets; and
- resolving issues associated with the ongoing financial viability of certain hospitals.

Quality of financial reporting

3.3.13 During 2002-03, we observed improvement in the quality of the financial reporting by entities within the portfolio. In particular, there was increased compliance by agencies with pro forma financial statements issued by the Department for use by hospitals, ambulance services and other health agencies.

SIGNIFICANT ISSUES

Financial viability of public hospitals

3.3.14 In previous reports to Parliament, we have outlined our assessment of the financial position of public hospitals and the measures taken by the Department of Human Services to address financial difficulties faced by certain hospitals.

3.3.15 In assessing the financial position of hospitals, we have used the following financial indicators:

- operating result for the year, prior to transactions of an extraordinary nature;
- operating result prior to revenue grants provided to finance asset renewals and replacements, and extraordinary items;
- net cash flows generated from operating activities during the year; and
- the working capital position at year-end.

3.3.16 Our February 2003 *Report on Public Sector Agencies* commented on the financial position of public hospitals at 30 June 2002. The report concluded that 9 public hospitals were showing signs of financial difficulty, with unfavourable results in all 4 of the indicators used in our assessment. A further 15 hospitals had unfavourable results in at least 2 of the indicators used. This represented a significant deterioration in the financial performance of certain public hospitals compared with our review at 30 June 2001.

3.3.17 **We analysed the financial position of public hospitals for 2002-03. This analysis identified that the aggregate financial standing of the public hospital sector measured against the 4 indicators continued to decline during 2002-03. In relation to the financial performance of individual public hospitals, the analysis revealed that:**

- **15 hospitals showing signs of financial difficulty with unfavourable results in all 4 indicators; and**
- **a further 22 hospitals having unfavourable results in at least 2 of the indicators.**

3.3.18 Details of our analysis for 30 June 2003 are outlined in the following paragraphs.

Aggregate financial standing of public hospitals

3.3.19 Figure 3.3D provides a summary of the aggregate financial standing of all public hospitals as at 30 June 2003 compared with the previous financial year.

FIGURE 3.3D
AGGREGATE FINANCIAL STANDING OF PUBLIC HOSPITALS, AS AT 30 JUNE 2003

		30 June 2003	*30 June 2002*
Operating result *(a)* -			
Revenue	($million)	5 842	5 477
Expenditure	($million)	5 963	5 429
Operating surplus/(deficit)	($million)	(121)	48
Operating deficit excluding capital income	($million)	(317)	(161)
Net cash flows from operating activities (excluding capital income)	($million)	(58)	10
Working capital -			
Current assets less current liabilities	($million)	(160)	77
Ratio	(current assets/current liabilities)	0.85	1.08

(a) Revenue and operating results for 30 June 2003 exclude a net gain of $34.8 million on transfer of assets from LRH Pty Ltd to Latrobe Regional Hospital, a $13.5 million forgiveness of finance lease debt by SEMCL Pty Ltd to Southern Health and expenditure of $23.6 million at Melbourne Health arising from a decrement on the revaluation of buidings.

3.3.20 As indicated above, total revenue of public hospitals from Government and other sources increased by $365 million, or around 7 per cent for 2002-03. This increase included additional grants made to public hospitals by the Department of $336 million.

3.3.21 **Despite the revenue increase, the aggregate financial standing of the hospital sector worsened during 2002-03 as indicated by the decline in operating results, net cash flows from operating activities and the movement of aggregate working capital from a positive to negative position.**

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

The Department does not agree that the operating deficit excluding capital income is an appropriate indicator of the aggregate financial standing of public hospitals. This indicator should exclude capital income, depreciation and other capital expenses.

Public hospitals operating under financial difficulties

3.3.22 Figure 3.3E outlines the public hospitals, which we consider to be operating under financial difficulties across all 4 financial indicators at 30 June 2003.

FIGURE 3.3E
PUBLIC HOSPITALS DISPLAYING SIGNS OF FINANCIAL DIFFICULTY AT 30 JUNE 2003 *(a)*
($'000)

	Operating result prior to extraordinary items		*Operating result prior to funding for capital purposes and extraordinary items (b)*		*Net cash inflows (outflows) from operating activities (c)*		*Positive (negative) working capital position*	
Hospital	*2002-03*	*2001-02*	*2002-03*	*2001-02*	*2002-03*	*2001-02*	*2002-03*	*2001-02*
Metropolitan hospitals								
Eastern Health	(2 335)	(5 271)	(21 928)	(12 715)	(6 107)	(2 394)	(38 512)	(22 160)
Melbourne Health *(d) (e)*	(13 798)	(6 020)	(35 509)	(19 907)	(25 800)	(6 181)	(39 508)	(34 613)
Mercy Public Hospitals Inc	(515)	6 160	(4 055)	1 483	(1 185)	6 227	(3 002)	(641)
Peninsula Health	(4 644)	126	(10 083)	(7 253)	(1 037)	(577)	(6 320)	4 460
Southern Health *(e) (f)*	(26 035)	(9 118)	(36 245)	(26 092)	(33 538)	1 307	(51 773)	(20 454)
Western Health	(22 990)	(7 741)	(30 371)	(16 788)	(11 242)	(10 776)	(31 226)	(20 958)
Women's and Children Health *(e)*	(21 993)	(4 599)	(34 188)	(15 058)	(16 561)	(8 851)	(13 333)	12 462
Regional and rural hospitals								
Bairnsdale Regional Health Service	(1 155)	(15)	(3 303)	(1 641)	(1 564)	(559)	(2 044)	(703)
Barwon Health	(8 964)	4 781	(10 108)	2 023	(5 829)	2 125	(998)	11 419
Bass Coast Regional Health	(1 647)	(430)	(2 159)	(696)	(844)	208	(882)	742
Central Gippsland Health Service	(2 199)	704	(5 392)	(2 894)	(1 397)	558	(6 371)	(1 733)
Dunmunkle Health Services	(133)	(227)	(133)	(360)	(17)	(293)	(375)	(293)
Latrobe Regional Health *(g)*	(3 127)	10 176	(3 718)	9 603	(6)	(2 085)	(5 337)	12 897
Northeast Health Wangaratta	(1 986)	3 130	(4 251)	(2 554)	(340)	(812)	(4 685)	(2 167)
Wodonga Regional Health Service	(3 571)	1 838	(3 620)	1 170	(1 489)	2 036	(3 706)	(674)

(a) Based on audited financial statements except for Melbourne Health for which the audit was incomplete at the date of preparation of this Report.

(b) Funding for capital purposes means revenue grants provided to finance asset renewals and replacements. While this indicator excludes funding for capital purposes, it does include depreciation expense.

(c) In those instances where capital grants have been included in the reported net cash inflows/(outflows) from operating activities, for our analysis they have been excluded to ensure consistency.

(d) The amounts included for Melbourne Health are unaudited at the date of this report. The 2002-03 operating results exclude $23.6 million expenditure related to a decrement on the revaluation of buildings.

(e) Consolidated figures for health service and controlled entities.

(f) Operating result excludes $13.5 million forgiveness of finance lease from South Eastern Medical Centre Limited.

(g) Operating result excludes $34.8 million net gain on transfer of assets from LRH Ltd.

3.3.23 Based on the above analysis, **we consider that 15 hospitals are currently facing financial difficulties, a significant increase from the 9 considered to be in this situation at 30 June 2002.**

Recommendation

3.3.24 **We recommend that the Department work closely with the hospitals identified to ascertain the reasons for financial difficulties currently faced, review its current funding strategy and develop ongoing strategies to improve the financial performance of these hospitals in the future.**

Public hospitals with unfavourable results in at least 2 of the indicators

3.3.25 Our review indicated that a further 22 hospitals had unfavourable results in at least 2 of the indicators.

FIGURE 3.3F
PUBLIC HOSPITALS WITH UNFAVOURABLE RESULTS IN AT LEAST 2 OF THE INDICATORS, AS AT 30 JUNE 2003 *(a)*
($'000)

Hospital	*Operating result prior to extraordinary items*	*Operating result prior to funding for capital purposes and extraordinary items (b)*	*Net cash inflows (outflows) from operating activities (c)*	*Positive (negative) working capital position*
Metropolitan hospitals -				
Austin Health	(13 409)	(21 568)	3 460	(21 148)
Bayside Health	(8 193)	(24 320)	1 453	(29 787)
Regional and rural hospitals -				
Alpine Health	(288)	(722)	47	(392)
Ballarat Health Service	(4 542)	(5 226)	898	(8 260)
Colac Area Health	3 564	(1 556)	(881)	(1 038)
Coleraine District Health	(894)	(949)	(198)	666
Djerriwarrh Health Services	(274)	(446)	304	(278)
East Wimmera Health Service	(1 188)	(1 631)	(569)	2 187
Echuca Regional Health	(552)	(1 583)	901	(1 792)
Goulburn Valley Health	(4 688)	(5 579)	648	(6 809)
Heywood Rural Health	(2 128)	(2 136)	187	(513)
Kooweerup Regional Health	(81)	(306)	201	(42)
Lorne Community Hospital	(33)	(402)	(159)	59
Manangatang and District Hospital	(84)	(152)	(46)	56
Omeo District Hospital	123	58	(132)	(161)
Portland and District Hospital	(1 808)	(2 021)	1 194	(2 674)
Rural Northwest Health	(2 404)	(3 449)	(1 667)	95
Swan Hill District Hospital	(11)	(862)	(129)	3 049
Tallangatta Health Service	(522)	(522)	(100)	655
Upper Murray Health and Community Services	(147)	(172)	300	(530)
Wimmera Health Care Group	(1 171)	(1 586)	152	(1 887)
Yarrawonga District Health Service	(943)	(1 167)	256	(596)

(a) Based on audited financial statements except for Rural Northwest Health which was unaudited at the date of preparation of this report.

(b) Funding for capital purposes means revenue grants provided to finance asset renewals and replacements. While this indicator excludes funding for capital purposes, it does include depreciation expense.

(c) In those instances where capital grants have been included in the reported net cash inflows/(outflows) from operating activities, for our analysis they have been excluded to ensure consistency.

Recommendation

3.3.26 **We recommend that the Department closely monitor the budget strategies and ongoing financial performance of the hospitals with unfavourable results in at least 2 of the financial indicators subject to review.**

Need for changes to funding arrangements

3.3.27 The operating result prior to extraordinary items, as outlined in Figures 3.3D, 3.3E and 3.3F, includes the cost of depreciation. In 2002-03, the depreciation expense incurred by public hospitals totalled $218 million ($204 million in 2001-02).

3.3.28 Although the parliamentary appropriation arrangements currently operating in Victoria are based on the full cost of service delivery including depreciation, the grants provided to individual public hospitals do not cover the cost of depreciation. In lieu of providing funding equivalent to the cost of depreciation, the Department provides revenue grants to certain hospitals, totalling $216 million in 2002-03, to finance asset renewals and replacements.

3.3.29 In previous years, the Department has questioned the inclusion of depreciation in the operating results of hospitals used in our assessment of financial performance. The Department considers that given it funds major new capital works and equipment in certain hospitals and not the equivalent of annual depreciation charged in each hospital, the operating result will move up and down depending on whether large capital injections are provided to individual hospitals in a particular year.

3.3.30 While recognising the view of the Department, we consider that it illustrates the shortcoming of the current method of funding hospitals. This shortcoming is that by not providing the funding equivalent of the cost of depreciation to each hospital, the service capacity of hospitals may not be maintained. The current arrangements confuse funds required for new capital works that increase service capacity with funds for renewals or replacements. The former require full business cases to support new capacity whereas the latter should be managed by hospitals in line with asset replacement plans.

Recommendation

3.3.31 **We recommend that the Department of Human Services, in conjunction with the Department of Treasury and Finance, re-assess the current method of funding for public hospitals. This re-assessment should address the need to ensure depreciation funding is provided to hospitals to effectively maintain existing hospital infrastructure.**

Initiatives taken by the Department

3.3.32 The Department took a number of initiatives in 2002-03 with the aim of addressing the financial viability concerns faced by public hospitals. Specific initiatives included:

- Implementation of a Financial Sustainability Strategy to address the immediate financial viability concerns faced by major metropolitan and rural hospitals. Specific actions under the strategy included:
  - Establishing the Metropolitan Health Services Relations Branch (MHSRB) to assist metropolitan public hospitals in their analysis of service costs, the preparation of financial budgets and plans, and performance monitoring. The MHSRB assumed the role of the Financial Management Review Unit established earlier in the financial year;
  - Reduction in public hospital use of agency nurses to contain remuneration costs;
  - Improving the revenue position of hospitals by encouraging patients with private health insurance to be treated as private patients; and
  - Development of a standard chart of accounts and finance software to assist benchmarking of financial performance;
- Establishment of a central purchasing agency to achieve cost savings for public hospitals for medical, pharmaceutical and prosthetic supplies;
- Establishment of the Victorian Public Hospitals Governance Reform Panel that has provided recommendations for enhancing governance and accountability within public hospitals;
- Encouraging public hospitals to realise productivity gains;
- Providing funding over the next 4 years for information and medical technologies to improve the efficiency of public hospitals; and
- In conjunction with the Department of Treasury and Finance and the Department of Premier and Cabinet, undertake a review of price and resource allocation in public hospitals for financial targets and long-term financial sustainability purposes.

3.3.33 The 2003-04 State Budget allocated a further $464 million over 4 years to create a greater capacity for public hospitals to deal with extra patient admissions and emergency treatment as well as providing additional nurses and healthcare staff.

3.3.34 **We recognise the action taken by the Department to address issues surrounding the financial performance of public hospitals. However, we remain concerned that, despite these efforts, the financial standing of the hospital sector has continued to decline in 2002-03.**

Recommendation

3.3.35 **We recommend that the Department and public hospital managers examine all avenues to ensure that action to address the deteriorating financial position is implemented expeditiously.**

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

The Department has commented for a number of years that the figures used by the Auditor General as representative of operating results are potentially misleading in illustrating signs of financial difficulty. The operating results as used by the Auditor-General include both depreciation and capital income. Although the depreciation amount is relatively stable, capital income varies widely from year to year as the Department funds major new capital works and major items of equipment on the basis of requirement. Capital works in particular e.g. the rebuilding of the Austin hospital, can require large amounts of expenditure in some years and much lesser amounts in others. The Department believes that it is better to eliminate both capital expenditure and depreciation to show the underlying operating result.

A table showing the underlying operating results which total a $102 million deficit is attached.

AGGREGATE FINANCIAL STANDING OF PUBLIC HOSPITALS

As at 30 June 2003	*VAGO* *$m*	*DHS* *$m*
Net operating deficit as reported in annual reports	**-72.7**	**-72.7**
Less -		
Latrobe Regional Hospital - net asset received free of charge *(1)*	-34.8	
Southern Health forgiveness of lease liability *(1)*	-13.5	
Less -		
Capital purpose income		-219.7
Interest on capital fund		-1.4
Proceed from sale of fixed assets		-53.6
Assets received and forgiveness of liability (net) *(2)*		-52.3
Add -		
Depreciation		215.1
Written Down Value of assets sold		59
Land / building decrement / write off		13.5
Infrastructure maintenance grants wrongly classified		9.6
Adjusted Deficit	**-121**	**-102.5**

(1) These items excluded by VAGO are included in *(2)* by DHS.

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

Recommendations in paragraphs 3.3.24 and 3.3.26

The Department accepts that there has been deterioration in the performance of public hospitals, with a further increase on 2001-02 in the number of hospitals displaying signs of financial difficulty.

The Department continues to work closely with hospitals to identify the reasons for the financial difficulties currently faced and has identified governance reform, benchmarking, improved information technology, reasonable indexation of non-wage items and improved management performance as key initiatives for action. Significant action has already been undertaken in a number of these areas, including:

- *Monitoring the implementation of agreed three year financial recovery plans developed by poorly performed Metropolitan Health Services identified in 2002-03.*
- *Assisting Metropolitan Health Services, identified during 2003-04 as exhibiting financial stress, to develop agreed three year financial recovery plans.*
- *Agreeing realistic and achievable budget targets with these Metropolitan Health Services.*
- *Regular meetings with Metropolitan Health Services to discuss and influence financial performance including:*
    - *annual budgets and the strategies underpinning these.*
    - *performance against budget.*
    - *cash forecasts including provision of cash injections if required.*
    - *performance against activity targets.*

Similar activities are undertaken in regard to rural hospitals identified as at risk.

The Rural and Regional Health and Aged Care Services Division has also implemented a system of more detailed cashflow reporting to provide early identification of hospital's cash positions. It is currently being applied to the hospitals with the poorest results but will be gradually extended.

In 2002-03, the Small Rural Health Services Funding Model was introduced for all Group D and E hospitals in rural areas to enhance the viability of these 35 hospitals.

The Department has acted to strengthen the capacity of Boards of Governance of Metropolitan Health Services and major regional hospitals through;

- *the commissioning by the Minister for Health of the Victorian Public Hospital Governance Reform Panel Report; and*
- *action to improve the information provided to Hospital Boards of Governance, through the development of a standard Integrated Performance Report, that will provide a standard suite of financial, strategic, access and quality information to Boards.*

The Department is also implementing a standard chart of accounts for public hospitals to improve the comparability of hospital financial information and to enhance the benchmarking capacity of the sector. This will contribute to the identification of areas for management action.

In addition the Department, in consultation with the Department of Premier and Cabinet and the Department of Treasury and Finance has commenced a pricing review of the State's public hospital sector.

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

Recommendation in paragraph 3.3.31

The Department agrees that the incorporation of depreciation funding for the replacement of plant and equipment in public hospitals has merit and will examine the feasibility of such an approach.

The Department does not agree that depreciation funding for the replacement of hospital buildings should be provided to individual hospitals. Such an approach would disadvantage those hospitals that require replacement over those that have been recently redeveloped and would not support the Department's strategic approach to major developments. Major capital developments are mostly for the replacement of existing assets – such as the redevelopment of the Austin and Repatriation Medical Centre, or a mixture of redevelopment with some additional capacity – such as Maroondah. Providing depreciation funds directly to hospitals would diminish the capacity of the State to meet specific hospital needs as they arise.

Recommendation in paragraph 3.3.35

The Department agrees that action to address the deteriorating financial position is implemented expeditiously and has a number of initiatives underway. The outcomes of the Price Review and Paediatric Cost Weight Study will feed directly into the Department's budget planning for 2004-05.

Adequacy of control environment

3.3.36 A key responsibility of the management of each agency is to establish and maintain a sound control environment and an adequate system of internal controls to ensure that:

- the agency's financial records and other information completely and accurately reflect its activities;
- its assets are safeguarded; and
- irregularities are prevented, detected and corrected, should they occur.

3.3.37 The 2002-03 financial audit process confirmed that the overall control environments established within agencies in this sector, and the associated systems of internal control subject to audit examination, were generally satisfactory. However, a number of matters were identified in relation to the preparation and review of key accounting reconciliations which that require particular attention by the respective agencies. The following issues outlined below in Figure 3.3G are indicative of the types of matters raised in our reports to agencies, however, they are not widespread across the sector.

FIGURE 3.3G
AUDIT ISSUES IDENTIFIED AND REPORTED DURING THE 2002-03 FINANCIAL AUDIT CYCLE

Subject area	*Issues identified*
Governance	• Integrated risk management frameworks not yet finalised across agencies. • Fraud prevention strategies not formalised. • Audit committee composition not in line with better practice.
Financial management and reporting	• Policies and procedures for specific accounting activities (e.g. investment policy) are not formalised. • Preparation of financial recovery plans and monitoring of performance outcomes needs to be improved.
Revenue/receivables	• Inadequate controls over the issue of credit notes. • Debtor's ledger reconciliations not performed in a timely manner or independently reviewed.
Expenditure/accounts payable	• Inadequate monitoring of master files which have resulted in duplicated or incomplete supplier information.
Payroll	• Inaccurate or incomplete employee information on master files and possible non-compliance with legislative obligations with regard to tax and other matters. • Lack of independent review over journal adjustments, payroll reports and reconciliations with the general ledger.
Assets	• General ledger account reconciliations not performed in a timely manner or independently reviewed. • Unpresented cheques not investigated in a timely manner. • Asset registers not accurately maintained or reconciled to general ledger. • Policies and procedures not formalised. • No formal policies for the recognition and capitalisation of assets.
Liabilities	• Accumulation of excessive annual leave entitlements.

3.3.38 The matters raised were referred to the relevant agencies. We will review remedial action taken by the respective agencies during the 2003-04 financial audit.

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

The recent implementation of Victorian Government's Financial Management Compliance Framework together with ongoing Auditor-General scrutiny of the control will further focus entities resources towards improving their control environment towards best practice.

Part 3.4

Infrastructure

PORTFOLIO OVERVIEW

3.4.1 The Infrastructure portfolio comprises the Department of Infrastructure and a range of other entities that provide services in the transport, energy and major projects (including property development) sectors. The Minister for Transport, the Minister for Major Projects, the Minister for Information and Communication Technology and the Minister for Energy Industries and Resources have responsibility for the Department and specific responsibility for individual entities within the portfolio.

3.4.2 Figure 3.4A provides a profile of portfolio entities with 30 June 2003 balance dates, subject to audit by the Auditor-General.

FIGURE 3.4A
TYPE AND NUMBER OF AGENCIES WITHIN THE INFRASTRUCTURE PORTFOLIO, AT 30 JUNE 2003

Reporting entity	*Number*
Department	1
Public bodies *(a)*	12
Companies, trusts and joint ventures	9
Total	**22**

(a) Includes the Public Transport Ticketing Body which was formed in June 2003, however, this body has received an exemption under the *Financial Management Act* 1994 from reporting as at 30 June 2003 and will prepare its first financial report for the period ending 30 June 2004.

3.4.3 The Department has responsibility for the strategic planning and delivery for Victoria's essential infrastructure. Working directly, or through portfolio agencies and private sector providers, the Department is responsible for Victoria's road and rail transport services and infrastructure, the ports and marine sectors, implementing information and communication technology policy, providing strategic advice on energy policy and managing the delivery of large-scale development and construction projects for the Victorian Government.

3.4.4 The activities of other major portfolio entities include:

- Maintaining and improving Victoria's roads – through the Roads Corporation of Victoria (VicRoads). VicRoads also develops road safety programs, registers vehicles and licenses drivers;
- Management and development of the Port of Melbourne and commercial shipping channels – through the Port of Melbourne Corporation;
- Growing and adding value to the rail infrastructure network and property assets and seek and develop commercial opportunities – through VicTrack;
- Developing sustainable communities around major transport hubs – through VicUrban; and
- Managing the Spencer Street Station precinct and its redevelopment – through the Spencer Street Station Authority.

3.4.5 Portfolio entities and departmental output groups changed during the 2002-03 financial year as a result of machinery of government changes. New portfolio entities are the Office of Gas Safety, Office of the Chief Electrical Inspector, Special Power Payments Trust, Victorian Energy Networks Corporation and the Network Tariff Rebate Trust Fund (established in April 2003). Departmental output groups for planning (including strategic land use planning), heritage, buildings and local government were transferred out of the Department and new output groups related to multimedia and energy policy were acquired by the Department.

3.4.6 As a consequence of recent developments in public transport franchising arrangements, 7 new entities were created during 2002-03, comprising the rolling stock holdings group of companies and Victorian Rail Services Pty Ltd.

3.4.7 Other new entities to be audited in the 2003-2004 financial year include:

- Public Transport Ticketing Body, created during June 2003 to ensure ongoing development and improvement of the Victorian public transport network ticketing system;
- Southern and Eastern Integrated Transport Authority, formed to manage the development of the Mitcham-Frankston Freeway;
- V/Line Passenger Corporation, created during July 2003 to oversee the operations of V/Line rail services and acquired a subsidiary company, V/Line Passenger Pty Limited during October 2003;
- Port of Melbourne Corporation, created during July 2003 and assumes the functions of the former Melbourne Port Corporation and the Victorian Channels Authority; and
- VicUrban, assumed the functions of the former Docklands Authority and the Urban and Regional Land Corporation from 1 August 2003.

3.4.8 Some of the key financial statistics associated with the portfolio include:

- property, plant and equipment assets of $21.3 billion;
- expenditure on the provision of rail services of $997.9 million;
- road expenditure of $811.1 million;
- bus services expenditure of $448.6 million; and
- interest bearing liabilities of $552 million.

RESULTS OF FINANCIAL AUDITS

Audit opinions issued

3.4.9 Clear audit opinions were issued on the financial statements of 15 portfolio entities. Qualified opinions were issued on the financial statements of 3 companies within the Rolling Stock Holdings group on the basis that comparative amounts included in their financial reports, for the 30 month period ended 31 December 2002, had not been previously audited. Consequently, we were not in a position to, and did not express an opinion on the comparative amounts due to this limitation on the scope of our audit.

Timeliness of reporting

3.4.10 Figure 3.4B outlines the performance of portfolio entities in meeting reporting requirements during 2002-03.

FIGURE 3.4B
TIMELINESS OF FINANCIAL STATEMENT COMPLETION, INFRASTRUCTURE PORTFOLIO *(a)*

Finalisation of audited financial statements (no. of weeks after end of financial period)	*2002-03*		*2001-02*	
	Number	*Per cent (cumulative)*	*Number*	*Per cent (cumulative)*
Less than 8 weeks	3	14	3	17
8 to 10 weeks	1	18	3	35
10 to 12 weeks	3	32	5	64
12 to 14 weeks	3	45	3	82
14 to 16 weeks	-	45	2	94
More than 16 weeks (b)	11	100	1	100
Total *(c) (d)*	**21**	**-**	**17**	**-**

(a) Includes all audited financial statements as at 31 October 2003.
(b) Includes 3 agencies whose financial statements had not been finalised at the date of this Report.
(c) Includes the former Docklands Authority and the Urban and Regional Land Corporation, both of which had their 2002-03 financial years extended to 31 July.
(d) Excludes the Public Transport Ticketing Body, which received an exemption from reporting as at 30 June 2003.

3.4.11 There was deterioration in the timeliness of completion of audited financial statements by entities, with only 32 per cent of entities meeting the statutory 12-week completion time frame (64 per cent in 2001-02).

3.4.12 A full list of all entities in the portfolio and audit opinions issued is set out in Appendix A of this report.

3.4.13 The factors contributing to the significant delays in the preparation of financial reports within the portfolio include:

Department of Infrastructure

- A number of significant and complex accounting issues were not resolved until significantly after balance date;

- Additional accounting and other requirements arising from machinery of government changes;
- Preparation of complete draft financial statements was significantly delayed; and
- The creation of a new company, which assumed certain functions of a public transport franchisee, delayed finalisation of the financial reports of both the Department and the Company.

VicTrack and subsidiaries

- A number of significant and complex accounting issues arose from VicTrack's acquisition of the Rolling Stock Holdings group of companies on 30 June 2003. The timing of the acquisition of these subsidiaries and various complex accounting issues delayed finalisation of the financial reports of both VicTrack and its subsidiaries.

Quality of financial reporting

3.4.14 During 2002-03, the quality of reporting by entities within the portfolio was maintained at a satisfactory level.

Adequacy of control environment

3.4.15 A key responsibility of the management of each entity is to establish and maintain a sound control environment and an adequate system of internal control to ensure that:

- the entity's financial records and other information completely and accurately reflected its activities;
- its assets are safeguarded; and
- irregularities are prevented, detected and corrected, should they occur.

3.4.16 Audit procedures designed to assess the control environment and the effectiveness of key entity controls are an integral part of financial statement audit. The 2002-03 financial audit process confirmed that the control environments established within portfolio entities and the associated systems of internal control, to the extent subject to audit examination, were generally satisfactory. However, certain matters were identified which required management's attention at the respective entities. The more significant and/or common of these issues are outlined below.

FIGURE 3.4C
AUDIT ISSUES IDENTIFIED AND REPORTED DURING THE 2002-03 FINANCIAL AUDIT CYCLE

Subject area	*Issues identified*
Corporate governance	• Two entities did not have properly constituted audit committees.
Financial management and reporting	• Excessive annual leave entitlements at 2 portfolio entities. • Inadequate authorisation of asset disposal procedures at a major portfolio entity. • Inadequate policies for the recognition and capitalisation of assets at a major portfolio entity.
Control environment	• No evidence of the investigation and explanation of variances between the accounts payable subsidiary system and the general ledger. • Instances where payroll reconciliations were not performed, authorised or independently reviewed on a timely basis. • Failure to retain certain payroll records by an entity.
Information systems	• User access to a computerised payment system is not formally monitored. • Inadequate segregation of duties for a computerised payment system.

Other issues of significance

3.4.17 Comments follow on a number of other issues of significance arising from the 2002-03 financial audit process.

Public transport franchising arrangements and accounting for CityLink

3.4.18 During the 2002-03 financial audit process, a number of significant issues arose from:

- several key events and developments in respect of the State's public transport franchising arrangements, including:
  - the withdrawal of the National Express Group;
  - the creation of interim operating agreements with 2 of the franchisees in order to re-organise the public transport system;
  - the termination of one franchise during October 2003; and
  - the State's acquisition of companies associated with the procurement and financing of rolling stock for that franchise; and
- the State's accounting treatment of City Link, including the write-off of certain related State assets.

3.4.19 Detailed comment on these matters is contained in our November 2003 *Report of the Auditor-General on the Finances of the State of Victoria*. Our 2003-04 financial audit process will continue to review any further key developments within the portfolio and their implications for financial reporting.

Application of parliamentary appropriations

3.4.20 The Victorian parliamentary appropriation framework is based on a purchaser/provider model. A key principle embodied in this framework is that appropriation revenue is only made available, by the Treasurer on behalf of the Government, to Departments once outputs are delivered.

3.4.21 **Notwithstanding this appropriation principle, during 2002-03 we noted that the Department of Infrastructure received output appropriation funding of $207 million ahead of service delivery, with the amount subsequently transferred into 2 trust accounts within the Trust Fund and remaining unspent at 30 June 2003.** This funding comprised $151 million which was transferred into the Better Roads Victoria Trust Account and $56 million transferred into the Public Transport Fund account. The department expects to spend these appropriated funds in future years for purposes consistent with the trust accounts, that is, towards the construction and maintenance of roads (the Better Roads Victoria Trust Account) and public transport purposes (the Public Transport Fund account).

3.4.22 **The effect of the above transactions was to increase the value of Consolidated Fund payments (and the Consolidated Fund cash deficit) during 2002-03, and to provide funding for future years towards roads and other transport expenditure without impacting on the Consolidated Fund reported result for those years.**

Recommendation

3.4.23 **Consistent with the abovementioned purchaser/provider principle embodied in the current appropriation framework, we recommend that any amounts standing to the credit of trust accounts within the Trust Fund at the end of the financial year, which represent funds drawn-down from the Consolidated Fund for services not yet delivered, should be repaid to the Consolidated Fund.**

3.4.24 This recommendation reiterates that made in our April 2003 report on *Parliamentary control and management of appropriations*, in relation to similar practices observed at other departments.

***RESPONSE** provided by the Secretary, Department of Infrastructure*

The Department met all the reporting requirements of the Financial Management Act and the Minister was able to table the report within the legislative timelines notwithstanding the complex City Link accounting issues and Machinery of Government accounting implications identified by the Auditor-General in his report. With respect to the treatment of the City link assets, the position presented by the Department in late August 2003 was subsequently accepted by the Auditor-General.

In relation to the comments on the application of Parliamentary appropriations, the Department has met all the requirements agreed between the Department and the Treasurer to receive output funding in accordance with Financial Management Act 1994. Equally, the Treasurer has certified the outputs and provided the funding to the Department.

***RESPONSE** provided by the Secretary, Department of Infrastructure - continued*

Funding received relates to committed projects, which is held in the Better Roads Victoria Trust Fund and the Public Transport Trust Fund until the cash is required to meet commitments.

The Auditor-General's recommendation will be discussed with the Department of Treasury and Finance.

Part 3.5

Innovation, Industry and Regional Development

PORTFOLIO OVERVIEW

3.5.1 The Department of Innovation, Industry and Regional Development supports 7 ministerial portfolios, comprising State and regional development, industrial relations, innovation, manufacturing and export, financial services industry, small business and tourism.

3.5.2 Figure 3.5A provides a profile of portfolio entities with 30 June 2003 balance dates, which are subject to audit by the Auditor-General.

FIGURE 3.5A
TYPE AND NUMBER OF AGENCIES WITHIN THE INNOVATION, INDUSTRY AND REGIONAL DEVELOPMENT PORTFOLIO, AT 30 JUNE 2003

Reporting entity	*Number*
Department	1
Public bodies	4
Companies, trusts and joint ventures	5
Total	**10**

3.5.3 The Department has overall responsibility for developing and delivering the Government's commitment to build a creative, innovative and enterprising State with thriving businesses. In the main, its activities are directed towards:

- enhancing and attracting investment across the State;
- developing new economic growth capabilities;
- rebuilding rural and regional economic communities;
- overseeing the manufacturing sector;
- assisting Victorian small business;
- developing strategies to help grow Victoria's tourism and financial services sectors; and
- promoting fairer working conditions within Victorian workplaces.

3.5.4 The other portfolio entities operate in the tourism industry, stage the Australian grand prix events and manage Federation Square.

3.5.5 The Department is one of the smaller Victorian departments, with annual operating expenditure of around $310 million. Some of the key 2002-03 financial statistics associated with portfolio responsibilities include:

- provision by the Department of around $200 million in grants;
- management of Federation Square assets valued at around $490 million; and
- generation of around $53 million in ticket sales and sponsorships revenue by the Australian Grand Prix Corporation.

RESULTS OF FINANCIAL AUDITS

Audit opinions issued

3.5.6 Clear audit opinions were issued on the financial statements of 9 portfolio entities.

Timeliness of reporting

3.5.7 Figure 3.5B outlines the performance of portfolio entities in meeting the statutory reporting requirement for 2002-03.

FIGURE 3.5B
TIMELINESS OF FINANCIAL STATEMENT COMPLETION, INNOVATION, INDUSTRY AND REGIONAL DEVELOPMENT PORTFOLIO *(a)*

Finalisation of audited financial statements (no. of weeks after end of financial period)	*2002-03*		*2001-02*	
	Number	*Per cent (cumulative)*	*Number*	*Per cent (cumulative)*
Less than 8 weeks	-	-	-	-
8 to 10 weeks	-	-	-	-
10 to 12 weeks	3	30	-	-
12 to 14 weeks	3	60	4	44
14 to 16 weeks	1	70	2	67
More than 16 weeks *(b)*	3	100	3	100
Total	**10**	**-**	**9**	**-**

(a) Includes all audited financial statements as at 31 October 2003.
(b) Includes the financial statements of one entity that had not been finalised at the date of preparation of this report.
Source: Victorian Auditor-General's Office.

3.5.8 Figure 3.5B shows that **while there has been some improvement in the overall timeliness of completion of audited financial statements by entities within this portfolio, in 2002-03 only 30 per cent of entities met the statutory 12-week completion time frame compared with none in 2001-02.** Performance at the 16-week point was 70 per cent (67 per cent in 2001-02). Appendix A to this report includes details of the dates financial statements were signed and audit opinions were issued for individual entities.

3.5.9 The Department's audited financial statements were not finalised until 17 October 2003, some 16 weeks after balance date. The key factors contributing to this delay included:

- additional accounting and other requirements arising from the December 2002 machinery of government changes;
- delays in obtaining certification of annual output appropriations; and
- resource limitations within the department's finance section.

3.5.10 For other portfolio entities, major factors contributing to delays were:

- complexities associated with the valuation and accounting for the transfer of Federation Square assets from the Department of Treasury and Finance to Federation Square Management Pty Ltd; and
- resolution of issues by the Overseas Projects Corporation of Victoria Ltd related to the extension of its financing arrangements.

Quality of financial reporting

3.5.11 During the 2002-03 audit cycle we observed that the quality of reporting by entities within the portfolio was maintained at a satisfactory level.

Adequacy of control environment

3.5.12 As commented on earlier in this report, a key responsibility of the management of each entity is to establish and maintain a sound control environment and an adequate system of internal control to ensure that:

- the entity's financial records and other information completely and accurately reflect its activities;
- its assets are safeguarded; and
- irregularities are prevented, detected and corrected, should they occur.

3.5.13 The 2002-03 financial audit process confirmed that the overall control environments established within entities and the associated systems of internal control, to the extent subject to detailed audit examination, were satisfactory. However, certain matters were identified which required management's attention. The more significant and/or common of these issues are outlined below.

FIGURE 3.5C
AUDIT ISSUES IDENTIFIED AND REPORTED DURING THE 2002-03 FINANCIAL AUDIT CYCLE

Subject area	*Issues identified*
Governance	• The executive group of the Department did not receive sufficiently comprehensive reports prior to July 2003 on the operations of the Department, as existing reports primarily focus on budget performance, or adequately minute its deliberations. • Absence of an internal audit function for the Australian Grand Prix Corporation. The Corporation advised that this will be addressed in 2003-04. • Absence of annual declarations of pecuniary interest by the board of directors of Tourism Victoria to confirm declarations made upon initial appointment or the re-appointment of directors.
Financial management and reporting	• Departmental financial statement disclosures relating to compliance with appropriation authority required significant amendment to ensure that reported amounts were correct.
Expenditure/ accruals and commitments	• The Department's expenditure delegations listing did not include specimen signatures. • Vendor masterfile changes at the Department were not independently reviewed to ensure that changes were accurately processed and appropriately authorised prior to May 2003. • Expenditure commitments for the Department were manually derived rather than being system generated; consequently, major adjustments to reported commitments were required to account for expenditure commitments that had been omitted.

3.5.14 The matters raised were being pursued by the relevant agencies at the time of preparation of this report. It is also acknowledged that the Department commenced improvements to its governance arrangements as part of an organisational restructure and has initiated a financial management improvement program to enhance financial management practices within the organisation. We will review any remedial actions taken by agencies to address the issues as part of our 2003-04 audit cycle.

***RESPONSE** provided by the Secretary, Department of Innovation, Industry and Regional Development*

The majority of matters raised in the report are being addressed through initiatives being undertaken by the Department and its agencies during 2002-03. In this regard, it is to be noted that:

- *the Department's executive group operations, executive reporting and general governance arrangements were subject to internal review in the first half of 2003 and enhanced arrangements are now being progressively implemented;*
- *the Grand Prix Corporation advises that various actions relating to internal audit such as risk management and cost control analysis were completed in 2002-03, and that this program will be further developed in 2003-04 to incorporate a more comprehensive internal audit process;*
- *Tourism Victoria's arrangements for pecuniary interest declarations by its part-time board members during 2002-03 complied with government policy, and it has instigated the move to annual declarations in response to recent changes in that policy for effect in 2003-04; and*

***RESPONSE** provided by the Secretary, Department of Innovation, Industry and Regional Development - continued*

- *during 2002-03 and 2003-04, the Department has invested in the development of its budget, purchasing and financial reporting systems to enhance expenditure and budget controls.*

Other issues of significance

3.5.15 Comments follow on a number of other issues of significance arising from the 2002-03 financial audit process.

Underspend of parliamentary appropriations

3.5.16 We observed that the Department, over recent years, has consistently not fully utilised the parliamentary appropriations available to it. **Over the past 3 years, the value of appropriations applied by the Department has, on average, been around 24 per cent below the available parliamentary authority, equivalent to $107.8 million over this period**. For 2002-03, the Department "underspent" its total approved parliamentary authority by $102.3 million ($123.2 million, 2001-02).

3.5.17 The abovementioned "underspending" does not include funds held within the Department's Regional Infrastructure Development Trust Fund, which totalled $124.9 million at 30 June 2003 ($33.2 million, 30 June 2002). These funds are available over future years for regional development programs aimed at enhancing economic development.

3.5.18 **The continuing "underspending" by the Department of available parliamentary appropriation authority raises questions about the quality of internal budgeting and financial management processes**. The Department has previously advised that the carry-forward of unspent funds from year-to-year is consistent with the nature of its business which requires a high level of flexibility to meet the changing business demands and trends.

Recommendation

3.5.19 **We recommend that the Department further assess the underlying reasons for the above financial outcomes, and any implications for the preparation and management of future departmental budgets.**

***RESPONSE** provided by the Secretary, Department of Innovation, Industry and Regional Development*

The Department attributes significant resources and attention to managing its annual appropriations in both its day to day operations and in the annual budget processes involving extensive discussion with the Departments of Treasury and Finance and Premier and Cabinet.

***RESPONSE** provided by the Secretary, Department of Innovation, Industry and Regional Development - continued*

Within the framework of seeking and receiving annual funding to promote innovation, industry and economic development in Victoria, there is recognition given to the Department's need for a degree of flexibility in the application and outflow of funding over the forward estimates period. In particular, this flexibility is an important factor in positioning the Department to be a key player in the economic development environment and to respond to emerging business demands and trends.

A key feature of the Department's grant operations is the care taken to ensure accountability. Program expenditure is regulated by performance contracts that provide for the payment of funds only when performance conditions are satisfied.

Finally, the Department's role in industry development requires it to work with new industry sectors as these sectors develop genuine capability. This is particularly the case with the biotechnology and the science and technology sectors, and prudent financial management necessitates a flexible approach to the timing of funding to the various parties involved with the Department in growing these sectors.

Notwithstanding the work done to date in establishing sound budget management, the Department has invested in new reporting tools in 2002-03 and 2003-04 to better manage cash flows. Budget management will remain a priority, and individual program expenditure profiles will continue to be closely monitored.

In respect to the 30 June 2003 balance of the Regional Infrastructure Development Fund (RIDF), the inherently long lead time required for infrastructure projects has been previously recognised in your May 2003 report on the Fund. In addition, the Department's practice of only releasing funds progressively upon satisfactory achievement of milestones by recipients was recognised in that report as reflecting good practice.

Over $167 million worth of RIDF funding has been announced to 82 projects by the Government as at 13 November 2003. More approved projects will be announced in the future.

Australian Grand Prix events

3.5.20 The Australian Grand Prix Corporation has staged the Melbourne Formula One Grand Prix since 1996 and the Australian Motor Cycle Grand Prix since 1997. The Corporation is contracted to stage the Australian Formula One Grand Prix in Melbourne until 2010 and the Australian Motor Cycle Grand Prix at Philip Island until 2006.

3.5.21 Our previous reports have commented upon economic impact studies commissioned by the Government for the 2 Grand Prix events. Those economic impact studies concluded that the 2000 Formula One Grand Prix increased the Victorian Gross State Product by $130.7 million and resulted in additional taxation receipts for the State of $9.8 million. The Motor Cycle Grand Prix event conducted in 1997 was estimated to have contributed $54 million to the Victorian Gross State Product and $3.7 million in additional taxation receipts.

3.5.22 Figure 3.5D illustrates that **the net operating cost of staging the Formula One and Motor Cycle Grand Prix events for the 2002-03 financial year totalled $19.4 million ($16.2 million in 2001-02).** This cost, which represents an increase on the previous year and follows the trend established since the State first hosted these events, is less than the previously estimated annual economic benefit to the State from staging these events. It is, however, noted that the Government has not undertaken a more recent estimate of the economic benefit to the State from staging these events.

FIGURE 3.5D
NET OPERATING COST OF STAGING THE FORMULA ONE GRAND PRIX AND MOTOR CYCLE GRAND PRIX
($million)

Event	***2002-03 Actual***	*2001-02 Actual*
Formula One Grand Prix	**12.7**	10.3
Motor Cycle Grand Prix	**6.7**	5.9
Total net operating costs incurred by the State *(a)*	**19.4**	16.2

(a) Reflects the operating deficiency incurred by the Australian Grand Prix Corporation for the year, after excluding government grants.

3.5.23 As shown in Figure 3.5D, the net operating costs of hosting these events in 2002-03 increased by $3.2 million from the previous year. This has mainly arisen from:

- reduced general admission sales and sponsorship revenue, and increased operating expenses associated with the Formula One Grand Prix; and
- increased operating expenses and decreasing sponsorship revenue, partially offset by increased sales revenue, associated with the Motor Cycle Grand Prix.

3.5.24 **In addition to the above operating costs, during 2002-03 the State provided funding towards safety initiatives and infrastructure costs totalling $8.5 million ($2.6 million in 2001-02).** The increased 2002-03 contribution relates to additional funding for the building of higher debris fencing around the Formula One Grand Prix circuit to improve track safety.

***RESPONSE** provided by the Secretary, Department of Innovation, Industry and Regional Development*

Recognition needs to be given to the underlying reasons for the increase in the net operating costs in 2002-03. The reduced general admission sales for the Formula One Grand Prix was as a result of the first time that wet weather was experienced on race day. The increased operating expenses and decreasing sponsorship revenue for the Motor Cycle Grand Prix, was primarily due to the renegotiation of the promoters agreement. The agreement was restructured when it expired at the end of 2001 and as a result the commercial arrangements varied between 2001 and 2002.

In respect to the analysis of the economic benefit to the State of staging the Grand Prix events, these studies are undertaken approximately every 5 years. The last Formula One Grand Prix review was undertaken in 2000. The latest economic impact study for the 2002 and 2003 Australian Motor Cycle Grand Prix is currently being finalised and is due to be released in the near future.

Federation Square

3.5.25 Federation Square is a major development in Melbourne's central business district encompassing a range of recreational, cultural, commercial, multimedia and entertainment facilities. Responsibility for the day-to-day management of the Square rests with Federation Square Management Pty Ltd, a State-owned company.

3.5.26 We have previously commented on the progress of the Square's development in several reports to Parliament, most recently in our May 2003 *Report on Public Sector Agencies*. The major findings identified in that report included:

- the public areas of the Square were formally opened on 26 October 2002;
- there was an increase of $21.8 million in project costs since February 2002, bringing the total cost estimate of the Square to $473.3 million at May 2003;
- the confirmed funding available to the Company for the Square's development at February 2003 was $14 million less than the estimated completion cost at that date; and
- the Company's cash flow projections indicated that additional funds would be needed from June 2003 to meet the remaining project commitments.

Major developments since May 2003

3.5.27 **The revised estimated cost of the Square to the State, as at 30 September 2003, was $481.7 million. This represents an increase of $8.4 million from the estimate reported in May 2003,** mainly arising from increased:

- fit-out and minor works costs ($4.3 million);
- managing contractor and other consultant fees ($2.8 million); and
- contingency amounts to cover outstanding contractor claims ($1.3 million).

3.5.28 The estimated cost of the Square includes the fit-out costs associated with the National Gallery of Victoria Ian Potter Centre and the Australian Centre for the Moving Image. However, as mentioned in our earlier reports, it does not include certain costs, such as those relating to the demolition of the former Gas and Fuel Corporation Towers and Princes Plaza, which totalled $5.4 million.

3.5.29 **Actual expenditure on the Square to August 2003 amounted to $458.9 million.**

3.5.30 **Consistent with the total cost estimate for the Square, the value of confirmed project funding has also increased from $459.3 million at the date of our last report to Parliament to $482.9 million as at October 2003.** The $23.6 million increase in funding arises from the Government's approval of an additional loan facility of $18.7 million for the Company and an additional $4.9 million to be provided by the National Gallery of Victoria and the Australian Centre for the Moving Image.

3.5.31 The Government has also endorsed an increase in rentals to be paid by the National Gallery of Victoria and the Australian Centre for the Moving Image to allow the Company to meet its increased loan obligations over the term of that loan. At the time of preparation of this report, the increase in rentals was being finalised by the Treasurer, in consultation with the Premier and the Minister for Major Projects. **Consequently, it would appear that the increased funding required for the Square of $23.6 million will be met from rental and other payments by the National Gallery of Victoria and the Australian Centre for the Moving Image.**

3.5.32 **While the confirmed funding will be sufficient to meet the currently estimated cost of the Square, which includes an allowance for the resolution of outstanding contractor claims, any significant escalation in costs associated with outstanding contractor claims or any other additional costs will test the funding position of the Company.** The Company is continuing to negotiate final contractor claims for the major contentious outstanding contracts. Contingent liabilities of $5.6 million have been recognised in the 2002-03 financial report of the Company, representing the difference between the estimated value of work completed (and included in the current cost estimate) and the amount claimed by contractors.

3.5.33 Another key cost risk for the Company is the outcome of land tax assessments being undertaken by the State Revenue Office. While land tax has been reported as a contingent liability in the Company's 2002-03 financial report, a value for this liability is yet to be established.

Cashflow projections and associated sensitivities

3.5.34 The Company's financial report for 2002-03 recorded a negative working capital position at 30 June 2003. That is, the value of its current liabilities exceeded the value of its current assets at that date, indicating a deficiency in available liquid funds leading into the 2003-04 year. The Company's $43.7 million borrowing facility is expected to be fully drawn during 2003-04 to meet outstanding financial obligations associated with the Square.

3.5.35 In July 2003, the Company prepared revised cash flow projections covering a 5-year period to 2007-08. Based on those projections, the Company expects to achieve minor negative cash flow outcomes in 2003-04 and 2004-05, followed by minor surpluses in subsequent years. However, the cash reserves of the Company (totalling some $4 million at 30 June 2003) are expected to more than offset the negative cash flows in the first 2 years.

3.5.36 The Company's projected cash position over the 5-year period, however, relies on a number of key assumptions, including:

- sufficient increased rent will be paid by the National Gallery of Victoria and the Australian Centre for the Moving Image to enable the Company to meet its increased loan repayments;
- the existing cost estimate for the resolution of outstanding contractor claims will be adequate;

- municipal rates and land taxes will not be levied on public open spaces or the car park, or, alternatively, will be refunded by the Government;
- municipal rates and taxes attributed to cultural and civic buildings will be recoverable from the relevant tenants or, alternatively, rebated by the collecting authority or the Government;
- no substantial repairs, refurbishment or capital replacement in the formative years of the Square; and
- increasing revenue trends, generally in line with inflation, from revenue generating operations, including the car park, tenancies, events and hire of public space.

3.5.37 Due to the Square's brief period of operation, certain of the estimated cash flows are based on forecasts provided by consultants as there has been limited data upon which to base forecasts, especially the forecasts related to operating costs and longer-term maintenance costs.

3.5.38 **As outlined in this report, the Company's financial position is finely balanced and rests on a number of key assumptions over the 2003-04 financial year, which may be subject to variation and are not completely within the control of the Company. We recommend that the Company continue to closely monitor its budget and funding position.**

Independent review of the Company

3.5.39 As mentioned in our previous report, a temporary chief operating officer, nominated by the Treasurer, was appointed to review the Company's financial situation in respect of its project management and operational functions. We were advised that the Chief Operating Officer anticipates completing his review during November 2003.

3.5.40 We will review the Chief Operating Officer's final report as part of our 2003-04 audit of the company, together with the adequacy of the management response to any major issues raised in the report.

> ***RESPONSE** provided by the Secretary, Department of Innovation, Industry and Regional Development*
>
> *Recognition needs be given to the breakdown of the total reported cost of $481.7 million. $434 million is the final agreed cost to Government of the Federation Square Project. The additional $47.7 million covers the cost of new project works ($4.7 million) and the fit-out costs of the tenancies occupied by the National Gallery of Victoria and the Australian Centre for the Moving Image that are separately funded and do not form a part of the Federation Square Project Budget.*
>
> *The Department acknowledges that Federation Square Management's financial position looking forward is finely balanced and that the Company's projections of "break-even" cash flow outcomes rely on a number of assumptions that could vary and are not entirely controllable by the Company.*

RESPONSE *provided by the Secretary, Department of Innovation, Industry and Regional Development - continued*

> *However, the Department notes that this situation was identified some time ago and that the appointment of a temporary Chief Operating Officer was made specifically to identify the Company's full financial position and to mitigate any future financial risk associated with the completion of the Project. The set of strict protocols relating to the future performance and funding of works, as recommended by the Chief Operating Officer, is now operating and is designed to ensure that such works are only approved after being fully scoped and costed and the funding source clearly identified.*
>
> *Moreover, in relation to paragraph 3.5.34, the Company has advised that the negative capital position reported at 30 June 2003 was a reflection of the bringing to account all outstanding project liabilities, which were funded from new borrowings by the Company or amounts recoverable from tenants. Payment of construction related accounts since June has reduced current liabilities and seen the working capital ratio improve significantly to the extent that it is now in a positive position.*

Part 3.6

Justice

PORTFOLIO OVERVIEW

3.6.1 The Justice portfolio comprises the Department of Justice and 29 other entities including the Office of the Chief Commissioner of Police (Victoria Police), the Metropolitan Fire and Emergency Services Board, the Country Fire Authority, Victoria Legal Aid, and the Victorian Casino and Gaming Authority.

3.6.2 The primary responsibilities of the sector include:

- developing and implementing policies and strategies for public safety, crime and violence prevention, crime identification and investigation, road safety and emergency readiness;
- protecting legal rights through a just, responsive and accessible legal system, including providing support for the State's judicial system, providing legal aid for system users and supporting victims of crime;
- treating offenders in a just and humane manner, including the oversight and administration of the State's prison system;
- promoting rights and diversity through activities such as overseeing and administering the State's privacy, equal opportunity and consumer protection legislation, and providing advocacy and guardianship services;
- managing the State's emergency prevention and response services; and
- providing responsible regulation and management of the State's racing and gaming industries.

3.6.3 In meeting these responsibilities, the Department and other entities incur annual expenditure of around $4 billion, and manage assets of $3.5 billion and liabilities of $1.8 billion.

3.6.4 The Attorney-General, Minister for Police and Emergency Services, Minister for Corrections, Minister for Consumer Affairs, Minister for Gaming and Minister for Racing have responsibility for the Department and specific responsibility for the other individual entities within the portfolio.

RESULTS OF FINANCIAL AUDITS

Audit opinions issued

3.6.5 Clear audit opinions were issued on all financial statements of portfolio entities with a 30 June 2003 balance date. A prior year qualification on the financial statements of the Metropolitan Fire and Emergency Services Board, related to revenue recognition, was removed for 30 June 2003 based on materiality considerations.

Timeliness of reporting

3.6.6 Figure 3.6A outlines the performance of portfolio entities in meeting the statutory reporting requirement for 2002-03.

FIGURE 3.6A
TIMELINESS OF FINANCIAL STATEMENT COMPLETION, JUSTICE PORTFOLIO *(a)*

Finalisation of audited financial statements (no. of weeks after end of financial period)	*2002-03*		*2001-02*	
	Number	*Per cent (cumulative)*	*Number*	*Per cent (cumulative)*
Less than 8 weeks	3	10	1	4
8 to 10 weeks	4	23	3	14
10 to 12 weeks	13	67	8	43
12 to 14 weeks	6	87	10	79
14 to 16 weeks	4	100	-	79
More than 16 weeks	-	100	6	100
Total	**30**	**-**	**28**	**-**

(a) Includes all audited financial statements as at 31 October 2003.
(b) Figures for 2001-02 have been revised to incorporate gaming and racing entities transferred to the Justice sector as part of machinery of government changes implemented from 1 January 2003.
Source: Victorian Auditor-General's Office.

3.6.7 As indicated in Figure 3.6A, there has been a substantial improvement in the overall timeliness of completion of audited financial statements by entities in this sector, with 67 per cent of entities meeting the statutory 12-week completion time frame (43 per cent in 2001-02). The financial statements of all entities were finalised within 16 weeks (79 per cent in 2001-02). Appendix A of this report shows specific details of the financial statements and audit opinions issued.

3.6.8 Further improvement can be made by certain entities in the timeliness of financial reporting. Key factors contributing to the late completion of audited financial reports by certain entities included delays in:

- requesting ministerial approvals for allocation statements supporting machinery of government changes and assets transfers with other public sector entities;
- receipt of the Minister of Finance's certification of the Department's appropriation revenue for the June 2003 quarter; and

- finalising reconciliations of transactions and balances recorded by the Department with the amounts recorded by other agencies in the sector.

***RESPONSE** provided by the Secretary, Department of Justice*

The significant improvement in the timeliness in reporting the portfolio is noted and is encouraging. With the current work being undertaken with portfolio agencies to improve reporting processes, further improvement in the timeliness of reporting will be achieved. The complexity of the 2002-03 machinery of government changes will not be present in 2003-04, leading to further significant improvement.

Quality of financial reporting

3.6.9 During the 2002-03 audit cycle, the financial statements of all entities were appropriately prepared in accordance with Australian Accounting Standards and the reporting requirements of the *Financial Management Act* 1994. We considered that the overall quality of financial reporting by entities within the portfolio improved. This improvement was facilitated by all entities using the Model Financial Report for Victorian Government Departments to guide the format and content of financial statements.

3.6.10 Scope exists in certain agencies for improved quality control during the preparation of draft financial statements, particularly by ensuring the consistency of recording of transactions made between the Department and other agencies. Further comment on this matter is provided in subsequent paragraphs.

***RESPONSE** provided by the Secretary, Department of Justice*

The Department has applied considerable effort to improving the quality of its financial reporting, especially in relation to the underpinning Oracle financial system's reporting capability in regards to separate reporting entities. Continuing refinement of the processes is being undertaken to enhance the quality control of financial recording and reporting with these entities not currently on the Department's Oracle financial system to address the need for improvement.

Adequacy of control environments

3.6.11 A key responsibility of the management of each entity is to establish and maintain a sound control environment and an adequate system of internal controls to ensure that:

- the entity’s financial records and other information completely and accurately reflect its activities;
- its assets are safeguarded; and
- irregularities are prevented, detected and corrected, should they occur.

3.6.12 The 2002-03 financial audit process confirmed that the control environments established within Justice entities, and the associated systems of internal control subject to audit examination, were generally satisfactory. However, various matters were identified which required management attention at the respective entities. The more common of these issues are outlined below.

FIGURE 3.6B
AUDIT ISSUES IDENTIFIED AND REPORTED DURING THE 2002-03 FINANCIAL AUDIT CYCLE

Subject area	*Issues identified*
Expenditure/accounts payable	• Failure to identify and correctly account for accrued expenses at Victoria Police. • Examples of lack of appropriate authorisation or supporting documentation for expenditure at Victoria Police.
Payroll	• Excessive annual leave balances and inaccuracies in leave entitlement records of the Equal Opportunity Commission. • Inadequate maintenance of payroll documentation and personnel files by the Department, the Victorian Law Reform Commission and Emergency Communications Victoria.
Assets	• Delays in transferring completed capital asset projects from work in progress to fixed assets by the Department and the Country Fire Authority. • Lack of evidence of review of bank reconciliations in a number of agencies. • Incorrect assessment of useful lives of assets and related depreciation rates.
Liabilities	• Misstatement of provisions for employee entitlements by the Department and Victoria Police. • Lack of evidence of review of creditor reconciliations by the Victorian Institute of Forensic Medicine.
Risk management	• Lack of a formal risk management strategy at the Legal Practice Board. • Absence of fraud control strategies in the most sector agencies.

3.6.13 The matters raised were referred to the relevant agencies. We will review remedial actions taken by the agencies as part of our 2003-04 audit cycle.

> ***RESPONSE*** *provided by the Secretary, Department of Justice*
>
> *The issues identified in Figure 3.6B have been noted by the Auditor-General in his management letter to each reporting entity. Remedial action has been, or is being, undertaken on each issue to ensure the requisite improvements in control processes.*

OTHER SIGNIFICANT ISSUES

3.6.14 Comments follow on a number of the issues of significance arising from the 2002-03 financial audit process.

Fraud control within Justice agencies

3.6.15 The primary responsibility for the prevention and detection of fraud rests with those charged with the governance and management of a department or public body. The establishment of appropriate fraud control procedures, as an integral part of an agency's overall risk management strategy, assists in meeting this responsibility and minimises the risk that frauds will eventuate.

3.6.16 As at 30 June 2003, we identified that agencies within the Justice portfolio were yet to establish a formal approach to fraud control.

Recommendation

3.6.17 We recommend that all agencies should formally document and adopt fraud prevention and detection strategies as part of their overall approach to risk management.

***RESPONSE** provided by the Secretary, Department of Justice*

The Department fully endorses the Auditor-General's recommendation and will ensure its implementation in all reporting entities. In connection with the issue of overall risk management, of which fraud control procedures are a key aspect, the Department's approach to risk management is an extremely thorough and extensive one. This rigour of its methodology and general approach will be transplanted to all agencies within the Justice portfolio. Through the Financial Management Compliance Framework (FMCF), DoJ will be working with all agencies to ensure that appropriately designed and documented fraud prevention and detection strategies are put in place.

Department of Justice

Lack of funding agreements

3.6.18 The Department of Justice receives annual appropriations to fund the cost of its outputs. From this funding, the Department provides grants to a number of agencies within the portfolio for the delivery of their respective outputs. This grant funding exceeded $1.3 billion in 2002-03.

3.6.19 There are currently no formal funding agreements in place between the Department and other portfolio agencies receiving annual grants. Given the level of annual grants provided, we would expect the Department to have established funding agreements which include:

- the terms and conditions under which funding is provided;
- appropriate output and other performance targets;
- the level and timing of annual funding; and
- clear reporting arrangements for agencies for grants received.

3.6.20 During 2002-03, the absence of formalised funding agreements had contributed to delays in the finalisation of financial statements due to:

- uncertainty within agencies about the total funding to be provided by the Department and to be recorded in their annual financial statements; and
- inconsistencies between records retained by the Department and other agencies and the time taken to resolve these matters.

Recommendation

3.6.21 To overcome these issues and to improve accountability arrangements, we recommend that the Department formalise funding agreements with all agencies in receipt of annual grant funding.

RESPONSE *provided by the Secretary, Department of Justice*

The Department endorses the Auditor-General's recommendation and will implement an appropriate regime of funding agreements with all reporting entities for the 2003-04 financial year. These agreements will encompass the general terms and conditions under which funding is provided, relevant performance data and requisite reporting arrangements. The Department already has in place a detailed budget management system that provides agencies with their direct operating budgets and any adjustments necessary during the financial year. The uncertainty noted by the Auditor-General was confined to only a small number of reporting entities, and the funding agreements will greatly assist in overcoming this residual uncertainty.

Monitoring and reporting of capital projects

3.6.22 The Department's regime for monitoring and reporting of capital projects requires project managers to notify project completion so that costs are reclassified from work in progress to assets in the financial records of the Department and depreciation of the completed asset is commenced.

3.6.23 Our review of the Department's capital work in progress indicated that completed capital projects totalling $58 million had not been transferred to asset accounts in financial records at 30 June 2003. Accordingly, depreciation of these completed assets had not commenced on a timely basis. While not material to the financial report of the Department for the year ended 30 June 2003, the failure to correctly record these completed assets resulted in an understatement of the depreciation expense for the year.

Recommendation

3.6.24 We recommend that the Department review and enhance its current processes for monitoring capital projects to ensure the timely recording and depreciation of completed assets.

RESPONSE *provided by the Secretary, Department of Justice*

As a result of the Auditor-General's recommendation, the Department has reviewed its current monitoring and capitalisation processes. A new regime will be introduced involving a joint approach by Portfolio Infrastructure Development and Finance including monthly reviews of outstanding capital works in progress regime and follow up by monthly meetings with responsible Business Units, to ensure more timely and accurate recording and depreciation of completed assets. In addition, the $58 million in capital projects not transferred to asset accounts in 2002-03 have now been certified as complete by the responsible Business Unit and the relevant Statement of Financial Performance and Statement of Financial Position entries completed.

Country Fire Authority

Monitoring and reporting of capital projects

3.6.25 The Country Fire Authority (CFA) records the progressive cost of constructing fire tankers and pumpers as capital works in progress (CWIP).

3.6.26 Our review of the composition of CWIP indicated a lack of adequate monitoring of these transactions in that:

- there was a lack of ongoing review of the stage of completion of projects, including the absence of progressive certification by project engineers or contractors undertaking the works; and
- on the completion of projects, total project costs were capitalised without an assessment of whether all amounts recorded against individual projects would contribute to the future economic benefits of the agencies concerned and, accordingly, be correctly treated as fixed assets.

Recommendations

3.6.27 We recommend that the CFA undertake a comprehensive review of current processes for monitoring CWIP. This review should include consideration of the:

- **criteria used by the agencies for decisions about amounts to capitalise for individual projects;**
- **regular certification by project engineers and, where applicable, external contractors, of the stage of completion of individual projects and their progress against cost targets; and**
- **the processes to be used for progressive monitoring of costs charged against projects and the quality of reporting to senior management.**

***RESPONSE** provided by the Chief Executive Officer, Country Fire Authority*

The CFA accepts the recommendations and acknowledges the process for monitoring capital works in progress (CWIP) could be improved. It is proposed that a comprehensive review of CWIP will be completed by March 2004 and all recommendations will be implemented by June 2004. This review will both improve the content of the Annual Report and also the quality of capital reporting across CFA.

Victorian Electoral Commission

Need for clarification of funding arrangements

3.6.28 Funding arrangements for agencies within the State's budget sector are normally based on:

- the provision of appropriations to meet the cost of operations of the agency; and
- fees or other revenue collected by the agency being paid to the State's Consolidated Fund and not retained by the agency.

3.6.29 Under the *Electoral Act* 2002, all fees and deposits payable to the Commission and all penalties recovered for offences are required to be paid into the Consolidated Fund.

3.6.30 Under these funding arrangements, the operating costs incurred by the Victorian Electoral Commission should be funded from grants provided by the Department of Justice, which are mainly sourced from a special appropriation established for this purpose.

3.6.31 We identified that, in practice, this funding arrangement is not followed. Under current practice, the Commission:

- receives funding from the Department sourced from a Special Appropriation established for the Commission's activities;
- retains funds raised from municipal council elections rather than paying these amounts to the State's Consolidated Fund; and
- repays amounts in excess of requirements to the Consolidated Fund at year-end following an annual reconciliation of funds raised and the level of appropriation funding to which they were entitled from the Department.

3.6.32 We also identified a discrepancy of $1.3 million between the grants provided by the Department and the grants recorded by the Commission.

3.6.33 The current practices adopted by the Commission are not in line with the requirements of the *Electoral Act* 2002 or practices adopted by other budget sector agencies.

Recommendations

3.6.34 **We recommend that the Commission:**

- **review its current practices, in conjunction with the Department, to ensure that they comply with the legislative requirements for revenue collection and the receipt of appropriations; and**
- **enter into a formal funding agreement with the Department to facilitate reconciliation between amounts recorded in its financial records and corresponding amounts recorded in the Department's records.**

***RESPONSE** provided by Electoral Commissioner*

The VEC does not use receipts received for municipal Councils as additional funding and the VEC does not exceed its annual budget allocation. The VEC is keen to ensure that its treatment of funds received from municipal Councils complies with legislative requirements and at the same time meets business requirements. The VEC will work with Justice to improve this process.

Part 3.7

Premier and Cabinet

PORTFOLIO OVERVIEW

3.7.1 The Premier and Cabinet portfolio comprises the Department of Premier and Cabinet, (which includes Arts Victoria, the Office of the Governor and the Office of the Chief Parliamentary Counsel), and other agencies including the Office of Public Employment, the Office of the Ombudsman and 8 arts agencies. The Premier and the Minister for the Arts have responsibility for the Department and specific responsibility for individual entities within the portfolio.

3.7.2 Figure 3.7A provides the profile of portfolio entities with a 30 June 2003 balance date, for which we have audit responsibility.

FIGURE 3.7A
TYPE AND NUMBER OF AUDITED AGENCIES WITHIN THE PREMIER AND CABINET PORTFOLIO, AT 30 JUNE 2003

Reporting entity	*Number*
Department and other administrative units	3
Public bodies	8
Total	**11**

Source: Victorian Auditor-General's Office.

3.7.3 The Department is responsible for developing whole-of-government initiatives and managing Victoria's relationships with other governments. It provides assistance in the overall administration of the State's operations, plays a key role in initiating, planning and implementing special projects and events, delivers services and programs in relation to Government information and communication, and oversees state-owned cultural agencies through Arts Victoria.

3.7.4 Key activities of the Department are to provide advice to the Premier and the Cabinet on all aspects of policy, manage official visitor programs to increase Victoria's investment opportunities and enhance its reputation, and organise ceremonial and special events and hospitality to support the Government's strategic priorities.

3.7.5 The activities of other portfolio entities mainly relate to:

- investigation of complaints concerning administrative actions taken by government Departments - through the Victorian Ombudsman;
- provision of advice on the application of public sector employment and conduct principles - through the Office of Public Employment; and
- development and presentation of cultural projects, programs and services to benefit the Victorian arts industry and community - through Arts Victoria and arts agencies.

3.7.6 Some of the key financial statistics associated with portfolio responsibilities include:

- parliamentary appropriations of $413.9 million were applied towards the provision of departmental outputs;
- recurrent grants for arts and cultural development totalled $256.1 million;
- amounts totalling $34.6 million were contributed by government to arts entities for building upgrades and redevelopment works;
- bequests and donations to arts agencies totalled $17.5 million; and
- management of the State collection, including works of art, valued at $2.4 billion.

RESULTS OF FINANCIAL AUDITS

Timeliness of reporting

3.7.7 Figure 3.7B outlines the performance of portfolio entities in meeting the statutory reporting requirement for 2002-03.

FIGURE 3.7B
TIMELINESS OF FINANCIAL STATEMENT COMPLETION, PREMIER AND CABINET PORTFOLIO *(a)*

Finalisation of audited financial statements (no. of weeks after end of financial period)	*2002-03*		*2001-02*	
	Number	*Per cent (cumulative)*	*Number*	*Per cent (cumulative)*
Less than 8 weeks	-	-	-	-
8 to 10 weeks	-	-	1	9
10 to 12 weeks	8	73	5	55
12 to 14 weeks	2	91	1	64
14 to 16 weeks	1	100	2	82
More than 16 weeks	-	100	2	100
Total	**11**	**-**	**11**	**-**

(a) Includes all audited financial statements as at 31 October 2003.
Source: Victorian Auditor-General's Office.

3.7.8 Figure 3.7B shows that **there has been substantial improvement in the overall timeliness of completion of audited financial statements by entities in this sector, with 73 per cent of entities meeting the statutory 12-week completion time frame (55 per cent in 2001-02).** Appendix A to this report shows specific details of financial statements and audit opinions issued.

Audit opinions issued

3.7.9 Clear audit opinions were issued on all financial statements of portfolio entities with a 30 June 2003 balance date. The prior year qualification for the Library Board of Victoria (concerning the non-revaluation of assets) was resolved during the year.

Quality of financial reporting

3.7.10 During 2002-03, we observed some improvement in the quality of financial statements presented for audit by entities within the portfolio. The key factors contributing to this improvement were:

- improved finance and accounting functions within entities; and
- a more stable accounting policy environment and improved timeliness in the issue of accounting policy directives under the *Financial Management Act* 1994.

Adequacy of control environment

3.7.11 A key responsibility of the management of each entity is to establish and maintain a sound control environment and an adequate system of internal controls to ensure that:

- the entity's financial records and other information completely and accurately reflect its activities;
- its assets are safeguarded; and
- irregularities are prevented, and detected and corrected should they occur.

3.7.12 Audit procedures designed to assess an entity's control environment and test the effectiveness of key controls are an integral part of a financial statement audit. In this regard, our 2002-03 financial audit process confirmed that the overall control environments established within portfolio entities, and the associated systems of internal control subject to audit examination, were generally satisfactory.

3.7.13 However, our audits did identify the need for management at particular entities to:

- strengthen controls over cash collections; and
- carry out a physical stocktake of assets, including collection pieces, to ensure that items exist and records are complete.

3.7.14 The matters raised were referred to the relevant agencies. We will review remedial actions taken by the relevant agencies during our 2003-04 audit.

Part 3.8

Primary Industries

PORTFOLIO OVERVIEW

3.8.1 The Primary Industries portfolio comprises the Department of Primary Industries, together with 13 entities that facilitate:

- *industry development* (7 entities), including the activities of Agriculture Victoria Services Pty Ltd, the Greater Victoria Wine Grape Industry Development Committee, Melbourne Market Authority, Murray Valley Citrus Marketing Board, Murray Valley Wine Grape Industry Development Committee, Northern Victorian Fresh Tomato Industry Development Committee and Victorian Strawberry Industry Development Committee;
- *the conduct of research* (3 entities), including the activities of the Australian Food Industry Science Centre, Food Science Australia and Phytogene Pty Ltd; and
- *regulation and assurance services associated with product and service safety* (3 entities), including the activities of Dairy Food Safety Victoria, the Veterinary Practitioners Board of Victoria and the Victorian Meat Authority.

3.8.2 The Department was established in December 2002 as part of the machinery of government changes that came into effect following the State election. It is one of the smaller Victorian departments and delivers 3 outputs, at an annual cost of around $300 million, namely:

- *agriculture* - which is concerned with improving the profitability and market competitiveness of agricultural industries, while ensuring that such operations remain sustainable and environmentally responsible;
- *fisheries* - which facilitates the sustainable development of Victoria's commercial and recreational fishing industries and aquaculture, and provides for the management of Victoria's marine and freshwater fish resources; and
- *minerals and petroleum* – which focuses on the promotion and regulation of the exploration and development of Victoria's extractive, mineral and petroleum resources.

3.8.3 The Minister for Agriculture and the Minister for Energy Industries and Resources have responsibility for the Department and specific responsibility for individual entities within the portfolio.

RESULTS OF FINANCIAL AUDITS

Audit opinions issued

3.8.4 Clear audit opinions were issued on all financial statements of portfolio entities with 30 June 2003 balance dates.

Timeliness of reporting

3.8.5 Figure 3.8A outlines the performance of portfolio entities in meeting statutory reporting requirements for 2002-03.

FIGURE 3.8A
TIMELINESS OF FINANCIAL STATEMENT COMPLETION, PRIMARY INDUSTRIES PORTFOLIO *(a)*

Finalisation of audited financial statements (no. of weeks after end of financial period)	*2002-03*		*2001-02*	
	Number	*Per cent (cumulative)*	*Number*	*Per cent (cumulative)*
Less than 8 weeks	1	7	1	8
8 to 10 weeks	2	21	-	8
10 to 12 weeks	4	50	-	8
12 to 14 weeks	2	64	2	25
14 to 16 weeks	4	93	2	42
More than 16 weeks *(b)*	1	100	7	100
Total	**14**	**-**	**12**	**-**

(a) Includes all audited financial statements as at 31 October 2003.
(b) Includes the financial statements of one entity that had not been finalised at the date of preparation of this report.
Source: Victorian Auditor-General's Office.

3.8.6 Figure 3.8A shows that **there has been significant improvement in the overall timeliness of completion of audited financial statements by entities in this portfolio, with 50 per cent of entities meeting the 12-week statutory completion time frame in 2002-03 compared with 8 per cent in the previous year**. Only one entity had not completed its financial reporting obligations after 16 weeks. Notwithstanding this positive result, significant scope exists for further improvement in future periods. Appendix A to this report shows details of the financial statements and the issue of the audit opinions.

3.8.7 A number of factors contributed to the failure of entities to meet the 12-week reporting time frame, including:

- delays by entity governing boards in providing formal approval of financial statements;
- in relation to the department, difficulties encountered in complying with the requirements of the machinery of government changes; and
- for a number of smaller portfolio agencies, a lack of appropriately qualified and experienced personnel to prepare the financial reports.

Quality of financial reporting

3.8.8 During the 2002-03 audit cycle, we observed some improvement in the quality of financial reporting by entities within the portfolio, generally related to the presentation and disclosure of information within the financial statements. The key factor contributing to this trend was that only minor changes to the reporting framework occurred during the year.

3.8.9 Despite the general trend towards improved financial reporting processes, a number of difficulties were encountered, particularly in relation to the implementation by the Department of the significant changes resulting from the machinery of government changes. As these impacts were specific to 2002-03, they are not likely to result in any ongoing difficulties in financial reporting.

Adequacy of control environment

3.8.10 A key responsibility of the management of each entity is to establish and maintain a sound control environment and an adequate system of internal controls to ensure that:

- the entity's financial records and other information completely and accurately reflected its activities;
- its assets are safeguarded; and
- errors are prevented or detected.

3.8.11 For those entities subject to detailed controls review, the 2002-03 financial audit process confirmed that the associated systems of internal control were generally satisfactory. However, various matters were identified which required management attention. The most common of these issues are outlined below.

FIGURE 3.8B
CONTROLS ISSUES IDENTIFIED AND REPORTED DURING THE 2002-03 FINANCIAL AUDIT CYCLE

Subject area	*Issues identified*
Governance	• Need to maintain on-going management and oversight of the shared services arrangements (by the department). • Need to improve the structure of audit committees.
Financial management and reporting	• Lack of segregation of duties within a number of smaller portfolio agencies. • Inadequate financial performance of commercial ventures. • Lack of pro-active management of the collection of accounts receivable. • Failure to conduct proper account reconciliations.
Accounting for assets	• Inaccuracies in the reporting of acquisitions and disposals of items of property, plant and equipment. • Inappropriate capitalisation of expenditure.
Other	• Excessive leave balances.

3.8.12 These matters were referred to the relevant agencies. We will review the remedial action taken to address the issues as part of our 2003-04 audit cycle to assess whether appropriate management responses have been developed to mitigate the risks identified.

Other issues of significance

3.8.13 Comments follow on a number of the issues of particular significance arising from the 2002-03 financial audit process.

Melbourne Market Authority – Investment in Fresh Chain Ltd

3.8.14 The Melbourne Market Authority is the majority (88.5 per cent at 30 June 2003) shareholder of Fresh Chain Ltd, a company incorporated in May 2001. The principal activity of the company was the development of an electronic trading system and internet portal environment for the horticultural industry, and the ongoing provision of this system to the industry. However, due to the poor financial performance of the company, its directors resolved to cease all operations and close the business on 30 June 2003.

3.8.15 My Office did not audit the company, as it is not a wholly-owned entity of the State or the Authority.

3.8.16 Figure 3.8C provides an outline of the total investment in Fresh Chain over the 26 months it operated.

FIGURE 3.8C
FUNDS INVESTED IN FRESH CHAIN
9 MAY 2001 TO 30 JUNE 2003
($'000)

Item	*Amount*
Total funds invested	**14 182**
Total revenues	12
Total expenses	13 885
Accumulated losses	**13 873**

3.8.17 Of the total funds of $14.2 million invested in Fresh Chain, the Melbourne Market Authority provided $13.8 million, including $3 million provided as an investment through a debt for equity swap, $6.05 million provided in the form of a repayable loan and $4.75 million in assets purchased and held by Melbourne Market Authority for the benefit of the company. In addition, the final winding-up procedures for the company are likely to give rise to additional costs of approximately $75 000.

3.8.18 At the time of preparation of this report, the Melbourne Market Authority was endeavouring to sell its Fresh Chain assets.

3.8.19 It is my intention to review this matter and report to Parliament on the outcomes of the review in the 2004 Autumn Session.

Establishment of shared service arrangement

3.8.20 As a result of the recent machinery of government changes, a shared service arrangement was established between the Department of Sustainability and Environment and the Department of Primary Industries for the provision of various services, including information technology, financial and human resource systems, and payroll services. Under the agreement, the Department of Primary Industries has the primary responsibility for the provision of these services.

3.8.21 This arrangement was entered into to enable the efficient and effective delivery of services that were previously provided centrally by the former Department of Natural Resources and Environment and that were deemed to be most efficiently delivered as shared services into the future. The ongoing management and monitoring of the shared services is undertaken through a committee established to oversee the operation, comprising representatives from both Departments.

3.8.22 Both Departments have advised that through the inter-departmental committee, they will continue to monitor the appropriateness of the shared service arrangement and the associated costs, to ensure it remains cost-effective.

Part 3.9

Sustainability and Environment

PORTFOLIO OVERVIEW

3.9.1 The Sustainability and Environment portfolio comprises the Department of Sustainability and Environment and a large number of entities that mainly operate within the water sector. The Minister for Environment and Water and the Minister for Planning have responsibility for the Department and specific responsibility for individual entities within the portfolio.

3.9.2 Figure 3.9A provides the profile of portfolio entities with 30 June 2003 balance dates, for which we have audit responsibility.

FIGURE 3.9A
TYPE AND NUMBER OF AUDITED AGENCIES WITHIN THE SUSTAINABILITY AND ENVIRONMENT PORTFOLIO, AT 30 JUNE 2003
(number)

Reporting entity	*Number*
Department	1
Metropolitan water bodies	4
Regional water authorities	15
Rural water authorities	6
Catchment management authorities	10
Waste management groups	16
Companies, trusts and joint ventures	5
Other public bodies	14
Total	**71**

Source: Victorian Auditor-General's Office.

3.9.3 The Department of Sustainability and Environment was established in December 2002 as part of the machinery of government changes that came into effect following the State election. Under the new structure, the Department assumed responsibility for certain outputs previously delivered by the former Department of Natural Resources and Environment, and the Department of Infrastructure.

3.9.4 The Department has broad responsibility for the provision of leadership in the management of Victoria's environment, both natural and built, and a strong focus on sustainable development. In particular, the Department's primary functions include:

- nature and biodiversity conservation;
- facilitating effective and efficient water management;
- public land management of forests, coasts, alpine resorts, Crown land reserves and parks;
- identifying and promoting sustainable resource use and management practices among industries and the general community; and
- promoting sustainable development.

3.9.5 The activities of other portfolio entities mainly include the:

- provision of water and waste water services;
- management of catchments and waterways;
- water industry regulation and guidance; and
- management of related public infrastructure and other assets.

3.9.6 Some of the key financial statistics associated with the portfolio include:

- total portfolio expenditure of around $2.6 billion, including $1.4 billion associated with the activities of water sector entities and $320 million provided in the form of grants to other parties;
- user charges of around $2.2 billion collected by water sector entities; and
- management of a substantial asset portfolio, including water infrastructure assets valued at $13.2 billion and land managed by the Department valued at $2.6 billion - mainly comprising Crown land, national parks and associated reserves.

3.9.7 During 2002-03, portfolio entities also provided $355 million in dividend payments to the State. These dividend payments are largely sourced from Melbourne's 3 water retailers and Melbourne Water Corporation.

RESULTS OF FINANCIAL AUDITS

Audit opinions issued

3.9.8 Clear opinions were issued on the financial statements of all portfolio entities, which represented an improvement on the prior year where a number of qualified opinions were issued.

3.9.9 An "emphasis of matter" was included in our audit report on the financial statements of Casey's Weir and Major Creek Rural Water Authority. The emphasis of matter indicated that negotiations were continuing for the Goulburn-Murray Rural Water Authority to take over the Authority's property, rights, liabilities, powers and functions under the *Water Act* 1989. As a result, there was significant uncertainty on whether the Authority would continue to exist as a separate entity into the future.

Timeliness of reporting

3.9.10 Figure 3.9B outlines the performance of portfolio entities in meeting the statutory reporting requirement during 2002-03.

FIGURE 3.9B
TIMELINESS OF FINANCIAL STATEMENT COMPLETION, SUSTAINABILITY AND ENVIRONMENT PORTFOLIO *(a)*

Finalisation of audited financial statements (no. of weeks after end of financial period)	*2002-03*		*2001-02*	
	Number	*Per cent (cumulative)*	*Number*	*Per cent (cumulative)*
Less than 8 weeks	7	10	5	7
8 to 10 weeks	9	23	3	12
10 to 12 weeks	24	56	14	32
12 to 14 weeks	20	85	38	87
14 to 16 weeks	9	97	5	94
More than 16 weeks *(b)*	2	100	4	100
Total	**71**	**100**	**69**	**100**

(a) Includes all audited financial statements as at 31 October 2003.
(b) Includes the financial statements of 2 entities that had not been finalised at the date of preparation of this report.
Source: Victorian Auditor-General's Office.

3.9.11 Figure 3.9B shows that **there has been significant improvement in the overall timeliness of completion of audited financial statements by entities, with an increase from 32 per cent to 56 per cent in the number of entities meeting the 12-week statutory completion time frame**. A very small percentage of entities had not completed their financial statements after 16 weeks. Notwithstanding this improvement, scope exists for further improvements in future periods. Appendix A to this report records information about the financial statements and date of issue of the audit opinions for each entity.

3.9.12 A number of factors contributed to the failure of certain agencies to meet the 12-week statutory time frame. These included:

- Difficulties encountered by the Department in complying with the requirements of machinery of government changes, mainly relating to the formal verification of assets and liabilities transferred to the Department upon its establishment;
- For the smaller portfolio agencies, a lack of appropriately qualified and experienced personnel with sufficient time to dedicate to the task of preparing the financial statements; and
- A number of entities had not developed and agreed with us appropriate financial report preparation plans. This lack of planning led to delays in the timeliness financial statement preparation as well as the subsequent audit process.

Quality of financial reporting

3.9.13 The quality of financial reports of entities within the portfolio continues to improve, as demonstrated by the resolution in the year of all 2001-02 audit qualification issues.

3.9.14 Despite the general trend towards improved financial reporting processes, a number of difficulties were encountered, particularly by the Department in relation to the implementation of the machinery of government changes. These impacts were of a specific nature and are not likely to result in ongoing difficulties in financial reporting.

3.9.15 **The development and implementation of financial statement preparation plans remain vital steps in the successful completion of entity financial statements. Our Office and portfolio entities will continue to work together to facilitate the effective planning of the 2003-04 financial year-end process.**

Adequacy of control environment

3.9.16 A key responsibility of the management of each entity is to establish and maintain a sound control environment and an adequate system of internal controls to ensure that:

- the entity's financial records and other information completely and accurately reflected its activities;
- its assets are safeguarded; and
- errors are prevented or detected.

3.9.17 For those entities subject to detailed controls review, the 2002-03 financial audit process confirmed that the associated systems of internal control were generally satisfactory. However, various matters were identified which required management attention in some agencies. The more common of these issues are outlined below.

FIGURE 3.9C
AUDIT ISSUES IDENTIFIED AND REPORTED DURING THE 2002-03 FINANCIAL AUDIT CYCLE

Subject area	*Issues identified*
Governance	• Continuing weaknesses in the structure and role of some audit committees, including inadequate audit committee charters.
Asset management	• Inadequate reconciliation by the Department of Crown land records with external data. • Failure to identify inappropriate rates of depreciation. • Delays in updating fixed asset records, resulting in the inclusion of assets that have been previously disposed.
Transaction processing and review	• Lack of control over access to, and changes of, key information such as vendor masterfiles. • Poor segregation of duties and lack of compensating control procedures. • Inadequate management of delegation limits. • Failure to conduct key reconciliations in a timely manner. • Lack of review or retention of key reports evidencing control procedures.
Use of technology	• Adoption of new technology, such as wireless networking, without appropriate security upgrades. • Users with excessive and unnecessary system access. • Lack of formalised business continuity planning. • Lack of physical security over key technology assets.

3.9.18 These matters were referred to the relevant agencies. We will review the remedial action taken to address the issues as part of our 2003-04 audit cycle.

OTHER ISSUES OF SIGNIFICANCE

3.9.19 Comments follow on a number of other issues of significance arising from the 2002-03 financial audit process.

Department of Sustainability and Environment

Valuation of Crown land

3.9.20 During 2002-03, the Department engaged the Valuer-General to undertake a revaluation of all Crown land managed and reported in the financial statements of the Department. This process represented a significant investment of resources by the Department.

3.9.21 Although the revaluation was completed during the period, the impact was not incorporated into the financial report of the Department due to concerns raised as to the appropriateness of applying the fair value (in essence market value) methodology to Crown land. On the basis that the Department is progressively moving to fair value, in accordance with the requirements of the relevant accounting standard, this position was accepted for 2002-03.

3.9.22 **The Department agreed that the valuation basis to be used for Crown land assets needs to be resolved in the coming year.**

Completeness of Crown land records

3.9.23 The Department is responsible for recording the State's holdings of Crown land. Approximately 70 per cent of the individual parcels of Crown land are managed directly by the Department and recorded in the Department's financial statements. The remaining 30 per cent of the parcels are directly managed by other departments and agencies and, accordingly, are reported in the financial statements of those agencies.

3.9.24 Over many years, we have had concerns about the inability of the Department to confirm the completeness of its records of Crown land managed by external departments and agencies. Consequently, the Department has not been in a position to ensure that all Crown land is completely and accurately reflected in its records, or that its records are consistent with the records of other Crown land managers.

3.9.25 The Department has commenced a review of its records to address this situation, but at the date of preparation of this report, little progress had been made on this task. Ultimately, this process should enable the periodic reconciliation of Crown land holdings between the primary departmental records and the records of other agencies.

Recommendation

3.9.26 We recommend that the Department continue to pursue its review of the accuracy of its records of Crown land, in co-operation with other agencies managing Crown land.

Resolution of Seal Rocks litigation

3.9.27 Our previous reports to Parliament have referred to the dispute between the operator of the Seal Rocks Life Sea Centre, located on Crown land at Point Grant on Philip Island, and the State in relation to various aspects of the contractual agreements.

3.9.28 During 2002-03, the Department of Sustainability and Environment settled the dispute associated with the Centre. **The resolution involved the payment of $42.9 million to the former operators of the Centre. In addition, the Department incurred around $13 million in legal and other costs over the 3-year period of this dispute**.

Recommendation

3.9.29 Given the finalisation of this matter and its cost to the State, we recommend that the Department, in consultation with other stakeholders, undertake an ex-post review of the management of the original agreement and subsequent legal resolution, with the aim of identifying areas for future attention/improvement that could in turn reduce the risk of similar issues arising in the future.

Water sector

Overview of financial operations

3.9.30 An important element of portfolio responsibilities is the operations and performance of 25 entities within the water sector. Within this group are 3 sub-sectors; the metropolitan sector consisting of Melbourne Water and the 3 metropolitan water retailers; the regional sector consisting of 15 regional water authorities; and the rural sector consisting of 6 authorities.

3.9.31 The key activities of entities within this sector are the provision of water and waste water services in an environmentally sustainable manner. In providing these services, the authorities are required to operate in a ”commercial” manner. With the exception of the 6 rural water bodies, all the authorities are required to pay dividends to the Consolidated Fund, based on a percentage of the profits generated after allowing for certain “non-assessable” transactions. Although profit-based dividends are not required from rural water authorities on an annual basis, these authorities are required to make payments to the State from time-to-time.

3.9.32 Figure 3.9D provides a summary of some key financial statistics associated with water sector operations for 2002-03:

FIGURE 3.9D
WATER SECTOR - SUMMARY FINANCIAL INFORMATION, AT 30 JUNE 2003
($million)

	2002-03				*2001-02*
	Metropolitan	*Regional*	*Rural*	***Total***	*Total*
Financial performance -					
Total revenue	1 531	503	134	**2 168**	1 999
Total expenses	975	435	158	**1 568**	1 508
Profit/loss (pre-tax)	556	68	(24)	**600**	491
Dividends paid to government	353	1	1	**355**	276
Financial position -					
Cash assets	8	202	29	**239**	294
Infrastructure assets	6 060	4 710	2 469	**13 239**	12 743
Borrowings	2 186	109	-	**2 295**	2 264

3.9.33 The overall financial result achieved by the water sector in 2002-03 was a profit before tax of $600 million, which represented an increase of $109 million on the previous year. This improvement mainly resulted from strong revenue growth (of around 9 per cent) during 2002-03, principally driven from increased developer contributions received by water authorities, both in cash and assets, associated with the development of new residential estates. However, an overall loss of $24 million (2001-02, $18 million) was recorded by rural water authorities. This was mainly attributable to the level of depreciation costs, associated with the high value of infrastructure assets managed by these authorities, not being fully recovered through the current pricing levels.

Asset valuation in the water sector

3.9.34 Two major issues require attention over the next 12 months in relation to the valuation of assets in the water sector. The first relates to the application of current accounting standards by entities and the second relates to inconsistencies in the basis of valuation used by metropolitan water authorities, and rural and regional water authorities. These are discussed below.

3.9.35 Under current accounting standards, infrastructure assets can be valued at either their cost or their estimated fair value. Current Government policy requires public sector entities to utilise the fair value basis of valuation for infrastructure assets.

3.9.36 During 2002-03, the Minister for Finance extended an exemption granted in previous years to entities within the water sector from applying the above asset valuation policy. This exemption allowed water sector entities to retain previous valuations.

3.9.37 The exemption was of particular importance to the regional water authorities which, having previously revalued their assets over a number of years, faced the prospect of significant asset write-downs. Given the range of opinion regarding the appropriateness of the application of a commercial "profitability" based test to the assets of water sector authorities, and the potential for international accounting standards to again change the valuation requirements, the exemption has provided a degree of "breathing space" to the sector that will enable a more considered approach to be taken to the valuation of its assets.

3.9.38 The potential impact was more significant for the rural and regional authorities, than for Melbourne Water and the 3 metropolitan water retailers, given that these bodies currently value their assets at cost and, as such, the likelihood of an asset write-down is less likely.

3.9.39 **The cost method of valuing assets is available under existing accounting standards, however, the impact of the current situation (whereby some entities value their assets at cost while others record them at valuation), reduces comparability between entities operating in the same sector.**

3.9.40 **The current inconsistency in asset valuations increases the difficulties associated with the comparison of water sector entities.**

Recommendation

3.9.41 **We recommend that steps be taken by the authorities to ensure that an appropriate and consistent asset valuation basis is established across the water sector.**

Processes for approval of revenue waivers

3.9.42 A large number of entities within the portfolio, particularly those operating within the water sector, provide services to commercial customers in return for fees and charges levied for those services. During the year, we identified an instance where City West Water waived unbilled fees and charges totalling $243 000 in relation to a commercial customer. The authority's management advised that the amounts were waived in order to achieve an outcome combining ongoing financial viability with a significantly improved environmental outcome.

3.9.43 Our review indicated that the processes adopted by the authority did not ensure that adequate documentation was prepared to support the premise that the waiver of this amount would impact on the financial sustainability of the customer. As a result, the authority could not adequately demonstrate that an appropriate basis existed for the waiving of a significant amount of revenue.

3.9.44 Given the large number of commercial operations within the authority's client base, it is likely that many of these operations will experience varying degrees of financial hardship at various points in time, and may request assistance in the form of debt relief or waivers.

Recommendation

3.9.45 **We recommended that the authority review and update its current policy and guidance relating to debt relief and waivers to ensure consistency in the treatment, processing and consideration of all customers' requests for financial relief.**

***RESPONSE** provided by the Chief Executive Officer, City West Water*

While these cases rarely occur, City West Water will review and update its guidelines for commercial customer debt relief to ensure consistency of process, but retain sufficient flexibility to handle each case on its individual merits in order to achieve the most appropriate outcomes.

Review of performance indicators in the water sector

3.9.46 During the year, we undertook a preliminary review of the performance indicators disclosed by water sector authorities in their 2001-02 annual reports. The review was limited to assessing the accuracy and completeness of the performance indicator information and did not involve an assessment of the appropriateness of the indicators. The review was also undertaken to assist the sector to develop performance statements that can be audited.

3.9.47 Our overall conclusion was that **the reported indicators were generally supported by information that was complete and accurate. However, a number of areas were identified where improvements could be made to the current systems and procedures to increase the robustness of the recorded information and, therefore, increase confidence in the accuracy of the data generated**.

3.9.48 **We will review performance indicators reported in the 2002-03 annual reports. The aim of this review will be to determine what improvements have been achieved since our previous year review and to continue to work, in consultation with the sector, towards the development of a statement of performance which can be audited in the annual reports of entities**.

***RESPONSE** provided by the Secretary, Department of Sustainability and Environment*

I am pleased to note that you have reported an overall improvement in terms of the timeliness and quality of reporting as well as the provision of clear opinions on the financial statements of all portfolio entities. Your recommendations in respect to improvements are agreed and the required management attention to the issues will receive appropriate priority.

The Department has also agreed with your recommendations regarding other issues of significance which arose from the audit process in respect to Crown land and as well as the resolution of Seal Rocks litigation. A collective approach to Crown Land management is required across the state and the Department will initiate the appropriate action to progress this.

***RESPONSE** provided by the Secretary, Department of Sustainability and Environment - continued*

With respect to matters raised in your overview of the water sector, which is in part included in the portfolio overview and also in the other issues of significance section, the Department agrees with your recommendations and advises that pricing principles and asset valuation will be examined as part of the White Paper formulation process early in 2004. The Department recognises the importance of consistent valuations in increasing comparability of entities operating within the sector, and is working with water sector agencies to establish this principle.

The Department notes that City West Water has accepted the recommendation regarding requests for financial relief. A review of the process will be undertaken to ensure consistency and equity in all future decisions.

The Department further notes your intention to review performance indicators reported in the (water sector) 2002-03 annual reports, and agrees that the development of an annual statement of performance is important in increasing the transparency of achievements within the sector.

CENTRAL GIPPSLAND REGION WATER AUTHORITY WASTE MANAGEMENT OPERATIONS AT DUTSON DOWNS

Background

3.9.49 The Central Gippsland Region Water Authority is Victoria’s second largest non-metropolitan water authority. The Authority is responsible for the provision of water and wastewater services to over 130 000 people located in 41 towns in Central Gippsland, in Eastern Victoria. Of the State’s 15 regional water authorities, the Authority is the largest in terms of the volume of water supplied and wastewater treated.

3.9.50 Since the mid-1980s, the authority has also operated a prescribed industrial waste business, which involves the treatment and storage of prescribed waste received from industry for a fee. The authority currently handles 70 per cent of all prescribed waste generated in the Gippsland region, and around 2 per cent of prescribed waste generated in Victoria.

3.9.51 Industrial waste is produced from industrial, commercial and trade activities such as car repair workshops; dry cleaning services; fast food chain stores; food processing plants; chemical, paint and plastics manufacturers; dental surgeries; and hospitals.

3.9.52 In Victoria, industrial waste incorporates both liquid and solid industrial waste. Historically solid industrial waste has been stored in approved landfill sites, while liquid industrial waste is either classified as:

- Trade waste, which is processed through the wastewater treatment plants of water authorities; or
- Non-trade waste, which is directed to a stabilisation facility (intermediate processor), which turns the liquid into a semi-solid material. This material is used as landfill, in facilities licensed to accept such waste.

3.9.53 The *Water Act* 1989 provides the authority for water bodies to accept trade waste, while the Environment Protection Authority (EPA) is the regulatory authority for all industrial waste.

Prescribed industrial waste management in Victoria

3.9.54 In 1999, the Victorian Government established a bipartisan Hazardous Waste Consultative Committee (HWCC), with responsibility for developing a policy for the future management of hazardous wastes. The following year, the HWCC issued a report recommending that the use of landfill for the long-term storage of prescribed industrial waste be phased out.

3.9.55 In December 2000, the Government accepted the recommendations outlined in the HWCC report, including the adoption of its proposed *Industrial Waste Management Policy (Prescribed Industrial Waste).* At that time, the Government publicly announced the phasing-out of landfill for hazardous waste, and the development of safe and effective alternative facilities.

3.9.56 These alternative facilities included:

- soil recycling facilities;
- repositories for hazardous wastes for which recycling, re-use or treatment technologies were likely to be available in the near future; and
- long-term containment facilities for the remaining hazardous waste.

3.9.57 That same year, the Government released its Hazardous Waste Management Action Plan, *Future Directions for Industrial Waste Management in Victoria*. The plan gave effect to the findings and recommendations of the HWCC's report and incorporated a comprehensive industrial waste management strategy.

3.9.58 In establishing the plan, the Government aimed to:

- put in place measures to ensure that the environment is fully protected from prescribed industrial wastes;
- ensure industry had access to the facilities and support it needed to deal with the unavoidable wastes created through the production of goods and services;
- move Victoria to a situation where it was operating at world's best practice in waste management; and
- minimise the amount of waste generated in the State.

3.9.59 Part of the strategy includes diverting contaminated soil from landfill to specialised treatment facilities and the use of repository and containment facilities, the performance of which can be monitored and controlled to ensure long-term safety.

3.9.60 As contaminated soil makes up more than 35 per cent of all hazardous waste going to landfill in Victoria, the government made the provision of soil recycling and treatment facilities its first priority.

3.9.61 In March 2001, the Hazardous Waste Siting Advisory Committee (HWSAC) was established, to advise the Government in relation to the siting of future soil recycling and treatment facilities. HWSAC comprised representatives from State and Local Government, industry, unions, and environment and community groups.

3.9.62 While HWSAC was responsible for identifying sites for the State's first soil recycling and treatment facility, Major Projects Victoria is now responsible for the identification and recommendation, to the Minister for Major Projects, of suitable sites for future soil recycling and treatment facilities. The EPA is responsible for implementing the statutory framework and, in particular, the Industrial Waste Management Policy (Prescribed Industrial Waste).

3.9.63 In May 2001 the EPA established the Prescribed Industrial Waste Advisory Committee (PIWAC) to advise the Authority on:

- priorities for classifying wastes;
- setting waste reduction targets and specifications for repositories and long-term containment facilities;
- measures to reduce hazardous waste generation and establish specifications for alternative facilities to landfills; and
- the classification of wastes that should no longer be placed in landfill.

3.9.64 At this time, the Authority had been reviewing options for generating additional revenue from its under-utilised Dutson Downs site and was aware of the Government's desire to establish soil recycling facilities in Victoria. One option examined by the Authority, in late 2001, was the establishment of a Resource Recovery Facility on a small portion of the site. One of the intentions for this facility was for it to be used for the recycling of contaminated soils and the storage of the residual waste products generated from the soil recycling process. In November 2001, following its deliberation, the Authority submitted an expression of interest to the HWSAC proposing its Dutson Downs property as a possible site for the State's first soil recycling facility.

3.9.65 In May 2002, the HWSAC submitted a report to the Minister for Major Projects, which assessed a number of potential sites for the location of soil recycling and treatment facilities, against an established set of criteria. All of the sites assessed by the HWSAC, with the exception of Dutson Downs, either failed to meet the environmental requirements or the proponents withdrew their application.

Basis for the audit

3.9.66 Strong local community interest and concern was generated following the Authority's announcement that it was proposing to establish a soil recycling facility at Dutson Downs. In response to the significant level of public interest in the Authority's waste management operations, the Auditor-General decided to review these operations, with particular emphasis on the Authority's compliance with its EPA licence conditions.

Audit objective

3.9.67 The primary objective of the audit was to undertake a compliance review of the Authority's current waste management operations, and to review the monitoring and supervisory role performed by the EPA. The audit was also intended to provide an outline of the Authority's proposed future soil recycling facility and the likely impact of this operation on the Authority and the local community.

Audit scope

3.9.68 The audit scope encompassed a review of the Authority's current waste management operations, including:

- compliance with legislative and EPA licence requirements;
- public relations management; and
- EPA's monitoring and oversight of these operations.

3.9.69 The audit also included a review of the Authority's proposed future soil recycling facility; and the statewide management of contaminated soils.

Current waste management operations

3.9.70 In 1985, an EPA licence was granted to the Authority for the purpose of receiving and disposing of solid and liquid waste prescribed under the relevant environmental protection regulations.

3.9.71 The Authority's waste management activities are primarily conducted at its Dutson Downs site, a property of 8 300 hectares located 15 kilometres south-east of Sale. The majority of the site (52 per cent) is currently used for agricultural activities such as grazing, cattle breeding and timber plantation, with 45 per cent of the site remaining in an essentially undisturbed state.

3.9.72 A small portion of the property, some 250 hectares, is utilised for the treatment and storage of prescribed industrial waste under licence from the EPA. Part of the site is also used for the treatment of sewage.

3.9.73 The property is located in the hinterland of the Gippsland Lakes region, with the Gippsland Lakes coastal park situated along the north-eastern boundary of the property. The lakes region has been classified as wetlands of international importance under the Ramsar Convention.

3.9.74 The south-eastern border of the property runs parallel to The Ninety Mile Beach and is about 2 kilometres from the sea. The nearest township is Golden Beach / Paradise Beach which is 9 kilometres from the centre of the site and 7.5 kilometres from the outermost boundary of the area currently used for waste treatment and storage. Although the permanent population of this township is around 200 people, the area of coastland adjoining the site, along with many other coastal areas in Victoria has experienced strong population growth over the last few years.

3.9.75 As indicated earlier, a distinction is drawn between trade waste and other industrial waste.

Trade waste

3.9.76 As with other communities across the State, significant volumes of wastewater are generated by urban communities, commercial businesses and industrial operations in central Gippsland. This wastewater must be collected, transferred, treated and disposed of without harm to the environment. The Authority provides this service through its sewerage system, which includes 12 wastewater treatment plants licensed by the EPA. Once treated, the wastewater is discharged to inland waterways, land and sea via 2 ocean outfall pipelines.

3.9.77 Dutson Downs began accepting wastewater in 1957 when its first regional outfall sewer was commissioned. In June 1992, the ocean outfall at Delray Beach (Dutson Downs) commenced operations. The Saline Waste Outfall Pipeline (SWOP) ocean outfall off McGauran's Beach was commissioned in late 1982, and during 2000 became the first ocean outfall to be granted an accredited EPA licence in Victoria.

Industrial waste (other than trade waste)

3.9.78 In 1985, the EPA issued a licence for the acceptance of specified prescribed industrial waste. Under this licence, the Authority is permitted to receive a variety of wastes including:

- waste from grease traps;
- waste oil and water mixtures;
- milk, vegetable, fruit and food processing effluent;
- soil contaminated by oil and oil products and sands and scale sludges removed from offshore and onshore oil and gas processing facilities and which are contaminated with oil;
- septic tank sludge; and
- biosolids from sewage treatment plants.

3.9.79 The organic wastes have been either land farmed or deposited in shallow bio-remediation trenches to allow aerobic (use of natural, oxygen-requiring bacteria to dispose of waste) or anaerobic (use of natural, non-oxygen-requiring bacteria to dispose of waste) degradation of the wastes.

3.9.80 Non-biodegradable works are currently stored, by type of waste, in 20 metre landfill trenches with a naturally occurring clay lining. Once filled, these trenches are labelled and covered with a layer of soil and clay.

3.9.81 In 1995, the Authority was issued with a licence to accept tannery and asbestos waste. The following year, the Authority ceased land-farming activities for liquid wastes and commenced operation of a biodegradable liquid waste facility. In July 2000, the EPA removed the regional restriction clause in the Authority's license, allowing the Authority to accept specified waste from outside the Gippsland region.

3.9.82 During 2001-02, significant capital works were undertaken at the site which included:

- construction of a new road and site entrance;
- installation of a weighbridge and an additional liquid waste unloading bay;
- construction of a waste stabilisation plant for the treatment of oily sludges containing naturally occurring radio-active material (NORM); and
- building of a basic laboratory and an office complex.

Newly constructed entry, office complex and laboratory on site.

3.9.83 The major types of industrial waste accepted at the site and the volumes received in 2001-02 and 2002-03 are outlined in Figure 3.9E.

FIGURE 3.9E
TYPE AND VOLUMES OF INDUSTRIAL WASTE RECEIVED AT THE DUTSON DOWNS SITE

Type of waste	*Volume 2001-02*	*Volume 2002-03*
Biodegradable prescribed waste	12 397 tonnes	16 899 tonnes
Biodegradable non-prescribed waste	1 650 tonnes	2 702 tonnes
Tannery waste containing chromium	3 903 tonnes	4 678 tonnes
Tannery waste – Other	462 tonnes	390 tonnes
Biosolids (for Re-Use)	2 769 tonnes	1 202 tonnes
Contaminated soils	388 tonnes	456 tonnes
Asbestos	10.2 tonnes	627 tonnes
Saline wastewater	2 043 tonnes	213 tonnes.
Non-prescribed waste	1 506 tonnes	2 702 tonnes.
Number of loads received	2 780 loads	2 628 loads

Source: Central Gippsland Region Water Authority.

What we expected to see

3.9.84 If the waste management operations at the Dutson Downs site were managed in an efficient and effective manner, we would expect the Authority and the EPA, through its regulatory role, to ensure that these operations do not adversely impact on the environment, local communities, and individuals working or visiting the site. This would be achieved by ensuring:

- compliance with the Authority's legislative requirements;
- the site is an appropriate location for waste treatment and storage;
- facilities located on the site are appropriate for the current waste management operations;
- only wastes licensed to be received on that site are accepted;
- treatment and storage of waste is in accordance with EPA requirements;
- on-site handling procedures are adequate;
- potential risks impacting on the operations are adequately identified and managed;
- waste management operations are adequately monitored by the Authority and the EPA;
- any leakage from storages is quickly identified and appropriate action taken;
- the Authority has the technical capability to operate a waste management business;
- details of waste management operations and the results of environmental testing are adequately reported; and
- waste management operations are efficient and provide an adequate return on the investment of community resources.

Compliance with legislative requirements

3.9.85 As indicated earlier, the broad legislative classification of waste received by water authorities is largely determined by how it is transported. Trade waste is essentially waste received through an authority's sewerage system, while non-trade industrial waste is transported by other means, most often by road. This classification is different to that adopted by the EPA, where particular types of waste are prescribed when they are likely to have a detrimental effect on public health or the environment. The disposal of these particular types of wastes is required to be licensed by the EPA.

3.9.86 Although the Authority has operated a waste management business at Dutson Downs since the 1950s, some local residents have questioned whether it had the legislative authority to operate such a business. It was also claimed by some members of the local community, that the Authority had been accepting waste from outside the Latrobe Valley without the required ministerial approval. Our investigation of these issues disclosed the following.

3.9.87 The operations of all water authorities are governed by the *Water Act* 1989, which provides them with powers in respect to catchment, distribution and usage of Victoria's water resources, as well as the authority to operate sewerage systems. The Act also provides Authorities with the power to accept trade waste which is defined as any:

- waterborne waste (other than sewage) which is suitable, according to the criteria of an Authority, for discharging into the Authority's sewerage system; or
- other matter, which is declared by a by-law made under the Act to be trade waste.

3.9.88 Historically, the Authority also had specific legislative power to accept other waste under schedule 8 of the Act. This schedule, which specifically related to the former Latrobe Valley Water and Sewerage Board, (the Authority's predecessor body), expanded the approved functions of the Authority to include the receipt of the following waste for treatment or disposal:

- waste from any person in the Latrobe Valley; and
- with the approval of the Minister, waste from any person outside the Latrobe Valley.

3.9.89 In the mid to late 1990s, during the former Government's legislative water reforms, this schedule to the Act was repealed. Unfortunately, in removing the schedule, the Authority's statutory power to accept non-trade waste was also removed. **In the absence of this schedule, the Authority was inadvertently operating a waste business at Dutson Downs since the late 1990s without legislative authority.**

3.9.90 In June 2003, this situation was remedied by the passing of the *Essential Services Commission and Other Amendments Act* 2003, which also amended the *Water Act* 1989. Under the amendments to the *Water Act* 1989, the Authority's functions have been expanded to include the receipt of waste from any person, whether inside or outside the sewerage districts managed and controlled by the Authority, for treatment or disposal by the Authority.

3.9.91 The Act describes waste as:

- trade waste or any sewage, whether that waste or sewage is untreated, treated or partially treated;
- any matter that is offensive or injurious to human life or health;
- any ash, coal dust or matter that may discolour or impart discolouration to water; and
- any other matter that the Authority by by-law declares to be waste.

3.9.92 In essence, these amendments provide the Authority with the legislative power to continue its non-trade waste business at Dutson Downs. A section included in the amendments to the Act also provides retrospective approval for the operation of the Authority's waste management business. This section states that:

> "Anything done or purported to have been done under this Act by the Central Gippsland Regional Water Authority, before the commencement of Section 8 of the Water Legislation (Essential Services Commission and Other Amendments) Act 2003 that would have been validly done had that section been in operation has, and is deemed to have had, the same force and effect as it would have had if that section had been in operation".

3.9.93 **Our inquiries have led us to conclude that the omission of the legislative power for the Authority to operate its non-trade waste business in the legislative reforms of the late 1990s was unintentional. Accordingly, the Authority's action in continuing the business was not contrary to the intention of the Government, which was always to allow the Authority to continue its waste management activities as it had done in the past.**

3.9.94 Authority staff indicated to us that when this issue came to their attention, 2 separate legal opinions were obtained and legal advice was sought from the Department of Sustainability and Environment. The legal advice received by the Authority, while not definitive, indicated that the general provisions in the Act probably allowed it to undertake a non-trade waste business.

3.9.95 Our investigations indicated that, although waste had been received from outside the region, the required Ministerial approval had not been obtained.

3.9.96 The Authority advised us that as the EPA had issued a license amendment, allowing the Authority to accept industrial waste from outside its region, it was, therefore, reasonable to assume that ministerial approval was implicit in the licence approval.

3.9.97 However, we do not consider that the issuing of a licence by an entity responsible to the Minister, such as the EPA, is a substitute for formal ministerial approval.

Recommendation

3.9.98 Given the events outlined above, we consider that the Authority and the Department would benefit from a re-examination of the internal processes in place to oversee and manage legislative reform. Such a review would help ensure that the potential for a re-occurrence of similar events in the future is minimised.

Planning and environmental approvals process

3.9.99 In order for an organisation to establish or alter its waste management operations, it basically requires 2 separate approvals:

- land use planning approvals under the *Planning and Environment Act* 1987, either through a planning permit or a planning scheme amendment process; and
- a works approval and licence under the *Environment Protection Act* 1970.

3.9.100 In most cases, planning approvals are sought from local councils and works approvals from the EPA. A works approval application can be considered jointly with a planning approval application, thereby enabling the one panel to consider both applications and make recommendations to the responsible planning authority and the EPA.

Environmental effects statement

3.9.101 Under the *Planning and Environmental Act* 1987, the Minister for Planning has the power to require an environmental effects statement (EES) to be prepared as part of the planning approval process. In addition, under the *Environment Effects Act* 1978, the Minister with responsibility for the proposed works can have these works declared as public works for the purposes of the Act. If such a declaration is made and published in the Government Gazette, an EES must be prepared.

3.9.102 The EES assesses the environmental effects or impacts of the proposed works. The preparation of the EES requires a significant amount of public consultation. The preparation of the EES reflects good practice where the proposed works may have an adverse impact on the environment.

3.9.103 The Authority undertook an EES in 1984, which covered operations involving the receipt and storage of specified wastes. Since that date, other wastes such as tannery and asbestos waste have been received by the site, and works have been undertaken to construct a waste stabilisation plant for the treatment of oily radioactive sludges (NORM). Despite these changes to the business, no further environment effects statements have been prepared.

3.9.104 When this issue was raised with the EPA, the Authority indicated that it was of the view that the additional types of wastes subsequently received by the site did not warrant the preparation of a new EES. The Authority considered that the original EES determined that the site was appropriate for the treatment and storage of prescribed industrial waste and that any additional environmental concerns were adequately addressed through the works approval process. In effect, the EPA considered that time and cost associated with the preparation of a new EES could not be justified.

3.9.105 We are not in a position to determine whether the changes to the Authority's waste business since 1984 created new environmental concerns, which justified the preparation of a new EES. Given the ongoing concern regarding the waste management operations at Dutson Downs, the preparation of a new EES may have been justified in that it would have helped to ensure a greater degree of public confidence in the Authority's management of its waste business.

EPA approval processes

3.9.106 EPA licensing involves the issuing of a works approval for the construction of facilities to be used for the treatment and storage of waste, and licensing of the waste management operations undertaken on the site.

Works approval

3.9.107 Before an organisation can construct waste management facilities, it must prepare and submit, to the EPA, specifications for the construction of waste disposal and storage facilities for inspection and approval. Under the *Environment Protection Act* 1970, the EPA is required to consider each application based on its consistency with environmental objectives and criteria, as established in the State Environment Protection Policies (SEPPs) and Industrial Waste Management Policies (IWMPs).

3.9.108 The primary purpose of the works approval process is to assess whether the proposed works are consistent with the state environment protection policies and waste management policies, and whether the proposal is likely to cause or contribute to pollution or environmental hazard.

3.9.109 The works approval process will also help ensure the:

- appropriateness of the site for the proposed waste management operations;
- adequacy of treatment and storage facilities; and
- appropriate placement of these facilities on the site.

3.9.110 A significant concern of the local community is the potential for contaminated wastes to escape the various means of containment, as a result of floods or other environmental events, and for toxins contained in those wastes to escape into nearby rivers and streams, including the Gippsland Lakes. The works approval process is one of the mechanisms used by the EPA to ensure that the surrounding environment is not exposed to these toxins.

3.9.111 In determining the appropriateness of the proposed works, the EPA considers factors such as:

- the proximity of the site to other sensitive uses;
- average annual rainfall on the site;
- whether the land is subject to flooding;
- proximity of the works to the local watertable; and
- impact of the proposed operations on significant ecological and archaeological sites.

3.9.112 The works approval is also used to ensure that the storage facilities are constructed to meet certain standards and appropriately located on the site.

3.9.113 **In relation to the risk to the environment and the community, we are satisfied that the current waste management facilities on the Dutson Downs site have received appropriate works approval. Implicit in this approval was that the site proposed for the facility met all the environmental and safety requirements specified by the EPA**

3.9.114 Based on environmental testing conducted by the EPA and other technical experts, there is no evidence of groundwater or soil contamination from the current operations. This leads us to believe that the Authority's current waste management processes, and its management of hazardous wastes to date is of a standard that reduces the risk of an adverse event from these operations on the environment or the community to an acceptable level.

Appropriateness of the site for current waste management operations

3.9.115 Studies recently undertaken by Gippsland Water show that groundwater under the waste treatment and storage site is 6 to 9 metres below the surface and that this water is separated from the stored waste by a 1.5 to 9 metre layer of virtually impermeable clay.

3.9.116 In addition to this thick layer of clay, the Authority has recently undertaken the additional precaution of lining landfill trenches during construction with a 1.5 mm thick geomembrane (plastic) to further reduce the potential for leakage.

Landfill trench under construction being lined with geomembrane.

3.9.117 During the audit, it was suggested to us by a party external to the Authority, that the abovementioned clay layer does not provide a continuous barrier across the site and was likely to be broken in parts by gravel intrusions. If these intrusions do exist, they can effectively act as a drain transporting contaminants into groundwater systems and, ultimately, into the nearby lakes.

3.9.118 Testing of this clay layer during environmental studies, undertaken by the Authority, found no evidence that these gravel intrusions exist. This conclusion was based on the samples taken from a number of test wells dug across the site to measure the thickness of the clay layer. Given that it is not feasible to test the consistency of the clay layer across the entire site, it is not possible to categorically establish the existence or otherwise of these intrusions.

3.9.119 We acknowledge that there is no perfect site for the location of a waste management operation. However, in selecting a site consideration should be given to:

- whether the risks associated with the waste operations can be reduced to an acceptable level with appropriate management; and
- the potential impact on staff, the community and the environment if an adverse event were to occur.

3.9.120 Based on environmental testing conducted by the EPA and other technical experts, there is no evidence of groundwater or soil contamination from the current operations. This leads us to the view that the Authority's current waste management processes is of a standard that the risk of an adverse event has been reduced to an acceptable level.

3.9.121 In developing criteria for siting future industrial waste facilities, the Government has taken into account:

- The risks these operations are likely to present to the environment and local communities from a scientific perspective; and
- community expectations.

3.9.122 With the inclusion of community expectations, the criteria established by the Government are of a higher standard than if they were based purely on scientific grounds.

3.9.123 Given siting criteria, and the likelihood scientific standards and community expectations will continue to evolve, the Department should continually reassess the suitability of the Dutson Downs site for the management of industrial waste.

Environment improvement plan

3.9.124 On 10 April 2001, the Authority was granted a works approval for the establishment of a waste stabilisation plant and associated waste disposal facility. This facility was designed to stabilise and store oily residue wastes from oil and gas extraction and refining operations. This waste contains low levels of naturally occurring radioactive materials.

3.9.125 The facility was completed in February 2002, with the EPA issuing the Authority with an amended licence, to incorporate the operation of the new facility, on 21 January 2003. The amended licence required an Environment Improvement Plan (EIP) for the site to be completed by 1 March 2003.

3.9.126 Guidelines issued by the EPA in June 2002, require an EIP to be prepared as a condition of a works approval for new developments. The guidelines require the EIP to be completed prior to the commissioning of any works.

3.9.127 EIPs are strategies, designed to facilitate the continuous improvement of an organisation's environmental management. These documents can be prepared at the initiation of the organisation, may be required as a licence condition to replace detailed prescriptive conditions in licences, or may be directed by the EPA to be prepared in accordance with section 31C of the EPA Act.

3.9.128 As the draft EIP covers the entire waste management operations (including the new works) conducted on the Dutson Downs site, it is likely that the plan:

- in relation to these new works, replaces the detailed prescriptive conditions normally found in the licence; and
- provides a strategy to improve the entire waste management operations on the site.

3.9.129 In August 2001, the Authority's Dutson Downs Advisory Committee was assigned responsibility for the preparation and adoption of the plan (in consultation with the EPA).

3.9.130 At the time of the audit, a draft EIP had been prepared and had been provided to the EPA for comment. **As a result, an EIP had not been submitted to the EPA for approval by the date specified in the Authority's licence**. Authority staff advised that the delays had arisen as they considered the issues surrounding the plan to be too critically important to the local community to be rushed. Rather, the Authority preferred full discussion and consideration prior to final adoption of the plan.

3.9.131 We note that at November 2003, the EIP has still not been finalised and approved by the EPA.

Recommendation

3.9.132 **While acknowledging the amount of work involved in preparing a comprehensive improvement plan, and the need for adequate community involvement in its development, the Authority should ensure that the plan is finalised, formally adopted by its board of management, approved by the EPA and implemented as a matter of priority.**

Compliance with operating licence

3.9.133 As indicated earlier, the Authority has been licensed to receive prescribed industrial waste at its Dutson Downs site since March 1985. This license has been amended on a number of occasions, the most recent of which was on 21 January 2003.

3.9.134 The Authority's current licence enables it to receive prescribed industrial waste under defined conditions. The licence has 4 major sections, the specific requirements of which are:

- *Waste management* - Specifies those wastes that may be deposited at the site and the general conditions under which this may occur;
- *Environment Improvement Plan and operational controls* - Outlines the requirements for the authority to prepare and regularly review its EIP. Good waste management processes required to be undertaken by the Authority to ensure the protection of the environment are also included in this section;
- *Monitoring and reporting* - Specifies the monitoring procedures required to be undertaken by the Authority, and the requirements for it to regularly submit reports on its waste management operations to the EPA; and
- *Plan of premises* - Requires a plan of the premises, covered by the licence.

3.9.135 Our review included an examination of each of these areas to determine whether the Authority has been complying with the requirements of its licence. The Authority's EIP was discussed in the previous section, with our observations in respect of the remaining sections of the licence outlined below.

Waste management

3.9.136 This section reviews the policies and procedures in place to ensure that only wastes stipulated in the Authority's licence are accepted by the facility and the handling of wastes on site is in accordance with licence requirements.

Receipt of approved wastes

3.9.137 We reviewed the procedures adopted by the Authority to ensure that only approved wastes are accepted for treatment and storage at the Dutson Downs site. **We found that the Authority's procedures for inspecting, weighing and testing of waste received, were robust, functioning effectively and were in accordance with licence requirements.**

3.9.138 As a result, we are satisfied that only wastes approved for receipt, under the Authority's license, are accepted. The results of random inspections, undertaken by the EPA as part of its normal monitoring functions, also indicated that the Authority is accepting only approved wastes.

Handling of wastes on site

3.9.139 During our review, we undertook an inspection of the Dutson Downs site and observed the Authority's waste handling and treatment processes. This inspection covered all of the Authority's waste management activities, including the treatment of biodegradable liquid wastes and oily sludges containing naturally occurring radioactive material (NORM), and operation of the Authority's waste stabilisation pits and the landfill trenches.

Recently constructed waste stabilisation pit.

3.9.140 Our observations indicated that formal on-site waste handling procedures have been established and are generally operating effectively. We also observed Authority personnel working at various locations and noted that they practiced a satisfactory degree of care and prudence in carrying out the waste management functions. Our observations were also supported by the independent EPA monitoring of site operations.

3.9.141 **Based on these observations, we are satisfied that the Authority's treatment and storage of wastes is in accordance with EPA licence requirements.**

Monitoring and reporting of adverse environmental impacts of waste management operations

3.9.142 The Authority's licence requires it to establish procedures to monitor and regularly report to the EPA and the Department of Sustainability and Environment on the environmental impact of waste management operations at the site. In essence, the purpose of these reports is to make sure that adequate procedures are in place to ensure that adverse environmental events, such as the leaching of toxins or other contaminated materials from storages and into the surrounding environment, are quickly identified and appropriate action taken.

3.9.143 Requirements imposed upon the authority include:

- regular and ongoing sampling and testing of the various waste types at the site (such as wastewater sampling, bore analyses and independent testing by authorities such as NATA), and for reporting of the sampling and test results to the EPA in accordance with licence-prescribed frequencies and conditions; and
- preparation of monthly, quarterly and/or annual reports outlining the findings of the testing program.

3.9.144 A large network of monitoring bores has been established on the site. Samples from these bores are regularly taken and tested to determine whether contaminants contained in the bore sample fall within limits set by the EPA and specified in the Authority licence. Testing of samples, taken to date, have not indicated any negative impact of the Authority's waste management operations on the site's groundwater.

Part of the network of monitoring bores on the site.

3.9.145 Where any leakage of contaminants is identified, a management strategy has been developed to adequately address such an event. This strategy is included in the Authority's draft EIP.

3.9.146 **Our review indicated that the authority has complied with its monitoring and reporting obligations as contained in its EPA licence.**

Plan of premises

3.9.147 The Authority's licence also requires that a plan of the premises covered by the licence be created and provided to the EPA. Our review disclosed that the Authority had complied with this requirement.

Gippsland Water Dutson Downs Advisory Committee

3.9.148 The Dutson Downs Advisory Committee was established in August 2001 to closely examine a number of issues relating to past, current and future practices at the Dutson Downs site, with an overall objective of establishing an Environment Improvement Plan for the operations. The Committee is made up of a wide cross-section of representatives from community groups, tourism bodies, local government and local industries. Since its inception, the Committee has met on 18 occasions.

3.9.149 The Committee has an oversight function in relation to the development of the Authority's EIP. Following a review by the Committee of the key environmental concerns relating to waste management at the Dutson Downs site, the following issues requiring action were identified:

- communication of plans and activities;
- non-sustainable current practices;
- reduction of new wastes requiring long-term storage;
- degraded areas of Dutson Downs;
- habitat improvement;
- odour and amenity;
- site management; and
- remediation of contaminated soils.

3.9.150 The Committee membership comprises of representatives from the Authority, industry, local residents and government instrumentalities. As such, the Committee has been a valuable mechanism for the consideration and resolution of issues affecting the Authority's waste management business. It was, therefore, pleasing to note that the Authority's Board recently approved the continuation of the Committee for the foreseeable future.

3.9.151 Overall, we consider that the Committee has been operating effectively, however, we noted the following issues:

- While accepting that the Committee is dealing with complicated and sensitive environmental issues, its ability to produce outputs on a timely basis could be improved. For example, although the committee's primary objective, at its establishment in August 2001, was the development of the EIP, at the date of audit review, 2 years later, the plan was still in draft form; and
- The current chairperson of the committee is employed by the EPA. Notwithstanding that this officer is centrally located in Melbourne and is not directly involved in the EPA's oversight of the Dutson Downs operations, the fact that the chairperson is engaged as a senior officer of the agency with responsibility for the regulation of the Authority's waste management operations, could be perceived as representing a potential conflict of interest.

3.9.152 In order to address these issues, consideration should be given to:

- Introducing mechanisms to ensure that the committee considers and finalises its deliberations in a timely manner; and
- Ensuring that the person appointed as chairperson of the committee is both free, and seen to be free, of any potential conflict of interest.

Risk management

3.9.153 Risk management, which covers strategic, operational and financial risks, is designed to minimise the impact of detrimental events on an organisation's business. In effective organisations, development of a risk management framework is a key component of the organisation's corporate planning process. This framework would normally involve:

- establishing an organisation-wide process to identifying events likely to have a detrimental impact on the business;
- assessing the probability of each identified event occurring, and determining the consequences resulting from its occurrence; and
- developing strategies and actions to reduce the probability of certain identified events occurring and/or the consequences of these events should they occur.

3.9.154 A sound knowledge of potential risks and a strategy to manage adverse events, enables organisations to effectively manage their risks. In particular, it enables the organisation's management to systematically trade-off the costs of an event occurring against the cost of reducing the risk. In this way, good risk management is a key driver of organisational efficiency.

3.9.155 The risks associated with the management of a waste management business are many and varied, and include financial risks, environmental risks, occupational health and safety risks, and community safety risks**.** The Authority's draft EIP includes sections, which deal with a number of these risks, such as environmental and fire risks.

Recommendation

3.9.156 **While acknowledging that some of the risks associated with the Authority's waste management business are addressed in its EIP, we consider that the Authority's waste management operations would benefit from the establishment of a separate risk management strategy.**

Fire management plan

3.9.157 Our enquiries disclosed that, while the Authority had established arrangements with the local Country Fire Authority to manage the risks of fire in its forest plantation, the Authority had not established an emergency event management strategy. While recognising the Authority's intention to establish this strategy (to be included in the EIP), we were surprised, considering the length of time the site has been operating, that such a plan had not already been developed, adopted and regularly tested for readiness.

Recommendation

3.9.158 **We recommend that the Authority's emergency management strategy, incorporating fire protection procedures, be established by the Authority, following consultation with the local Country Fire Authority branch and other local emergency services.**

Community safety

3.9.159 During our visit to the Dutson Downs site, we noticed that the fencing around the perimeter of the property was of varying standards, with most of the property easily accessible by members of the community.

3.9.160 In addition to the contaminants stored on the site, the sewage settling ponds, the storage for biodegradable wastes and the infrastructure, could pose a significant threat to anyone venturing onto the site, particularly small children and youths.

3.9.161 The size of the property and the high cost of constructing secure fencing, make it prohibitively expensive to adequately fence the entire site. One solution may be to securely fence only the land on which the Authority's waste management operations are located.

Pubic relations management

3.9.162 Over the years, and more intensely in recent months, the Authority's waste management operations at Dutson Downs have attracted significant local interest. More recently, the level of statewide public interest has increased as it has become increasingly apparent that Dutson Downs is likely to become the location of Victoria's first soil recycling facility and, as a result, contaminated soils from throughout the state will be transported to the site.

3.9.163 In order to manage the sensitivities surrounding its waste management processes, the Authority, over the past 2 years, has adopted a policy of openness, transparency and accountability in regards to its Dutson Downs operations.

3.9.164 This policy has resulted in the following communication and consultative activities:

- numerous open days have been held at the site for members of the public;
- site tours conducted for groups such as the Wellington Shire Council, West Gippsland Catchment Management Authority and local Rotary clubs;

- discussions with other community consultation committees, such as the Authority's Environment and Customer Committee and the Coastal Advisory Committee, on environmental management issues relating to Dutson Downs;
- presentations at public meetings;
- provision of information on its waste management operations on its website;
- full adherence and participation in the community consultation strategy adopted by the HWSAC;
- engagement of professional public affairs consultants to advise the Authority on its public relations management;
- annual customer satisfaction survey;
- establishment of a formal customer complaints system; and
- discussions with individuals and community groups, on request, on specific environmental management and operational performance issues.

3.9.165 The Authority has indicated that a strategic issues management group has also been established, which includes the chairman of the Board and the chief executive officer. This group often considers communication issues and reports its findings to the Board each quarter. Our inquiries indicated that, notwithstanding the above array of communication activities, the Authority had not developed and adopted a formal communications strategy incorporating a set of communication objectives, medium to longer-term strategic plans to achieve these objectives and a formal means of evaluating the effectiveness of its communications strategy. The Authority indicated to us that it had made some progress in this regard and intended to finalise and adopt its strategy in the very near future.

Recommendation

3.9.166 **Considering the importance of maintaining effective communication with its local residents and interest groups, we recommend that such a strategy be completed and adopted without delay.**

3.9.167 We also reviewed complaints raised by the local community in relation to issues such as unusual odours, dust and smoke emanating from the site. **This review disclosed that complaints were generally followed-up by the Authority in a prompt manner and satisfactory explanations were provided as necessary.**

Technical capability of the Authority

3.9.168 We acknowledge that historically the Authority's waste management operations have complied with EPA requirements. However, it is generally accepted that, based on the current environmental standards for waste management operations, the Authority's past environmental performance was somewhat lacking. Two obvious examples of this were:

- the use of partially treated wastewater to irrigate land on the Dutson Downs site, which resulted in most of the land, currently used for agricultural purposes, becoming degraded; and
- discharge of contaminated waters into Lake Coleman, which has resulted in significant contamination of the lake.

3.9.169 **However, based on the evidence available to us, the Authority's recent performance in managing its waste management operations at Dutson Downs has been sound, with testing conducted indicating that these operations have had little or no impact on the surrounding environment.**

Reporting on waste management operations

3.9.170 As indicated earlier, the Authority's EPA licence requires regular reports on the waste management operations and environmental impacts to be provided to the EPA and the Department of Sustainability and Environment.

3.9.171 The Authority also provides information on its waste management operations in its annual financial reports, and on its website.

3.9.172 Our review generally found this information to be compliant with the Authority's licence requirements. **However, we consider that the transparency of the Authority's waste management operations could be improved through the provision of additional financial information and more information on the impact these operations are having on the environment and the local community.** This information should be made publicly available in the Authority's annual report and on its website.

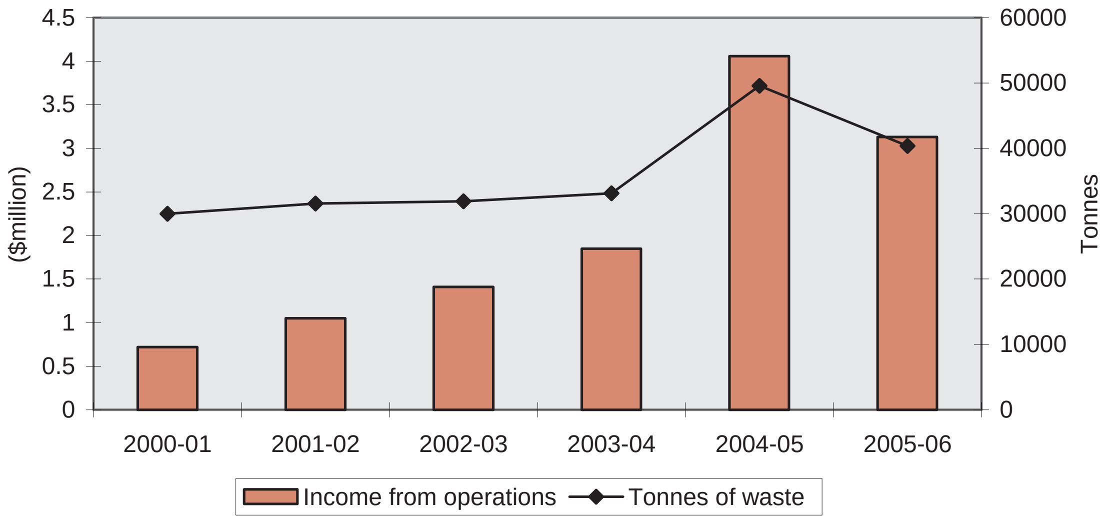
3.9.173 While reviewing information provided to the Department, we also noted that there was a lack of formal feedback from the Department in regard to this information. We can only conclude from this observation that the Department is happy with the operations of the waste management business. However, some periodic formal feedback from the Department would have provided us with more evidence that the Department's oversight function was operating effectively.

Efficiency of waste management operation

3.9.174 Figure 3.9F outlines the amount of waste received and the income generated by the Authority from its waste management operations over the last 3 years, and its projections for the next 3 years. Figure 3.9F shows that in respect of the past 3 years, the annual volume of trade waste accepted by the site increased slowly, while the income from the Authority's waste management activities increased at a somewhat faster rate. This trend is expected to continue into the 2003-04 financial year.

3.9.175 In 2004-05, the Authority predicts a significant increase in the volume of industrial waste accepted and the revenue generated from this waste. This sharp increase reflects the impact of the Authority's proposed soil recycling facility, which is expected to be operational by mid-2004.

FIGURE 3.9F
VOLUMES RECEIVED AND REVENUE EARNED FROM WASTE OPERATIONS

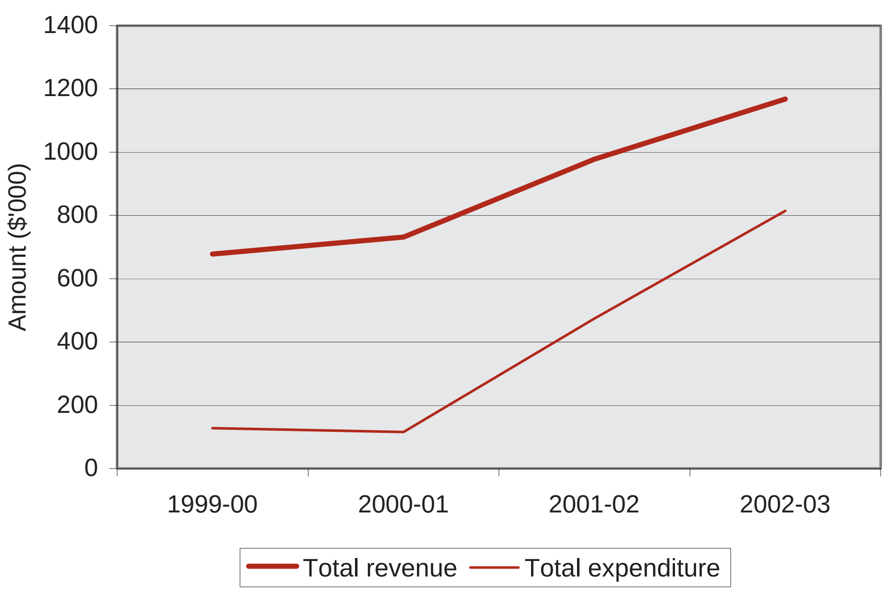


Source: Gippsland Water.

3.9.176 It can be seen that the business has generated average annual profits of around $500 000, over the last 4 years. With the area of the Dutson Downs property currently used for its waste management business, valued at approximately $3.8 million, the Authority is generating a return on its investment in this business of around 13 per cent.

3.9.177 This amount represents a good return, particularly when compared with the return generated on assets invested in other parts of the Authority's business.

FIGURE 3.9G
REVENUE GENERATED AND EXPENSES INCURRED
FROM THE AUTHORITY'S WASTE MANAGEMENT OPERATIONS



Source: Gippsland Water.

3.9.178 The above stated profits and return on investment figures are dependent on the Authority identifying and appropriately allocating its costs between its various business activities. In undertaking this audit, we have accepted the costing information provided by the Authority and have not verified the adequacy of its costing systems or the accuracy of cost allocations between the Authority's separate businesses.

3.9.179 The above financial analysis is based on short-term historical returns. The nature of the current waste operations is that the revenues generated are directly related to the volumes of waste accepted and stored on site. Costs associated with the maintenance of the site and its storage facilities will continue long after the storage capacity of the site is fully utilised and revenues have ceased. Therefore, the short-term comparison of revenues and expenses is unlikely to provide an indication of the long-term profitability of the business.

3.9.180 The Authority has not undertaken a long-term financial evaluation of its waste management business.

Monitoring and oversight by the EPA

3.9.181 The EPA is the State's regulatory agency responsible for environmental issues. In regards to the Authority's waste management operations, the EPA is responsible for the issue and monitoring of the Authority's operating licence.

3.9.182 Broadly speaking, the EPA carries out its responsibilities in regard to the Authority by:

- regularly receiving information on the types and volumes of waste transferred to the Dutson Downs facility, and arbitrating on any disputes between the Authority and waste disposers;
- examining and approving plans and specifications pertaining to the construction of waste processing and storage structures on the site;
- receiving, examining and acting on (where required) reports submitted by the Authority in compliance with the licence requirements; and
- undertaking a program of random tests and site inspections.

3.9.183 During our examination of the waste management activities at Dutson Downs, we visited the regional office of the EPA and held discussions with EPA staff. Based on our review, we consider that the EPA is effectively fulfilling its role in connection with the licensing of the Dutson Downs facility. We also noted that a close and co-operative working relationship exists between the Authority and the EPA, and that a system of regular monthly meetings between the 2 entities was an important contributing factor to this relationship working effectively.

3.9.184 We also examined actions taken and reports generated by the EPA following its investigations of complaints or inquiries received from local residents. We concluded that, overall, these matters were efficiently and effectively dealt with by the EPA.

3.9.185 During our review of the regulatory functions performed by the EPA, in respect to the Authority's licence, we noted that the EPA does not prepare, at the commencement of each year, a detailed plan outlining proposed visits and site inspections. We consider that the preparation of such a plan would help ensure regular inspections were carried out and that these functions were undertaken in an effective manner. Such a plan should be considered for immediate implementation.

Major issues currently confronting the Authority

3.9.186 The Authority currently faces a number of important issues and challenges that impact on its specific waste management activities and its operations more generally. A number of the major issues are outlined below.

Regional outfall sewer

3.9.187 The Authority's regional outfall sewer and pipeline receives domestic and industrial wastewaters in bulk from towns and major industries serviced by the Authority. This pipeline plays an important economic role in Gippsland, particularly for the service it provides to industries of State and National significance such as Australian Paper, Loy Yang Power, Hazelwood Power and National Foods.

3.9.188 The piped section of the sewer runs some 40 kilometres from Morwell to Rosedale, and then generally (with the exception of a section in the Longford area) by open trench for the remaining 43 kilometres to the Dutson Downs site. The treatment of the sewage basically involves a natural biological breakdown of the waste, which occurs during its 60 to 70 kilometre journey from Morwell and the time it spends in the Dutson Downs settlement pond. Once the treatment is complete, the effluent is discharged to Bass Strait via an Ocean Outfall at Delray Beach.

3.9.189 The open sewer section of the pipeline continues to cause unrest with the local community and negatively impacts on the Authority's image. The major issue relates to odour sometimes experienced by local residents and visitors to areas surrounding the open section of the pipeline. This odour occurs despite the Authority injecting oxygen and oxide iron salts into the sewage at various points during its journey to facilitate its decomposition and reduce the smell.

3.9.190 We note that the Authority's current sewage treatment processes, in particular the open sewer, are not to the world's best practice standard proposed by the EPA.

3.9.191 A report recently commissioned by the Authority examined the options available to address the outfall sewer and suggested that an opportunity exists for a significant wastewater re-use facility located at the source of the outfall sewer. In the longer-term, this scheme could lead to the elimination of the outfall sewer entirely. If the facility is implemented, it is projected that up to 30 megalitres of water per day, currently discharged to the ocean, could be redirected for either industrial or environmental use.

3.9.192 At the date of our review, the Authority was undertaking further feasibility studies to assess the viability of this proposal and the financial and environmental benefits that may be generated for the Gippsland region. The scale of this project is significant and has the potential to be one of the largest environmentally-sustainable wastewater re-use facilities in Victoria. Significant investment will be required in order to establish this facility, with early estimates indicating that the cost of such a project could be in excess of $160 million.

Recommendation

3.9.193 Given the Government's recent initiative to increase the re-use of Victoria's wastewater resources and the sensitivities of this issue, it is important that the Authority complete its feasibility study as soon as possible, and that the local community and industry is kept fully informed of the study's progress.

Naturally occurring radio-active material (NORM)

3.9.194 Most Australians benefit either directly or indirectly from the medical, industrial and scientific use of radioactive materials. Use of these materials generates a small amount of radioactive waste including lightly contaminated soil, plastic, paper, laboratory equipment, smoke detectors, exit signs and gauges.

3.9.195 Between 1995 and 1998, the Authority received 22 loads (120 kilolitres in total) of water containing amounts of oils and sand, for which it was licensed by the EPA to accept. In 2000, during a review of performance indicators in regional water authorities, we became aware that this waste contained naturally occurring radioactive materials (NORM). At that time, the Authority contended that the existence of NORM was only made known to it on 14 February 1999.

3.9.196 NORM is an inevitable by-product of petroleum exploration and production, which is naturally contained within the fluids that are extracted from gas and oil wells, and is typically found in low concentrations, but potentially high volumes.

3.9.197 The Department of Human Services (DHS) has responsibility for the regulation of NORM waste. The *Health (Radiation Safety) Regulations* 1994, incorporated under the *Health Act* 1958, require a license for the disposal of substances prescribed by the regulations as radioactive.

3.9.198 These regulations are designed to ensure that public exposure to ionising radiation is kept within defined limits. The regulations are formulated around high concentration, low volume sources such as those found in medical procedures and, as a consequence, they do not adequately cover NORM wastes.

3.9.199 In 1999, the Authority conducted a field survey of radioactivity levels in the area in which NORM wastes were treated and stored. The field survey indicated that the levels of radioactivity detected were similar to background levels evident in adjacent agricultural sites.

3.9.200 Following advice from DHS, the EPA and independent radiation experts, such as the Australian Radiation Protection and Nuclear Safety Agency (ARPANSA) and the Radiation Advisory Committee (attached to DHS), the Authority was satisfied its past practice of storing these materials in landfill, generated levels of radioactivity which were very low and presented no risk to human safety or the environment.

3.9.201 On receipt of a risk assessment report from ESSO/BHP (prepared by ARPANSA), DHS granted both ESSO/BHP and the Authority an exemption under the Act, which enabled the Authority to continue its previous practice of depositing this waste in landfill at Dutson Downs, providing a number of conditions were met.

3.9.202 Due to the long life of radioactive materials and the proximity of the site to internationally recognised wetlands, some community members have expressed concerns about the use of this site for the storage of this waste. Although the risk of serious contamination is very low, the Authority has been working with ESSO/BHP to establish a world's best practice facility for the containment of these wastes at the site. This facility was commissioned in February 2003.

3.9.203 The Authority has indicated to us that the facility has so far met all of the requirements outlined in its EPA Works Approval and licence.

Biodegradable liquid waste disposal

3.9.204 Biodegradable liquid wastes accepted by the Dutson Downs site are currently deposited in a lagoon on the property, historically referred to as the "Cardboard Pond". **The EPA advised that the current practices used by the Authority to manage its biodegradable wastes did not represent world's best practice.**

3.9.205 As a consequence, the EPA recently requested that the Authority change its waste management practices in relation to biodegradable liquid wastes, to allow for the recovery of organic material for reuse. The Authority, in conjunction with Collex (its technology partner), is currently developing appropriate technologies for the management of these wastes. The objective of this work is to develop a process to produce a stable organically rich solid material for agricultural applications.

3.9.206 The Authority is also developing a strategy for the rehabilitation of the "Cardboard Pond", including the removal and stabilisation of organic solids that have accumulated in the lagoon over a number of years. Appropriate provision of resources, to fund the proposed rehabilitation works has been made in the Authority's business plan.

Proposed soil treatment and recycling facility

3.9.207 Soil from properties used to operate gas works, paint or chemical factories, petrol stations or for other industrial, agricultural or commercial uses often become contaminated. In the past, the accepted practice was to excavate the polluted soil and dump it in an approved landfill site.

3.9.208 In 2000 there was a change in government policy. The objective of the new policy was to reduce the amount of waste produced and encourage recycling of wastes. This required the establishment of soil recycling facilities and the phasing-out of landfill for the storage of contaminated soils.

3.9.209 As indicated earlier, the Hazardous Waste Siting Committee nominated the Dutson Downs site, as an appropriate location for a soil recycling facility. The Minister for Major Projects accepted this recommendation and, in July 2003, formally announced that the Dutson Downs property was a suitable site for a soil recycling and treatment facility.

3.9.210 Following acceptance of the site, the Minister invited the Authority to proceed to the statutory approvals phase. This involved the Authority seeking planning and EPA approval for the proposed facility.

3.9.211 The Authority's original intention was to establish a new soil treatment and recycling facility, a short-term storage facility and a long-term containment facility. Wastes were to either be:

- processed to create usable products;
- retained in secure short-term storage for future processing and re-use, or
- stabilised for secure long-term containment or future destruction.

3.9.212 The Authority has now decided not to continue with the short-term storage repository or the secure long-term containment facility. The current proposal for the facility, as outlined in its works approval, will involve the Authority undertaking the following processes:

- acceptance and short-term storage of contaminated soils;
- pre-treatment and preparation;
- soil treatment;
- blending and composting; and
- re-use and recycling.

Treatment technology

3.9.213 After pre-treatment and preparation of contaminated soils, the Authority proposes one or more of the following technologies to treat these soils.

- enhanced bioremediation;
- chemical fixation;
- catalytic oxidation; and
- thermal desorption.

3.9.214 An outline of the proposed treatments is provided below.

Enhanced bioremediation

3.9.215 Bioremediation uses natural biological processes to treat and premeditate soils contaminated with organic pollutants, typically petroleum hydrocarbons. In essence, bacteria are used to breakdown the organic contaminants to carbon dioxide and water.

3.9.216 Enhanced bioremediation involves increasing the rate and growth of microbial activity by providing an ideal environment for bacteria to exist. This environment is created through the injection of air and the addition of minerals, nutrients and moisture into the soil.

3.9.217 The enhanced bioremediation system proposed is a fully enclosed in-vessel system, which will allow air and leachate to be captured and recycled, and facilitate treatment by the build-up of moderate temperatures up to 55^{C} via natural processes. This system is currently used for composting and treatment of grease trap waste at Dandenong.

Chemical fixation

3.9.218 The chemical fixation process involves the addition of materials to solidify the soil in order to produce an insoluble heavy metal complex within the soil. This process is specifically designed for soil contaminated with heavy metals such as lead, zinc, copper, chromium, cadmium, nickel, selenium, arsenic and mercury.

3.9.219 The process minimises the potential for heavy metals to leach from the soil, treating heavy metal contaminated soils to a far greater degree than most alternative processes.

Catalytic oxidation

3.9.220 The catalytic oxidation process incorporates the use of processing proprietary re-agents for the remediation of contaminated soils. In particular, this process is specifically targeted to the treatment of more complex organic species, such as PAHs, which are typically found in soil contaminated with gasworks wastes. Contaminated soils can be remediated within several days using this process.

3.9.221 The catalytic oxidation process involves the use of a treatment unit, which consists of a large hopper and a closed reaction vessel. Contaminated soil is loaded into the hopper and conveyed to the vessel. According to contaminant type, the appropriate re-agents are then added to effect remediation. The soil is typically treating to “clean fill” standards. Any hazardous material resulting from the process is captured, preventing emissions to the environment.

Thermal desorption

3.9.222 Thermal desorption is to be used for the treatment of hydrocarbon contaminants, including petroleum hydrocarbons, tarry gasworks wastes (PAHs and BTEX) and organochlorine compounds (OCs), including polychlorinated biphenyls (PCBs).

3.9.223 The process involves heating of the hydrocarbon-impacted soil to convert contaminants into gas, which is subsequently converted to water and carbon dioxide. Treatment of the gases produced by the process and the use of dust collection systems prevent contaminants from reforming.

Re-use and recycling

3.9.224 All treated soils contaminated by organic contaminants will be re-used and recycled.

3.9.225 Opportunities identified to date for re-use and recycling include:

- blending with compost for subsequent use for pasture improvement and soil conditioner on-site at Dutson Downs and or on other private property;
- bulk potting mix or garden soil for nurseries, local council and non-residential property developments; and
- clean fill for large-scale property development or site restoration projects.

Assessment of appropriate sites and operators for the State's first soil treatment and recycling facility

3.9.226 Following its establishment in late 2001, the Hazardous Waste Advisory Committee called for expressions of interest from proponents to nominate sites and/or technologies for the recycling and treatment of contaminated soils.

3.9.227 Seven proponents submitted expressions of interest on 2 November 2001, nominating a total of 11 sites: 9 in Melbourne and 2 in country Victoria. Eight sites were subsequently withdrawn from consideration due to the failure of proponents to secure tenure over sites, or to a recognition that the sites were unlikely to satisfy the siting criteria for contaminated soil re-cycling and treatment facilities. This left 3 sites, which were assessed in detail by the Committee.

3.9.228 Following the assessment process, the Committee recommended that 2 of the 3 sites reviewed proceed to the statutory approvals process. Subsequently, the other remaining site was withdrawn, leaving Dutson Downs as the only site approved by the Committee.

3.9.229 In the Committee's final report, released in May 2002, the following comments were made.

> "Notwithstanding the recommendations made in this Report, HWSAC is not convinced that the general quality of many of the sites that came forward from the proponent-led process were of an optimal standard. Consequently:
>
> - the proposals that are recommended to proceed into the statutory approvals processes may not fully meet Victoria's needs for recycling and treating contaminated soil; and

- similar proponent-nominated processes are unlikely to be viable method for identifying sites for long-term containment facilities.”.

3.9.230 **In effect, the Committee was selecting the best option from a number of less than optimal sites. One of the Committee members was so concerned about the selection process that he presented his own minority report, which was highly critical of the site selection process.**

3.9.231 Some members of the Authority’s Dutson Downs Advisory Committee, also having concerns regarding the site selection process, recommended that the Authority withdraw its Dutson Downs site proposal. Had this course of action been taken, the Government would have had to effectively re-start its site selection process.

3.9.232 While the Minister for Major Projects accepted the HWSAC recommendation that the Authority should be permitted to proceed to the statutory approval stage with its proposal, he determined that further investigation was required into the potential environmental impacts, financial viability and transport options associated with the facility, before the project could proceed further.

3.9.233 **Before providing an expression of interest to the HWSAC for its proposed soil recycling facility, the Authority undertook a preliminary assessment of the facility. However, a detailed business case and full environmental assessments were not undertaken. Given the size and significance of the undertaking, we consider that it would have been more financially prudent for the Authority to undertake these assessments prior to providing its expression of interest.**

3.9.234 Major Projects Victoria (MPV) in conjunction with the Authority, engaged GHD Pty Ltd (GHD) to investigate and report on the issues raised by the Minister. GHD produced 2 reports: one dealing with environmental concerns and the other addressing the financial viability and transport issues.

Environmental study

3.9.235 The objective of the GHD environmental study was to determine the suitability of the site for the development of a soil recycling facility. The review looked at the location of the site and its specific characteristics, including topography, history of flooding, hydrology and regional geology. Work undertaken included:

- an evaluation of stormwater flood levels;
- chemical analysis of soil and groundwater;
- geotechnical sampling, testing and evaluation of the low permeable clay layer;
- a heritage and archaeological study;
- a flora and fauna survey; and
- an air quality assessment.

3.9.236 As referred to above, the study concluded that the establishment of the proposed facility would have an insignificant effect on the surrounding environment.

Financial viability study

3.9.237 The objective of the GHD viability study was to assess the viability of a "typical best practice" contaminated soil recycling facility at Dutson Downs, incorporating a range of treatment technologies capable of dealing with all classes of contaminated soils nominated in the EPA's prescribed industrial waste policy.

3.9.238 The methodology used included:

- an assessment of the potential market demand for the treatment of different classes of contaminated soils and the Authority's potential market share of this waste;
- identification of technologies capable of treating all classes of contaminated soils nominated in the EPA policy, including the development of a base case and optional facility designs to accommodate these technologies; and
- development of a financial assessment of the base case and optional facility formats, including sensitivity analysis in the event of fluctuating volumes and assessment of the impact of alternative pricing structures.

3.9.239 The study indicated that the break-even point for the business is around 15 000 tonnes per annum. The study also indicated that the Authority would be able to implement its desired technologies and obtain a sufficient market share of contaminated soil to ensure that the facility would generate returns on its investment, which were comparable with those normally expected in the waste management industry.

3.9.240 The cost of the facility is likely to be in the order of $6 million and the Authority estimated the site could be operational within 12 months of receiving approval.

3.9.241 Discussions with staff from MPV disclosed that their initial assessment of the proposed facility indicated that the soil recycling operation is likely to generate an internal rate of return to the owners of around 14 to 15 per cent.

3.9.242 As most of the contaminated soils are close to Melbourne, processing of contaminated soils at Dutson Downs is likely to add an additional $20 per tonne in transport costs to the overall costs of recycling.

Transport study

3.9.243 Currently, all wastes transferred to the Dutson Downs site are transported by road, with approximately 14 trucks per day travelling to the Dutson Downs site to dispose of industrial waste. Once the soil recycling facility was proposed, it became apparent that, if the new facility was built, the volume of waste transferred to the site would increase and a greater portion of the wastes received would originate from outside the Gippsland region.

3.9.244 Given this likely increase in traffic to the site, community concern has been raised regarding the suitability of road transport for the movement of waste to Dutson Downs. These concerns included issues such as road safety, increases in traffic volumes, wear and tear of road surfaces, dust and odour.

3.9.245 The GHD Transport Report indicated that:

- Even if a significantly greater proportion of waste were transferred to the site from outside the Gippsland area, road transport would continue to be the most appropriate mode of transport to the site. This evaluation considered factors such as environmental impact, community exposure, safety, regulatory requirements, logistics and handling, infrastructure establishment costs, vulnerability to tampering, and transport costs; and
- The number of trucks visiting the site each day was likely to increase to 22 (57 per cent), once the proposed facility was established.

3.9.246 In reviewing the impact of the facility on local roads, the study concentrated on the Longford-Loch Sport road. The report generated following the study noted that this road was classified as a class "C" major road under the Victorian Rural Arterial Road Network Strategy developed by VicRoads, and that such roads were generally maintained to existing widths and standards based on current traffic volumes and the incidence of traffic accidents.

3.9.247 The GHD Transport Report concluded that due to the low traffic volumes currently experienced along this road, it has adequate capacity to absorb the additional traffic generated by the proposed recycling facility.

3.9.248 During the audit, we also became aware of community concern regarding the potential transport of contaminated soils through the main street of Sale. We noted that in order for the transport of contaminated soil to by-pass the city of Sale, trucks delivering waste to the site were likely to travel via the Rosedale-Longford Road. This road is narrower than the Longford-Loch Sport Road and has been classified by VicRoads as a minor road.

3.9.249 Again, the standard to which the Rosedale-Longford road is maintained will depend on the volume of traffic using the road and the incidence of accidents on the road. However, given the likely size of the trucks transporting contaminated soils and other waste to the site, and the current standard and classification of the road, it may need to be upgraded to safely accommodate the additional traffic.

3.9.250 The GHD environmental study also found that the number of trucks on the road would only increase by 4.5 per cent. These trucks will be covered so that there is no risk of spillage. There are currently 85 trucks per month (on average) utilising Gippsland roads and highways transporting Gippsland-generated wastes out of Gippsland to other regions of the State. This movement of waste is monitored by the EPA, which has responsibility for regulating the transport of waste throughout Victoria.

Risks associated with the soil recycling business

3.9.251 The decision to allow the Authority to establish a soil recycling business is a Government policy decision and as such we make no assessment as to the appropriateness or otherwise of this decision.

3.9.252 However, with all new business activities there are always additional risks, which have to be managed by the organisation. In respect of the Authority's proposed soil recycling facility, these additional risks arise due to:

- the Authority's lack of technical expertise with the proposed soil recycling processes;
- projected operating costs for the facility based on authority estimates without the advantage of prior operating experience;
- projected revenues based on volumes of soil likely to be received, the type of contaminants in the soil, the level of soil contamination and the price the market will bear to dispose of contaminated soils;
- the level of future competition the Authority is likely to face from other providers of soil recycling services;
- the Authority's lack of marketing knowledge and expertise;
- the transport of large volumes of contaminated soils from the Melbourne metropolitan area to the site; and
- environmental risks associated with treatment of contaminated soils and the storage of contaminants.

3.9.253 From a state perspective, the Government has made the decision that the benefits to the Victorian community from establishing a soil recycling facility outweigh the additional risks to the Authority, and that the facility will generate a reasonable return on the public money invested in its establishment.

3.9.254 In allowing the Authority to nominate its Dutson Downs site for the soil treatment facility, the Government is indicating that it is appropriate to have some public ownership in the soil re-cycling business. Alternatively, the provision of contaminated soil treatment services could have been left entirely to the private sector, or the site could have been made available to the private sector, through sale or lease agreement, to establish a soil recycling facility.

3.9.255 In making this decision, it is clear that the Government also considers that a significant amount of the risk associated with this business has been addressed by the Authority's partnership with Collex, which provides the Authority with the technical expertise it lacked. This was the primary reason the siting committee required the Authority to acquire a technical partner before it was willing to approve the Dutson Downs site.

Recommendation

3.9.256 **However, given the financial risks outlined above, it is imperative for both the Authority and the Department of Sustainability and Environment to closely monitor the establishment and operation of the proposed soil recycling facility.**

Other issues to be addressed

3.9.257 In progressing with its soil recycling business, the Authority will need to address a number of issues, which include the following:

Intellectual capital

3.9.258 As the proposed facility aims to introduce new technologies and practises for the treatment and storage of contaminated soils (in conjunction with Collex and the Australian Sustainable Industry Research Centre research centre), the issue of intellectual capital will need to be addressed.

3.9.259 For example, the viability of the Dutson Downs facility could be put at risk if the Authority's technical partner was to set up in competition, on another site, using new technologies developed at the Dutson Downs facility.

Recommendation

3.9.260 **It is, therefore, critical that the Authority ensures that any agreements entered into with these organisations, clearly establishes and protects the Authority's rights to the intellectual capital, created through their joint efforts.**

Cost sharing

3.9.261 Collex, as the Authority's technical partner, will necessarily have broad access to the facilities and infrastructure on the Dutson Downs site. **In these circumstances, it is important for the Authority to ensure that adequate costing systems and procedures have been developed to ensure an appropriate share of the site overhead costs are allocated to the soil recycling facility and, in turn, to Collex.**

Joint venture approval

3.9.262 Although the arrangement between the Authority and Collex has yet to be finalised, it is envisaged it will involve a joint venture arrangement between the two entities. Under the Water Act, Authorities must obtain ministerial approval prior to entering into a joint venture arrangement. **If as envisaged, the joint venture agreement is established, the Authority must ensure that the appropriate ministerial approval is obtained before the facility is established.**

Overall view on contaminated soil treatment and recycling facility.

3.9.263 Our overall view, based on the evidence available to us, is that the establishment of a soil treatment and recycling facility is both consistent with the Government's policy objectives in relation to the management of contaminated soils and provides better environmental outcomes for the State.

3.9.264 In relation to the siting of the facility at Dutson Downs, the environmental risks associated with this site, with the exception of pre-existing issues associated with long transport distances, are considered to be low. The proposed treatment and recycling processes are likely to present less risk than those currently employed for the treatment and storage of other industrial wastes on the site.

3.9.265 From a commercial viability perspective, we consider that sufficient work has been undertaken to justify the Authority's investment in the facility. However, we note that the future viability of the business is heavily reliant on the volumes of soil treated and the type of contaminants in the soil.

3.9.266 From the State's and the Authority's perspective, the facility creates a number of new risks, which need to be managed, and issues, which need to be addressed.

Statewide management of contaminated soils

3.9.267 As indicated earlier, in 2000, the Government released its Hazardous Waste Management Action Plan, *Future Directions for Industrial Waste Management in Victoria*. The central thrust of the new plan is to reduce the amount of waste needing to be managed and to phase-out the use of landfill for the storage of prescribed industrial waste.

3.9.268 Through this plan, the Government aims to put in place measures to ensure that the environment is fully protected from prescribed industrial wastes, while industry gets the facilities and support it needs to deal with the unavoidable wastes created through the production of goods and services. The Government also aims to ensure that the State's management of waste represents world's best practice and the amount of waste generated in Victoria is minimised.

3.9.269 In relation to the management of contaminated soils, the strategy includes diverting these soils from landfill to specialised treatment facilities and the use of repository and containment facilities, the performance of which can be monitored and controlled to ensure long-term safety.

3.9.270 The Government's policy of establishing soil recycling facilities, and phasing-out the use of landfill for the storage of contaminated soils, was announced in 2000. **Almost 3 years later, the State has only made limited progress in regard to establishing a soil recycling facility and appears a long way from discontinuing the use of landfill sites for the storage of this material.**

3.9.271 The EPA Information Bulletin of October 2002, *Classification for Contaminated Soil* states that: "EPA will implement the classification by amending landfill licences to prohibit the acceptance of contaminated soils once one or more facilities are developed".

3.9.272 Given the significant cost differential between re-cycling contaminated soils and dumping the soil in prescribed landfill sites at this time, this policy change was necessary to ensure that any re-cycling facilities established were economically viable.

3.9.273 The Dutson Downs facility, when fully operational, will be in a position to accept about half (30 000 tonnes) of contaminated soil generated in Victoria each year. The HWSAC report indicated that the capacity of the Dutson Downs facility would be insufficient to meet the State's annual requirement for soil recycling.

3.9.274 If applicable to all contaminated soil, adoption of the policy outlined in the EPA Bulletin, even after the Dutson Downs facility is operational, would result in insufficient capacity to re-cycle all contaminated soils. This would increase the risk of illegal dumping, stock-piling of contaminated soil by industry, or delays in development projects due to restrictions on the ability of developers to deal with contaminated soils on a timely basis.

3.9.275 The EPA advised that its Bulletin was not intended to require the compulsory recycling of all contaminated soils but will require recycling of specified contaminated soils for which options will be available in the foreseeable future. Given this intention, it will be important for the EPA to amend its bulletin to clarify the intended amendments to landfill licences.

3.9.276 There is, however, likely to be a continuing need to identify suitable sites for future waste management facilities. Given the previous concerns expressed by HWSAC with the process adopted for the selection of a suitable site for a soil recycling facility, it will be important for more effective site selection processes to be established.

Recommendation

3.9.277 **We recommend that the State establish a robust and effective site selection process. In our opinion, rather than requesting organisations to nominate sites, consideration should be given to:**

- **broadly identifying areas of the State which would be suitable for these facilities;**
- **through a review of these broad areas, identify specific sites; and**
- **once identified, use the Government's powers to compulsorily acquire these sites.**

Dispelling of some erroneous information and issues

3.9.278 Recent publicity surrounding the waste management facility at Dutson Downs has resulted a significant amount of misinformation about the facility including the following.

Toxic versus contaminated soil

3.9.279 The term "toxic" has been loosely used by some members of the community when referring to the contaminated soils that the Authority will handle if its proposed soil recycling facility is constructed. A contaminant in respect to soil is something that would not be expected to be present in the soil, or something that is present in the soil in unexpectedly high concentrations. Toxicity is the term used where a contaminant can cause harm to living organisms if those organisms come in contact with the contaminants.

3.9.280 Contaminated soils are considered toxic, or harmful to organisms, if stored in an inappropriate manner, which allows seepage of contaminants to the external environment, or interaction of organisms with the soils over an extended period of time.

3.9.281 The proposed soil recycling facility at Dutson Downs is designed to contain the soils and treat them, using a number of established processes, to either reduce the contaminants present to harmless by-products, or to extract and/or immobilise the contaminants for treatment at a suitable facility off-site and at a later date. The treated soils with contaminants removed will then be able to be re-used for activities such as land reclamation and landscaping.

3.9.282 It will be important for Gippsland Water to ensure that high calibre acceptance, storage, treatment and waste retrieval facilities and processes are utilised at the Dutson Downs site. This should be particularly important for wastes that require medium to longer-term storage.

Impact of the facility abutting an RAAF air bombing range

3.9.283 A number of recent media reports and community comments have criticised the location of the Dutson Downs facility due to its location, which is adjacent to an RAAF air bombing range. Local community fears are centred on the concern that the bombing range may be re-utilised for the RAAF's bombing practice. Such practice could result in the accidental dropping of a bomb on the site or in underground fissures opening up and allowing the seepage of contaminants into the local environment through the soil or local rivers and streams.

3.9.284 During the course of our review, we made inquiries regarding the current status of the bombing range. We were advised that the bombing range remains a "licensed" air bombing range for use by the Australian Defence Force. Although there are no current plans to use the range in the immediate future, this situation could change depending on defence requirements.

3.9.285 While the proximity of the bombing range to the Dutson Downs property represents another risk that needs to be managed by the Authority, in our opinion it is unlikely to have a major impact on the current or proposed future waste management operations on the site.

***RESPONSE** provided by Secretary, Department of Sustainability and Environment*

From the Department's perspective, I make the following observations:

- *the current waste management facilities have an appropriate works approval;*
- *the current operations meet EPA licence requirements for receiving and managing waste;*
- *the Authority is satisfactorily meeting its monitoring and reporting obligations;*
- *the technical capacity of the Authority is sound and its operations have had little or no impact on the surrounding environment;*

***RESPONSE** provided by Secretary, Department of Sustainability and Environment - continued*

- *further work is required in finalising the environmental improvement plan and in developing strategies for risk emergency and communication management. I note that DSE has now put in place guidelines for corporate governance for all water and catchment management authorities. The Department will continue to work with Gippsland Regional Water Authority on these matters.*
- *the environmental studies undertaken for the proposed soil recycling facility concluded that it will have an insignificant effect on the surrounding environment.*
- *the advice on intellectual property, equitable cost-sharing and appropriate approvals being sought for any joint venture entered into by the Authority is welcome.*

Whilst acknowledging the difficulties encountered in the site selection process, the Dutson Downs site has now been selected subject to obtaining a Works Approval from the EPA and, as noted in your report, the environment studies indicate it will have insignificant impacts.

I understand that the EPA is concerned about comments in the report about naturally occurring radioactive material (NORMS) which appear to be at odds with earlier acknowledgement that the facility has met all the requirements of the EPA Works Approval and licence.

In summary, I believe the report provides a "clean bill of health" for the current operations at Dutson Downs; it expresses satisfaction with Gippsland Region Water Authority's capacity to manage such operations; and it acknowledges that studies of the proposed soil-recycling facility indicate it will have insignificant environmental impacts.

DSE will continue to work with all water and catchment authorities on governance issues.

***RESPONSE** provided by Chief Executive Officer, Gippsland Water*

Assessment of appropriate sites and operators for the State's first soil treatment and recycling facility (paragraphs 3.9.226 to 3.9.250)

Gippsland Water would argue that it would not be financially prudent to over expend on studies whist still at an Expression of Interest phase. Note that 11 sites with 9 proponents were received and the possibility of being the successful applicant were low. The subsequent GHD study commissioned by Major Projects Victoria supported the conclusions of the Authority's preliminary study (paragraphs 3.9.226 to 3.9.234).

***RESPONSE** provided by Chairman, Environment Protection Authority*

EPA acknowledges the finding that the EPA is effectively fulfilling its role in connection with the Dutson Downs facility, and the current waste management activities have received appropriate works approval.

The proposed soil recycling and treatment facility at the Dutson Downs site will be subject to EPA assessment and public comment through the works approval process.

Planning and environmental approvals process (paragraphs 3.9.99 to 3.9.114)

Decisions about the need for an Environmental Effects Statement are the responsibility of the Minister for Planning. EPA is responsible for the issue of works approvals and licensing requirements for the operations at Dutson Downs.

Works approvals were issued to the Authority for the acceptance of asbestos in 1994, for tannery wastes in 1995, and for waste containing norms in 2001.

***RESPONSE** provided by Chairman, Environment Protection Authority - continued*

Assessment of the environmental risks associated with these wastes was undertaken as part of the works approval process.

EPA approval processes – works approval (paragraphs 3.9.107 to 3.9.104)

Works approvals assess whether a proposal is consistent with state environment protection policies, waste management policies and whether a proposal is likely to cause or contribute to pollution or environmental hazard. Assessment of the suitability of the site is considered by the works approval assessment in the context of these criteria.

Appropriateness of the site for current waste management operations

EPA has issued appropriate works approval for the current waste management facilities at Dutson Downs. Consistent with the audit findings, this site was assessed and this approval was issued as the facilities met environmental and safety requirements specified by the EPA.

Statewide management of contaminated soil (paragraphs 3.9.267 to 3.9.277)

The classification was developed in accordance with the industrial waste management policy (Prescribed Industrial Waste) 2000 in order to implement its provisions about requiring recycling or re-use of waste where practicable.

The EPA advised that the Classification does not require the compulsory recycling of all contaminated soils but will require recycling of specified contaminated soils for which options will be available in the foreseeable future. Once a facility or facilities are established, EPA would amend landfill licences to prohibit the acceptance of these specified soils.

The Classification does not preclude on-site treatment and recycling of contaminated soil. The EPA have advised that the establishment of a soil recycling and treatment facility will increase the State's capacity to recycle soil off-site which will, in some circumstances, allow land developers to move soil off site faster than may be possible with on-site treatment.We note that it will be important for EPA to implement an education and enforcement campaign to ensure that there is no illegal dumping or inappropriate stockpiling of soil as a results of any landfill bans.

Gippsland Water Dutson Downs Advisory Committee (paragraphs 3.9.148 to 3.9.152)

The Environment Improvement Plan (EIP) process is established under the Environment Protection Act and is used by EPA to enable effective input into identifying improvements in industry performance. As this mechanism is established under the Environment Protection Act, it is appropriate for EPA to chair such a committee. Further, more, EPA is unaware of any concern by current members of the Committee about having an EPA employee as the chairperson or of any concerns about potential conflicts of interest.

Monitoring and oversight by the EPA (paragraph 3.9.181 to 3.9.185)

EPA considers that the approach of planning detailed, unscheduled inspections at certain frequencies, along with inspections in response to certain events or at random times provides a more rigorous and effective inspection regime than a pre-arranged schedule.

A set frequency of inspections that effectively gives prior notice to industry is likely to prove ineffective.

CATCHMENT MANAGEMENT IN VICTORIA

Background

3.9.286 In 1994, the Government established a framework for the integrated management and protection of Victoria's water catchments. This initiative resulted in the creation of 10 catchment and land protection regions, corresponding Catchment and Land Protection Boards (CaLPBs), and the Catchment and Land Protection Council (now the Victorian Catchment Management Council). The Council is the Government's peak advisory body on catchment management.

3.9.287 Catchment management authorities replaced all CaLPBs, except for Port Phillip, in 1997. The role of the authorities incorporated the roles of the former CaLPBs, river management boards, and community-based advisory groups such as salinity plan implementation groups and water quality working groups.

3.9.288 Under the *Catchment and Land Protection Act* 1999 (CaLP Act) and the *Water Act* 1989, Catchment Management Authorities are responsible for co-ordinating activities and providing strategic direction for natural resource management at a regional level. In an operational sense, authorities have direct responsibility for waterway management, floodplain management and rural drainage.

3.9.289 Victoria's catchment and land protection regions are outlined in Figure 3.9H.

FIGURE 3.9H
CATCHMENT MANAGEMENT AUTHORITY REGIONS

Source: Department of Sustainability and Environment.

3.9.290 The Department of Sustainability and Environment has a number of responsibilities in relation to catchment management, which include:

- oversight of authority management;
- undertaking work on environmental programs and projects; and
- a fund provider for environmental projects.

Audit objective and scope

3.9.291 The objective of the audit was to review the management of Victoria's water catchments.

3.9.292 The scope included a review of:

- Victoria's catchment management framework;
- natural resource condition monitoring;
- the Department's grant acquittal process;
- corporate governance in catchment management authorities; and
- project and grant management in catchment management authorities

Basis for the audit

3.9.293 Following a request in 2002 from the former Minister for Conservation and Environment, the Auditor-General reviewed issues concerning over the financial position of the East Gippsland Catchment Management Authority. A report on this review was provided to the Minister.

3.9.294 The main findings of our review were that:

- at 30 June 2002, the authority had a deficiency in net liquid assets required to meet its existing commitments for projects and ongoing fixed costs;
- major factors contributing to the deficiency were:
  - under recovery of the authority's plant and labour on-costs; and
  - expenditure of $520 000 on the Flood Response Program from grant received for other purposes;
- the authority would be insolvent if it was required to repay grants received for work not completed, or complete all work for which it had received funding; and
- the financial position of the authority was not brought to the attention of the Board due to inadequate financial reporting.

3.9.295 Based on the results of the review, we decided to undertake a detailed review of the governance processes and the procedures and controls over the management of grant moneys. We also decided to review the overall management of Victoria's water catchments.

Natural resource management

3.9.296 Past natural resource management practices have been a major factor in the decline of Victoria's natural capital base and have adversely affected the state's ecosystems.

3.9.297 The Government recognises that the continuation of past practices would lead to further degradation of the state's ecosystems and a decline in biodiversity. This, in turn, would continue to undermine Victoria's natural capital base, reducing future opportunities for rural and urban communities.

3.9.298 To redress this situation, the Government determined that natural resources should be managed in a sustainable manner. The Government's broad objective is:

> "To ensure the ecologically sustainable development of our natural resource-based industries, the protection of land and water resources and the conservation of natural and cultural heritage."

3.9.299 The Government objective is endeavoring to ensure that Victoria's natural resources such as water and land are available for commercial use, while stopping, or where possible reversing, the decline in the state's natural capital base.

3.9.300 One of the major vehicles used by the Government to assist it in the achievement of its objective of sustainable resource management, is its integrated catchment management framework.

Victoria's catchment management framework

3.9.301 By establishing its integrated catchment management framework, the Government is recognising the inter-relationship between land, water and biodiversity and the need to apply a holistic (whole of catchment approach) to the management of natural resources.

3.9.302 The Victorian framework for catchment management has been developed to achieve:

- community involvement in, and commitment to, natural resource management;
- ecologically sustainable development of natural resource-based industries;
- maintenance and improvement in the quality of water and condition of rivers;
- conservation and protection of the diversity and extent of natural ecosystems;
- minimisation of damage to public and private assets from flooding and erosion;
- prevention and reversal of land degradation; and
- minimisation of the economic and environmental impacts of pest plants and animals.

3.9.303 In order to achieve the above outcomes, the Department aims to:

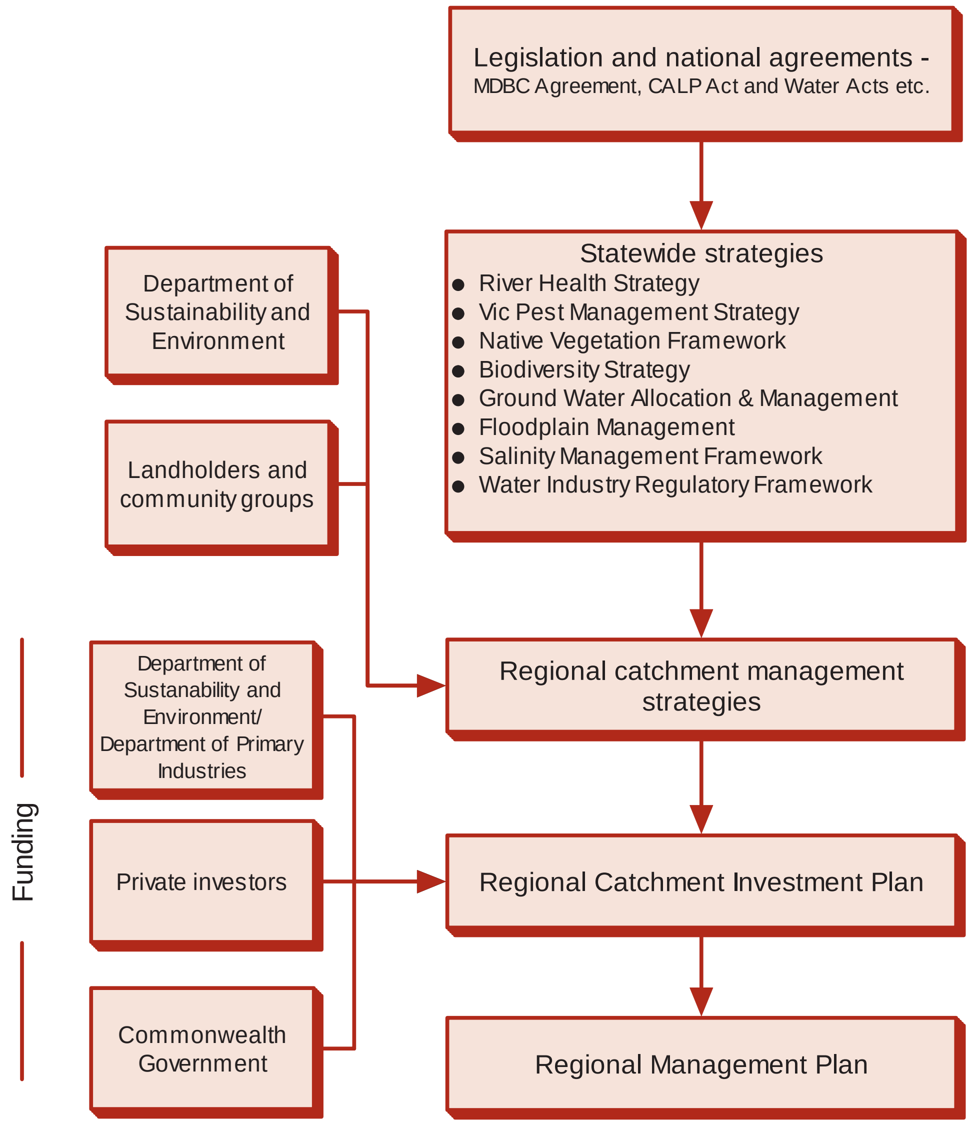
- target natural resource investments to ensure the limited resources available for these investments are directed towards addressing priority issues and delivering maximum benefits;

- ensure that managers of the state's natural resource are clearly accountable to Government and the community; and
- ensure catchment management activities are undertaken efficiently.

3.9.304 The framework and processes for catchment management planning and investment in Victoria are outlined in Figure 3.9I.

3.9.305 Natural resource management priorities are determined through State Government strategies, which deal with specific issues such as river health, pest management, native vegetation management and biodiversity and, where relevant, other Government policy documents such as *Growing Victoria Together*. Victoria is also in the process of developing an overarching statewide investment framework to determine priorities and guide decision-making in relation to natural resource management in Victoria.

FIGURE 3.9I
CATCHMENT MANAGEMENT PLANNING AND INVESTMENT FRAMEWORK



Regional catchment management strategies

3.9.306 The programs and associated action plans of each authority are directed by regional catchment strategies, which have been developed in conjunction with the State and Commonwealth Governments and the community. These strategies:

- outline the authority's agreed vision for the region and the outcomes expected to be achieved;
- provide information on the region's natural assets and their current condition;
- identify existing and potential problems threatening these assets;
- determine strategic management priorities for the catchments in each region;
- outline actions to protect or enhance assets;
- establish mechanisms to monitor performance; and
- are reviewed every 5 years.

3.9.307 The plans were first established in the late 1990s, with the first review scheduled for completion in June 2003. This approach acknowledges that factors impacting on the management of natural resources are subject to change. These include:

- the amount and condition of natural resources managed;
- knowledge of the resource system and the impact of farming, industry and urbanisation; and
- impact of technological change on farming/business practices, waste generation and re-cycling.

3.9.308 Significant funding is provided to authorities from Commonwealth-funded programs such as the Natural Heritage Trust (NHT) and the joint Commonwealth/State National Action Plan for Salinity and Water Quality (NAP). A recently introduced pre-requisite for both NAP and NHT project funding is national accreditation (Commonwealth and State Ministerial) of the authority's regional strategy.

Regional catchment investment and management plans

3.9.309 Authorities prepare annual investment proposals (called regional catchment investment plans), based on their strategic priorities. These plans identify the projects proposed, justification for the projects selected, outcomes expected and the estimated cost of each project. Investment plans are used to attract funding from the Department of Sustainability and Environment (DSE), the Department of Primary Industries and the Commonwealth Government.

3.9.310 From 2003-04, the regional catchment investment plans were changed from annual to 3-year rolling plans.

3.9.311 After project funding is determined, an annual management plan is developed for each region. The plans contain details of the proposed projects, the funding to be provided, and the desired deliverables and outputs. These plans enable authority programs to be linked to the departmental outputs, specified in the State's annual budgetary process and funded by parliamentary appropriation.

3.9.312 Management plans form the basis of quarterly reporting to fund providers on the progress of projects. The system provides for progress payments to authorities, following satisfactory completion of specified stages of the project.

Statewide strategic plan

3.9.313 DSE, in conjunction with the Environment Protection Authority (EPA), has focused significant effort over the last 5 years to develop a range of strategies that set priorities and strategic direction for natural resource management at a state and regional level.

3.9.314 From a state perspective, there are a number of strategies dealing with specific issues affecting the state's catchments, such as salinity, river health and pest management. However, there is no overarching mechanism for setting priorities and allocating resources between individual management programs. In effect, there is no statewide integrated catchment management strategy.

3.9.315 This observation was also made by the Victorian Catchment Management Council in its 2002 report *The Health of Our Catchments – A Victorian Report Card*. The report made the following comment.

> "Through Growing Victoria Together, the Victorian Government has made a commitment to build on the strong foundation of the CMA system. Since 1996, CMA regions have developed priorities to implement transparent, efficient and effective natural resource management programs. Victoria needs a vision for its rural landscape underpinned by a strategy, investment plan and whole-of-government implementation plan".

Recommendation

3.9.316 **We recommend that DSE develop an integrated catchment management strategy across the state. Such a strategy should:**

- **link together the individual issue-based strategies;**
- **provide the State Government's future vision for the Victorian landscape and for the role of agriculture within that landscape;**
- **identify potential opportunities for further sustainable development of the state's natural resources;**
- **allocate responsibilities for the management of natural resources across the state;**

- **include a knowledge management plan, to include research and development and monitoring, evaluation and performance review; and**
- **identify resources needed to address natural resource issues.**

Longer-term focus on sustainability

3.9.317 The catchment management framework, which allocates responsibility for the management of catchments to specific statutory authorities, was seen as leading edge in relation to the institutional reform of catchment management.

3.9.318 However, the natural resource management systems used by authorities and DSE to manage catchments, have evolved in a fairly ad hoc manner. The management of natural resources within catchments has also had a short-term focus. While this short-term focus was appropriate to redress some of the more urgent issues facing Victoria's natural resources, there is a need for a longer-term focus, with a view to designing catchments and landscapes for sustainability.

3.9.319 The planning time frame for such activities will need to be long-term, probably 20 to 50 years. This time frame will allow for current environmental works to impact on the State's natural resource base and for the community to adapt to, and adopt, the concept of sustainable development.

Funding

3.9.320 Figure 3.9J outlines the revenue received by Authorities for 2002-03.

FIGURE 3.9J
REVENUE RECEIVED BY CMAs, 2002-03
($)

Catchment Management Authority	*Natural Heritage Trust grant funding*	*National Action Plan grant funding*	*Other State grant funding*	*State recurrent funding (a)*	*Total funding*
Corangamite	487 147	3 118 656	170 000	4 209 500	**7 985 303**
East Gippsland	625 396	-	660 400	2 740 000	**4 025 796**
Goulburn Broken	3 806 944	7 847 468	1 537 000	4 591 600	**17 783 012**
Glenelg Hopkins	391 750	5 881 305	856 500	2 395 300	**9 524 855**
Mallee	658 447	3 968 000	1 006 150	1 602 950	**7 235 547**
North Central	1 000 760	6 616 350	1 275 000	3 566 700	**12 458 810**
North East	1 062 032	-	1 350 440	3 107 160	**5 519 632**
West Gippsland	591 000	-	962 012	5 036 988	**6 590 000**
Wimmera	326 126	4 159 371	672 000	1 758 200	**6 915 697**
Total funding	**8 949 602**	**31 591 150**	**8 489 502**	**29 008 398**	**78 038 652**

(a) Includes State Levy Replacement funding.
Source: Department of Sustainability and Environment.

3.9.321 Authorities receive funding of between $4 million and $18 million, of which about two-thirds is from Commonwealth or State-specific purpose grant funding.

3.9.322 Since their inception in 1997, authorities have progressively extended their roles as regional stewards of natural resources on behalf of government. Their workload has increased, and will continue to do so, with the progressive implementation of government policy and compliance with statutory requirements (under the *Water Act* 1989 and the *Catchment and Land Protection Act* 1994). For example, authorities have oversight, co-ordination and delivery roles for projects and programs associated with the implementation of newly developed regional catchment strategies for 2002-07.

3.9.323 As authorities assume responsibility for additional projects and manage larger amounts of project funding, they are subject to increased requirements to account for these projects. There is also an increasing need for authorities to:

- develop and upgrade systems to assess and record the condition of the natural resources which they oversee;
- enhance the quality of their external reporting by including additional information on the condition of catchments, and the impact resource development and their own activities have on the environment and local communities; and
- improve their project management and governance arrangements.

3.9.324 Work associated with improved community engagement and devolved decision-making, through the Authority Implementation Committees, has escalated and will continue to do so. Community expectations in relation to the delivery of actions proposed in regional catchment strategies have also risen following a 12-month process of authority engagement with local communities.

3.9.325 The above factors increase the workload and operating costs of authorities. There has not been an equivalent increase in non-project funding to meet these costs.

Recommendation

3.9.326 **We recommend that current funding levels for authorities be re-assessed in light of increased responsibilities and associated costs. This re-assessment should address financial difficulties faced by some authorities.**

3.9.327 The timing of development and implementation funding of regional strategies is different across Victoria. For example, 6 authorities received foundation funding under NAP in 2001-02 for the development of their regional catchment strategies, while the remaining 3 and the former Port Phillip Catchment Protection Board, did not receive funding until mid-2003. This situation resulted in delays in these authorities finalising their catchment management strategies.

3.9.328 Authorities are funded for projects designed to deliver outputs and outcomes outlined in their regional catchment strategies and plans. Often the achievement of these strategies requires authorities to undertake works over the longer-term.

3.9.329 With authorities dependent on short-term grants for environmental works, and with the level of grant funding available not determined until mid-year, it is extremely difficult for authorities to plan and deliver optimal long-term solutions for the environmental problems identified.

3.9.330 The uncertainty in funding also creates significant job uncertainty and work force management problems as changes in funding from year-to-year may require staff reductions.

Recommendation

3.9.331 DSE should consider funding authority programs for periods longer than 12 months and preferably for 3-year periods. We understand that the Investment Planning Project may assist in resolving this issue.

Condition of Victoria's natural resources

3.9.332 A primary objective of the Government is to ensure natural resources are managed in a sustainable manner.

3.9.333 Under the *Catchment and Land Protection Act* 1994, one of the key statutory roles of the Victorian Catchment Management Council is to provide a 5-yearly report to Parliament on the condition and management of land and water resources in Victoria.

3.9.334 The first report, *Know Your Catchments*, was produced in 1997 by the previous Catchment and Land Protection Council with the support of the former Department of Natural Resources and Environment and the EPA.

3.9.335 The report highlighted that while the condition of the state's natural resources was monitored, the information was incomplete and processes used to gather, store and interpret this information was unco-ordinated. This made it difficult for authorities to collect and present data in a clear, consistent statewide format. The Council also identified an inconsistency in ongoing priorities and little commitment to monitoring the condition of natural resources against agreed indicators.

3.9.336 The absence of a consistent set of indicators to measure catchment condition was addressed by a Natural Heritage Trust (NHT) funded project involving the Council, authorities, the former Department of Natural Resources and Environment and the EPA. The Resource Assessment and Monitoring (RAM) Group worked over 4 years to develop an agreed set of indicators to enable consistent reporting on catchment condition across the state.

3.9.337 The Council's second report, *The Health of Our Catchments – A Victorian Report Card*, produced in 2002, assessed the condition and management of land and water resources using 32 catchment condition indicators, developed by the RAM group. These indicators were grouped under themes, which included biodiversity, rivers, wetlands and estuaries, managing water, managing land, and pest plants and animals.

3.9.338 The report concluded that:

"Under current resourcing and management paradigms our efforts to protect and sustainably manage natural capital are not keeping pace with the breadth of degradation symptoms depreciating the natural capital base. One of the key hindrances to community and government efforts in this area is knowledge.

"New knowledge is helping and we have made great strides in the last five years. This knowledge coupled with experience and efforts over the past two decades tell us much about what we need to do. It is clear that current 'best management practices' will not be enough to ensure sustainable use of the land and water in many parts of the State. Major change will need to be made in the management of many areas to offset the impact of issues such as dryland salinity and soil acidity".

3.9.339 The Council also indicated that it is not currently possible to accurately assess the condition of the state's resource base. Other problems identified included:

- indicators to assess biodiversity, soils, greenhouse, and water management were inadequate;
- there were issues associated with the completeness, quality and accessibility of the information generated;
- systems designed to collect natural resource information were not well-developed;
- trends and performance were often difficult to assess, as in many instances information has not been gathered for long enough or in an appropriate form to identify trends;
- despite progress being made, gaps in our predictive understanding of environmental systems still exist; and
- increased resources are needed for interdisciplinary research and monitoring efforts.

3.9.340 At a national level, an Australian National Audit Office performance audit report conducted in 2001 on the Natural Heritage Trust program noted that similar problems with the assessment of natural resource condition were experienced across the country.

3.9.341 **As a State, there is additional work to complete before we are in a position to:**

- **determine the condition of Victoria's natural resource base;**
- **understand the impact on the state's natural resource base of current resource development activities; and**
- **assess the effectiveness of works undertaken in catchments to improve the State's natural resource base.**

Review of Authority management practices

Internal audit review

3.9.342 In October 2002, following the financial management problems experienced in the East Gippsland Catchment Management Authority, DSE instructed its internal auditors to review the financial management and business practices of the State's 9 catchment management authorities.

3.9.343 The internal audit report identified a number of good business practices in authorities, including:

- most authority Boards have appropriate governance practices in place;
- reporting to the Board for most authorities was adequate;
- many authorities have effective audit committees and finance committees;
- generally, authorities have adequate financial management practices and skills to manage the finance of the organisation; and
- human resources and occupational health and safety issues appear to be well-controlled.

3.9.344 The internal audits identified a number of areas requiring improvement, including:

- project management and reporting to the Board;
- use of key performance indicators to measure the performance of the authority;
- corporate governance and financial management training for Board members;
- accounting, project management and management information systems;
- establishing an effective internal audit program focusing on key risks of the business;
- the re-alignment of the East Gippsland and West Gippsland authorities' boundaries with DSE's regional boundaries;
- strategic planning, budgeting and reporting processes;
- allocation of corporate costs to projects; and
- authority policies and procedures.

Acquittal processes

3.9.345 A significant amount of each authority's operations are financed through grants received from the Commonwealth and State Governments.

3.9.346 DSE has overall responsibility for much of the grant funding received by authorities. It is, therefore, important that it is satisfied that these funds are only used for the purposes intended, and that grant objectives and expected outcomes are achieved. To achieve this, DSE needs to establish mechanisms to monitor, evaluate, report and review the use of project grants.

3.9.347 Specifically, DSE must ensure that:

- expected project financial and performance outcomes are identified;
- adequate systems are established to monitor and assess the condition of natural resources, to enable project outcomes to be evaluated;
- systems and procedures enable the financial performance of projects to be adequately monitored
- grant payments made by DSE are linked to the achievement of milestones;
- processes are established to evaluate project outputs/outcomes against project objectives; and
- the acquittal process is adequately documented.

3.9.348 At the time of our audit, procedures in place to ensure grant funding to authorities is properly acquitted included:

- outlining grant requirements in regional management plans;
- delivery of training/seminars on departmental output requirements for grant-funded projects;
- grant audits of non-NAP projects, by regional services; and
- departmental review of authority annual reports.

3.9.349 DSE's internal audit has recently been requested to assist the NAP Project Office to develop audit programs for NAP-funded projects.

3.9.350 **Although these processes go some way in ensuring appropriate accountability for grant funding, we identified a number of concerns with DSE's acquittal process. Specific concerns were:**

- **inadequate controls to ensure that grants provided for a specific purpose were used for that purpose and to prevent the cross-subsidisation of projects by authorities or the use of project funds to meet general operating costs;**
- **inadequate identification and documentation of expected grant outcomes and project milestones;**
- **no standard approach to the allocation of corporate/overhead costs to projects, which can lead to a distortion between competing bids for project funding;**
- **in some cases, NHT Phase I progress payments were made prior to the achievement of project milestones; and**
- **only limited audits were performed to assess the financial performance of projects and the delivery of outputs against project criteria.**

Recommendation

3.9.351 **The grant acquittal process would be improved through:**

- **better defined grant outputs and milestones;**
- **developing a standard approach to allocating corporate/overhead costs to projects;**
- **making progress payments only after previous funding has been expended and project milestones achieved;**
- **independent auditing of project outcomes at the completion of the grant; and**
- **independent auditing of project outcomes against objectives.**

3.9.352 Since our audit, DSE has introduced initiatives to address some of these issues.

3.9.353 DSE has been working with authorities to develop a consistent cost allocation framework for application across authorities. When fully implemented in 2004, the framework will better identify cost allocation to program and general operations, and enable authorities and DSE to assign funding to these functions more clearly.

3.9.354 DSE has advised that it is also implementing a standard project management and reporting system to enhance performance monitoring. Consideration is being given to the introduction of audits for all grants and the use a risk assessment process to target higher risk grant programs for audit.

3.9.355 In mid-2001, the Catchment and Water Division of the former Department of Natural Resources and Environment introduced a Catchment Activity Management System (CAMS) aimed at capturing, recording and managing information on catchment-based activities, including Natural Heritage Trust-funded projects. Projects can be mapped in CAMS and monitored over time to enable comparison project success.

Corporate governance

3.9.356 Corporate governance is concerned with:

- an organisation's decision-making structures and processes;
- the internal controls established by management; and
- the behaviour of staff to support effective accountability for performance outcomes.

Board and committee oversight

3.9.357 An important component of good corporate governance is the establishment of an effective Board and a specialist committee structure to provide strategic leadership to the organisation, establish accountability mechanisms and oversee operations. In an authority with an effective corporate governance framework, we would expect to see:

- a board of management, with the knowledge, experience and skills in key areas such as finance, executive remuneration, catchment management, technical matters, environmental management and community consultation;
- the Board includes independent members;
- an audit committee, which provides assurance to the board over the authority's financial reporting and internal control mechanisms, and oversees the internal and external audit functions;
- other governance committees, including finance, risk management, executive remuneration, and occupational health and safety;
- the board establishing a clear strategic direction through annual strategic plans, corporate plans and budgets;
- boundaries of activity, authority and accountability which are clearly established and communicated within the organisation to ensure the authority's operations are conducted in accordance with Board requirements;
- accountabilities within the authority are clearly defined;
- mechanisms in place to regularly review the performance of the Board;
- strategies and actions in place to minimise risks;
- the Board has established policies in relation to all key facets of the authority's operations;
- pecuniary interest statements for managers and Board members prepared to ensure management and board interests in businesses dealing with the authority are declared;
- the establishment of a Board charter to clarify the roles and ethical standards required of Board members;
- financial and other delegations, have been established.

3.9.358 We found that formal boards of management govern all authorities. DSE, as required by the CaLP Act, nominates 2 of the board members with the remaining members selected from the local community following approval by the Minister for Sustainability and Water.

3.9.359 All authority boards have sub-committees, which usually include an implementation committee, audit committee, finance committee, remuneration committee, and an occupational health and safety committee.

3.9.360 There is currently no requirement under the CALP Act or the Water Act that requires board members to have financial management skills. **Our review indicated that some boards lacked the level of knowledge and experience in financial management needed to adequately manage their businesses**.

3.9.361 In some authorities, the information provided to the Board was insufficient to meet their needs, often incomplete and, on occasion, inaccurate. In these circumstances, it would be reasonable to expect that an appropriately knowledgeable and competent Board would have queried the information presented to it.

3.9.362 In at least one case, an authority Board was not in receipt of, and had apparently not requested, information on:

- variances between authority budgeted and actual results, and explanations for these variances;
- the status of all current projects;
- outstanding debtors and debt management; and
- the reconciliation of the financial position of the authority to unexpended grants received.

3.9.363 This indicates that some Boards lacked the appropriate skills and knowledge to effectively perform their function and question information presented for decision-making.

3.9.364 The Board appointment process has recently been changed. For the period 2003-06, DSE requires prospective appointees to possess at least one of the following core competencies:

- business acumen;
- organisational governance;
- industry knowledge;
- general management;
- natural resource management;
- strategic development and change management;
- accounting and finance; and
- community engagement and social capital building.

3.9.365 DSE advised that Board members have recently undertaken governance induction training and have been provided with general governance guidelines prepared by DSE. From next year, the overall performance of each authority Board, and the performance of individual Board members, will be subject to an annual assessment.

Management structures

3.9.366 Sound corporate governance requires the establishment of appropriate internal management structures. These structures would include accountability mechanisms to provide assurance to the chief executive officer and the Board that:

- the authority's internal control systems and management processes are working effectively; and
- there are adequate financial and resource management structures to ensure the authority's resources are managed effectively, efficiently and ethically.

3.9.367 In a well-run authority, we would expect to see:

- a sound business planning process, involving preparation of:
  - strategic plans;
  - business plans;
  - regional catchment strategies; and
  - regional management plans;
- appropriate mechanisms to review organisational achievements against planned results;
- a sound risk management process;
- establishment of appropriate performance measurement indicators;
- monthly reporting on operations, including:
  - actual and projected financial position, financial performance and cash flows;
  - comparison of budgets with actual revenue and expenses, with explanations for variances; and
  - project statements for major projects;
- reconciliation of monthly reports to financial records;
- internal audit function;
- systems and processes to minimise scope for unethical practices, and protect public assets;
- controls to minimise the potential for waste, fraud and corruption;
- a comprehensive policy and procedure manual;
- effective stakeholder consultation to improve authority awareness and responsiveness to stakeholder needs;
- financial recording systems to monitor the authority's financial performance and facilitate management decisions; and
- procedures to address occupational health and safety requirements.

Monthly reporting

3.9.368 **While all authorities generated annual balance sheets, operating and cash flow statements, most were not preparing monthly statements.**

3.9.369 Access to timely information on operating revenues, expenses, cash flows and financial position, is essential for effective decision-making in all organisations. As a significant proportion of an authority's funding is provided by one-off grants and, therefore, not guaranteed from year-to-year, timely information on the operations of the authority, in particular cash flows, becomes critical.

Operating results and cash flow projection

3.9.370 Historically, authority reporting has involved the generation of information on past events. While this information is useful, the likely future position and operating results of the business is of far greater value. Management is likely to be interested in the future financial and cash position of the authority at year-end, and the authority's likely operating result for the current financial year.

3.9.371 Projections of an authority's future operational result, at set intervals during the year, provides management with a mechanism to identify and correct poor performance and allows the Board to adjust to external events impacting on the business

3.9.372 Projections are even more useful when accompanied by an appropriate sensitivity analysis. This involves authorities predicting the likely outcome on the operations of their businesses under different sets of assumptions.

3.9.373 **Our investigations found that projections of future operating results and financial and cash flow positions under different circumstances were not undertaken by most authorities.**

Reconciliations of internal reports to financial records

3.9.374 To make informed decisions, management needs accurate and reliable information. **In some authorities, monthly reports on the operations were generated independently of the general ledger and other financial records, and not reconciled with these financial records.**

3.9.375 The absence of a link between internal reports and an authority's financial records could result in management receiving incomplete or inaccurate information.

Risk management

3.9.376 Risk management, which covers strategic, operational and financial risks, is designed to minimise the impact of detrimental events on an organisation's business. Development of a risk management framework would normally involve:

- establishing an organisation-wide process to identify events likely to have a detrimental impact on the business;
- assessing the probability of each identified event occurring, and determining the consequences resulting from its occurrence;

- developing strategies and actions to reduce the probability of certain identified events occurring and/or the consequences of these events should they occur; and
- establishing a risk management reporting regime.

3.9.377 A sound knowledge of the risks facing the organisation and a strategy to manage adverse events, enables authorities to better manage their risks. In particular, it enables an authority's Board to systematically trade-off the costs of an event occurring against the cost of reducing the risk. In this way, good risk management is a primary driver of efficiency.

3.9.378 **Our review disclosed that a number of authorities had effective risk management processes in place, while others had not developed and implemented effective strategies.**

Internal audit

3.9.379 Internal audit functions are established and actively used by management to assist in managing the business. In these organisations, audit committees use their internal audit functions to:

- review the effective operation of the organisation's systems and internal controls, and provide assurance to management;
- identify risks facing the organisation and bring them to the attention of management; and
- assess specific operational functions and activities.

3.9.380 We identified that not all authorities had established an internal audit function and, where such functions were established, their activities were often narrowly focused on internal financial compliance work.

3.9.381 **In some authorities, due to the absence of an effective internal audit function, high-risk activities such as grant, project and debt management were not subject to internal review.**

Management of grants in advance

3.9.382 All authorities manage projects using grant moneys (which are generally received in advance). It is important for the authorities to have adequate controls over project funding and unexpended grants. In particular, authorities need information on the commitments associated with the grants and funds available to meet those commitments.

3.9.383 **While most authorities generate some information on commitments for incomplete works, the total value of these commitments is not always reconciled to the resources available to meet these commitments.** In the absence of this reconciliation, situations where authority commitments exceed resources available are unlikely to be brought to the attention of management.

Budgets

3.9.384 We found that all authorities prepared annual budgets. However, **budget reports generated by some authorities did not explain variances between budgeted and actual costs.** In the absence of this analysis:

- management's ability to recognise and resolve problems is impaired; and
- it is difficult for management to determine whether variances from budget represent one-off events or endemic problems.

Regional catchment strategies

3.9.385 Victoria's catchment management model requires authorities to identify problems facing the catchments for which they have responsibility, and to develop strategies to address these problems.

3.9.386 **We identified that not all authorities had finalised their catchment strategies by the June 2003 deadline.**

3.9.387 In the absence of these strategies, it is difficult for authorities to ensure the work needed to be undertaken in catchments is identified, prioritised and delivered in the most cost-effective manner.

3.9.388 As the receipt of project funding is dependent on the existence and quality of these strategies, an incomplete strategy could also adversely impact on an authority's ability to attract project funding.

Performance indicators

3.9.389 Despite the inclusion of key performance indicators in authority planning documents, such as regional management plans and the regional catchment strategies, our review found that limited information regarding the performance of authorities against key performance indicators is provided to authority Boards.

3.9.390 **To manage effectively, authorities need to assess their performance against pre-established performance indicators and use the information gained to implement changes where appropriate.**

Reporting to the Board

3.9.391 To carry out their functions, Boards need access to accurate, complete and reliable information on a timely basis. Our audit identified that, in most cases, there was room for improvement in the standard of information provided to Boards. Specifically, we identified deficiencies in information concerning:

- individual projects, such as financial performance of projects against budgets and timelines, expected completion costs, project risk and achievement of milestones;
- authority revenue, which did not include all grants received;
- bank balances;
- balance and collectability of debtors; and

- under-recovery of on costs.

Recommendations

3.9.392 **We recommend that:**

- **monthly reports on the financial position and the operating and cash flow results of the business be prepared by authorities;**
- **forecast results to year-end for operating statements, balance sheet and cash flow statement be prepared quarterly and presented to boards;**
- **consideration be given to the use of sensitivity analysis in relation to the performance of the business and major project expenditure;**
- **wherever possible, management reports be generated from the authority's financial systems and where not possible, be reconciled to those financial records;**
- **sound risk management processes be established in all authorities;**
- **a review of the current operation of the internal audit function be undertaken;**
- **cash available to meet project expenditure be regularly reconciled to unexpended grants received;**
- **explanations of major variances between budgeted and actual results be prepared;**
- **authorities complete these regional catchment strategies as soon as possible;**
- **monthly reports provided to authority Boards should include information on the status of projects; and**
- **each authority's performance be annually assessed against performance indicators established in its planning documents.**

Project management

Natural Heritage Trust grants

3.9.393 The Commonwealth Government established the Natural Heritage Trust (NHT) program in 1997, to provide funding for activities directed at restoring and conserving Australia's natural environment. The Trust was originally provided with funding of $1.25 billion over a 5-year period. The Trust provides funding for environmental activities at national, state, regional and community levels.

3.9.394 At the national level, a Ministerial Board oversees the management of the Trust. At the state level, funding is administered through partnership agreements between the State and Commonwealth, which set out the terms and conditions under which the financial assistance is provided.

3.9.395 Grants from the Trust are directed at the areas of sustainable agriculture, environment protection, and natural resource management. The *Natural Heritage Trust of Australia Act* 1997 defines a number of specific objectives in relation to each of these areas.

3.9.396 In choosing projects for funding, priority is given to activities that:

- reverse or mitigate the decline, or improve the condition and management of, the environment and natural resources;
- maximise cross linkages between programs, with a capacity to achieve multiple outcomes in relation to national strategies; and
- are derived from strategies to address fundamental causes of environmental and natural resource problems, rather than symptoms.

3.9.397 Regional Trust co-ordinators have been established in each state to assist in the operation of the Trust. These co-ordinators have broad responsibilities, which include:

- developing community capacity and capability for project development;
- regional planning;
- ongoing project support; and
- administration of grant applications.

3.9.398 Each of the Victoria's catchment management authorities has been designated as a regional co-ordinator.

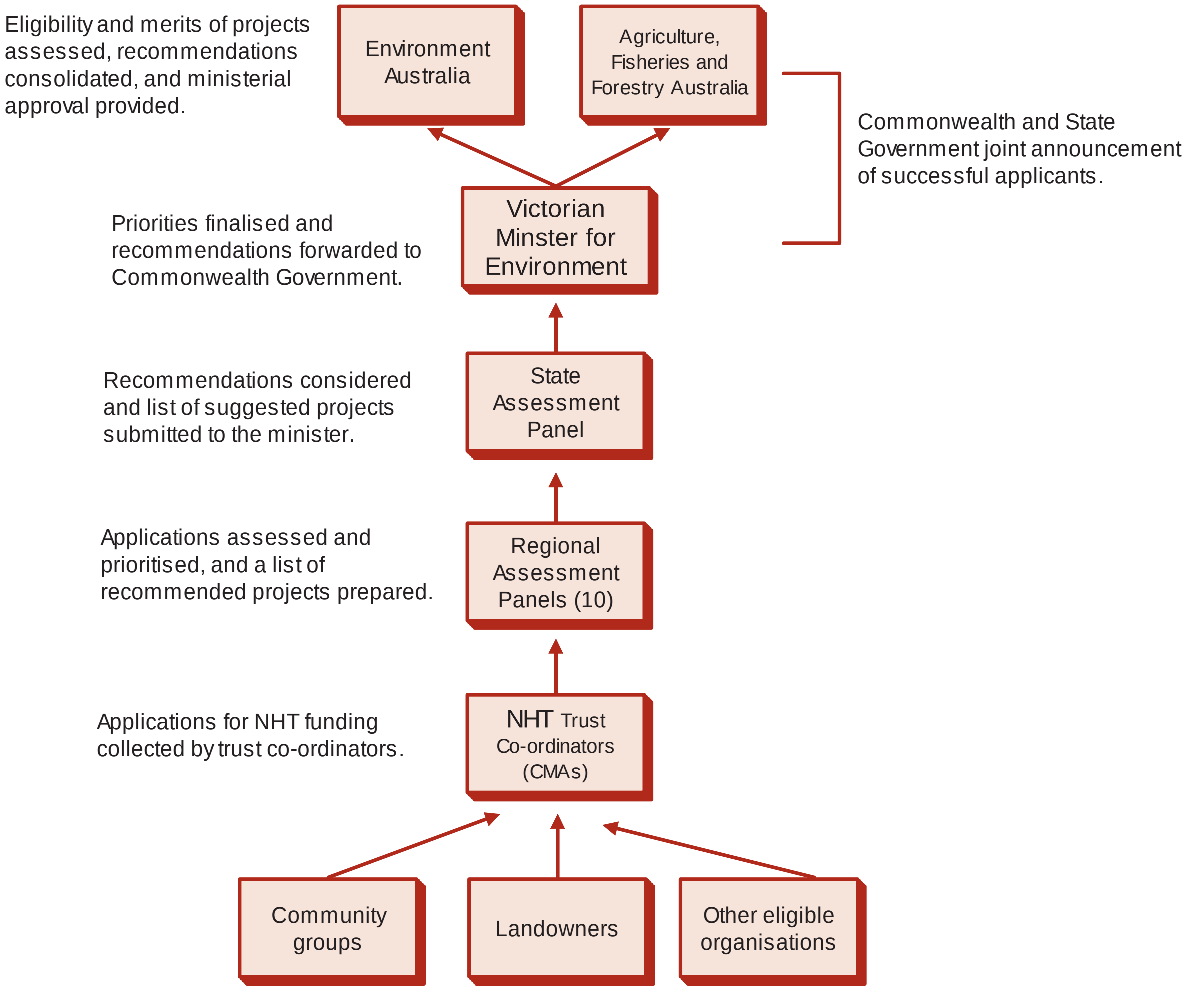
3.9.399 With grants totalling approximately $190 million provided for natural resource projects in Victoria, funding from the Trust represents a significant source of income for catchment management authorities.

3.9.400 DSE has overall responsibility for policy development, recommending grant proposals for funding and management of trust funds received.

3.9.401 Authorities have a varied role in relation to the administration of Trust grants. Depending on the type of works to be undertaken, authorities generally allocate funding to implementation committees (such as Landcare groups) for distribution, or undertake approved works on landowners' properties themselves. In some cases, authorities also make direct payments to private landowners to undertake approved works.

3.9.402 Figure 3.9K outlines the assessment process in place for the provision of funding during the first phase of the NHT program (1997 to 2001). Many of the projects funded by phase 1 NHT grants were still in progress in 2002.

FIGURE 3.9K
NATURAL HERITAGE TRUST – FUNDING ASSESSMENT PROCESS



3.9.403 Project monitoring and evaluation is identified as a State responsibility under the partnership agreement with the Commonwealth. The relevant authorities, together with catchment implementation committees and the regional assessment panels, primarily manage the oversight and monitoring of Trust-funded projects in Victoria.

Changes to the Natural Heritage Trust

3.9.404 In 2001, the Commonwealth Government announced that the program would be extended (with some alterations) for a further 5 years from 1 July 2002, with additional funding of $1 billion provided for the second phase.

3.9.405 To make the Trust more effective, the second phase of the program consolidated funding into 4 areas: Landcare, Bushcare, Rivercare and Coastcare. Three overarching objectives were also introduced to guide funding decisions: These objectives covered:

- biodiversity conservation;
- sustainable use of resources; and
- community capacity building and institutional change.

3.9.406 A framework for the implementation of the Trust extension was endorsed by State and Federal Ministers at the Natural Resource Management Ministerial Council in October 2002. Under the new framework, delivery of the NHT at the regional level has been integrated with the National Action Plan for Salinity and Water Quality (NAP), which was introduced in 2000.

3.9.407 The majority of funding under the second phase of the Trust was directed to regions for the implementation of their natural resource management plans. Funding has also been available to authorities to enable them to continue with priority projects until their 2003 plans are accredited and implemented.

National Action Plan grants

3.9.408 In recognition of the significance of problems associated with salinity and water quality, agreements were signed between the Commonwealth Government and the States and Territories to implement the National Action Plan (NAP).

3.9.409 The Commonwealth Government has provided $1.4 billion over 7 years for grants to:

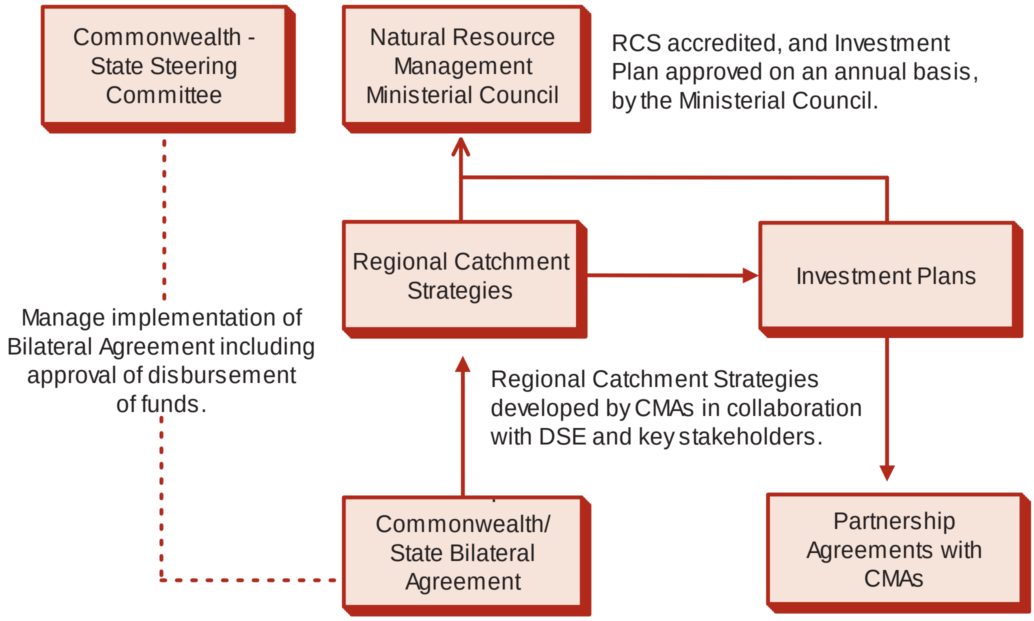
- prevent, stabilise and start to reverse trends in dryland salinity affecting the sustainability of production, the conservation of biological diversity and the viability of our infrastructure; and
- improve water quality and secure reliable allocations for human uses, industry and the environment.

3.9.410 The Commonwealth Government's intention is for the NAP to build on the achievements of the NHT and other initiatives by individual State and Territory governments and the Murray Darling Basin Ministerial Council.

3.9.411 In Victoria, the NAP has identifies 4 priority areas falling within the responsibility of 6 authorities. These authorities are Glenelg-Hopkins, Corangamite, Goulburn-Broken, North Central, Mallee and Wimmera.

3.9.412 Chart 3.9L below outlines the process for the provision of funding under the NAP. This same process will be followed for phase 2 NHT funding.

**FIGURE 3.9L
NATIONAL ACTION PLAN – PROCESS FOR PROVISION OF FUNDING**



3.9.413 In accordance with this new approach, the provision of funding for both the NAP and NHT programs will now be based on:

- a single accredited natural resource plan (formulated from revised regional catchment management strategies) per region, incorporating the major natural resource management issues in the area;
- an investment strategy that flows on from the resource management plan and details the specific actions, costs and time frames required to implement the regional plan; and
- partnership agreements (signed by the Commonwealth and State Governments and Authorities) that outline funding amounts for actions identified in the investment strategies, responsibilities for undertaking the activities, agreed outcomes, performance measures, and monitoring and evaluation processes.

3.9.414 We reviewed the administration of a sample of NHT grants by authorities in Victoria.

3.9.415 If authorities were managing their projects efficiently and effectively, we expected to see:

- written procedures for tendering and awarding contracts;
- development of plans for major projects;
- establishment of budgets for each project;
- project risk assessments;
- systems to accurately record costs incurred against individual projects, with overhead costs associated with each project appropriately recognised;

- systems and procedures to identify and account for grants in advance, which should be tied to future expenditure;
- systems and procedures are established to enable the financial performance of projects to be adequately monitored, which would include:
  - the identification and recording of project costs;
  - establishment of milestones;
  - monitoring of costs and progress of projects against milestones; and
  - periodic analysis of revenue earned;
- processes are established to evaluate project outputs/outcomes against project objectives; and
- an established post-project evaluation process.

3.9.416 Our review found that the standard of management of grant-funded projects by authorities was variable. In many authorities, the project management processes have generally been informal and ad hoc, rather than structured and systematic. In some authorities, poor project management resulted in the cost of works performed on some projects exceeding the value of grant funding received. In at least one authority, poor project management was a major contributing factor to the authority experiencing serious financial difficulties.

Project responsibility and staff capability

3.9.417 Effective project management is assisted where responsibilities for individual projects are clearly defined and assigned. Sound project management is also dependent on staff possessing appropriate project management skills, knowledge of the activity being undertaken, and sufficient administrative support to enable the collection, recording and reporting of project information.

3.9.418 At a number of authorities, responsibility for projects was not always clearly defined and some staff lacked project management skills. We do acknowledge that in some rural areas it is difficult for authorities to recruit and retain appropriately skilled and experienced staff.

3.9.419 **In our opinion, the absence of clearly defined responsibilities for projects, and a lack of adequately trained and skilled staff in some areas, has affected the ability of some authorities to effectively manage projects under their control.**

Information systems

3.9.420 To assist the effective management of projects, appropriate management information systems, including costing systems, need to be established and maintained. These systems should provide useful and timely information to management, so that potentially ineffective, inefficient or fraudulent use of grant funding can be addressed.

3.9.421 Our audit indicated that costing systems in a number of authorities were inadequate. Of particular concern was the inadequate accounting for overhead costs.

3.9.422 In some authorities, project costs such as administration, rental and other corporate costs were not allocated to specific projects. **In these circumstances, grant moneys received by authorities were only applied to variable costs and not the full costs associated with each project.**

3.9.423 **We also noted that, where individual project costs exceeded funding, some authorities were using grant moneys, received in advance for other projects, to meet these costs.** As the reporting systems in these authorities did not separately identify revenues and expenses associated with these overhead costs, this problem was not brought to the attention of management.

Allocation of grant funding

3.9.424 Guidelines for NHT funding have been provided by the Commonwealth to be used in the grant selection process. Adherence to these guidelines will ensure that grant funding is only used for the purposes outlined in the funding agreement.

3.9.425 We found that, in most cases, it is unusual for the total value of grant applications for NHT funding within a catchment region, to exceed the amount of funding available. As a result, applications for grants were generally approved if they satisfied Trust guidelines. Where applications for funding exceeded funding available, project proposals were evaluated on a priority basis.

3.9.426 A review of a selection of grant recipients did not find any instances of grants being approved for projects that did not meet the criteria for Trust funding. We were, however, unable to assess whether the action taken by some authorities, in rejecting grant applications, was appropriate as authorities did not retain unsuccessful applications.

Equitable allocation of grant funding

3.9.427 Allegations that some Board members were using their positions to enable them or their families to inappropriately access grant funding were made to our Office. Our review did not find any instances of this occurring.

Appropriate use of grant expenditure

3.9.428 Project funding is provided to authorities on the condition that it is used for the purpose for which it was approved. Therefore, it is important for authorities to establish appropriate controls to:

- prevent funding provided for a specific project or program from being used for another purpose; and
- detect instances where funding has been used for purposes other than those approved.

3.9.429 Our review of grant expenditure identified that at some authorities the value of grants approved for specific projects and programs was not reconciled to the amounts expended on these projects and programs.

Project monitoring

3.9.430 Project monitoring arrangements should be clearly defined, effective and appropriately resourced. The extent and frequency of project monitoring required should be based on a risk identification, analysis and assessment process. Risk factors include the size of the project, the capability of the contractors engaged to undertake the work on behalf of the authority and the sensitivity of the project.

3.9.431 There are 2 fundamental aspects of monitoring grant programs: performance monitoring, and financial monitoring. Performance monitoring determines the extent to which desired outcomes have been achieved; while financial monitoring assesses compliance with relevant accountability procedures.

3.9.432 **Our review identified that project monitoring was variable across authorities, ranging from detailed monitoring of projects in some authorities to limited monitoring in others.**

Project evaluation

3.9.433 Project evaluation is an essential requirement of effective project management. Appropriate evaluation processes improve accountability for project funding, enhance decision-making processes and ensure better use of resources.

3.9.434 In any project, evaluation process the measurement of performance is difficult. This is even more difficult when dealing with environmental projects as while the lives of these projects are short, their resulting impact can only be reliably measured over the longer-term.

3.9.435 Despite this limitation, it is important that the short-term project outputs and achievements are measured and used to evaluate the effectiveness of the project.

3.9.436 In the longer-term, the condition reporting of catchments will provide an indication of whether the State's combined efforts over a period of time are generating improved environmental outcomes for Victoria's natural resource base.

3.9.437 In evaluating the effectiveness of projects it is also important to recognise that benefits achieved in one area can lead to adverse impacts in another.

3.9.438 **Our review indicated that significant scope exists to improve post-evaluation programs at authorities**. In particular, the review found that the quality of the post-evaluation programs in place is extremely variable, ranging from an evaluation of a selection of projects each year at some authorities, to the absence of any formal post-evaluation programs at others.

3.9.439 **We also considered that authority assessment of project economy and efficiency could be improved**. Although economy is not an end in itself and should not be pursued without regard to the level and quality of output, ways in which the cost of resources used in projects can be minimised should nevertheless be constantly considered. A sound evaluation process would incorporate an assessment of the project manager's efforts to minimise project costs.

3.9.440 If projects are managed efficiently, authorities will be identifying opportunities for reducing both direct project expenditure and administrative costs. Again, a sound evaluation process would incorporate an assessment of project efficiency.

Project reporting

3.9.441 In order for projects to be effectively managed, appropriate, accurate and timely information on the status of projects must be made available to authority management for decision-making purposes.

3.9.442 Our review found that project information generated by authorities was quite variable. Important information, regarding the financial performance of projects against budgets and timelines, expected completion costs, project risks and achievement of milestones, was not regularly reported by a number of authorities.

Recommendations

3.9.443 **In regard to project management, we consider that the performance of authorities could be improved by:**

- **clearly assigning responsibility for projects to appropriate staff;**
- **ensuring that their staff are adequately trained in project management;**
- **establishing appropriate project costing systems and procedures to allocate all costs to projects;**
- **ensuring that, in future, all applications for funding received are retained for at least 2 years, in order to maintain an adequate information trail for the grant selection process;**
- **reconciling the value of grants approved for specific projects and programs to the amounts expended on these projects and programs;**
- **greater public disclosure of grant recipients and the value of the grants provided, in the annual reports of DSE and individual authorities; and**
- **developing appropriate project monitoring and evaluation procedures.**

3.9.444 **In addition, project reporting could be enhanced by authorities reporting the following information in relation to their major projects:**

- **earned value analysis, including variations to project budget and actual costs;**
- **estimated costs at completion, including variations to project budgets;**

Recommendations - *continued*

- **a risk assessment, with further analysis provided in relation to high-risk projects; and**
- **an analysis of milestone achievements and shortfalls.**

External reporting

3.9.445 Under current Australian Accounting Standards, grant revenue received by authorities is considered to result from a non-reciprocal transaction. That is where the provider of grant money does not directly benefit from the use of the money. The appropriate treatment of this revenue is to recognise it once the authority controls it, which is usually when the grant is received.

3.9.446 This treatment of grant funding results in the recording of revenue on receipt, while the associated grant expenditure is recognised when it was incurred. Where projects are completed in the financial year in which funding is provided, revenues and expenses are recognised by the authority in the same year.

3.9.447 However, where projects extended over more than one reporting period, this treatment results in financial statements recognising a surplus in relation to specific projects, in the year in which grant moneys are received, followed by deficiencies in following years.

3.9.448 There are also no statutory or accounting requirements for authorities to disclosure grant moneys is received, for which the conditions of funding have not been met. This amount represents the likely future cost to the authority of works required to finalise its uncompleted projects.

3.9.449 Application of Australian Accounting Standards to grant funding, combined with the absence of any requirement for authorities to disclose details of outstanding commitments in respect of grants received, makes it difficult to determine from a review of an authority's financial statements, how well it is managing its grant funding.

Recommendation

3.9.450 **We have recommended that authorities include additional information in their financial statements relating to outstanding project commitments.**

Other issues identified by the audit

Adequacy of systems and procedures

3.9.451 With the significant influx of Commonwealth funding, and associated growth in operations, many authority businesses have outgrown their basic financial and project management systems and procedures. In some authorities, management no longer has access to the type and detail of information needed to make informed business decisions.

Recommendation

3.9.452 **Authorities should review their systems and procedures to ensure they are still adequate to meet their needs.**

Recent departmental initiatives

3.9.453 In recognition of the problems associated with project costing, DSE, in conjunction with the authorities, has employed a contractor to develop and implement a Project Costing Framework and assess accounting systems currently used by authorities. Each authority has agreed to seek expressions of interest for the development of an appropriate accounting and project management system for all authorities.

3.9.454 DSE has also advised that it is also currently developing *Projects In Action*, a new project management framework for its project management processes. It is intended to link this framework with CMA project reporting arrangements under the regional management process, and that CMA project data will be loaded onto a corporate system, which will be capable of automatically sending reminders of impending projects reporting to authorities. It is expected that this pro-active interaction will assist authorities with both the timeliness and quality of their project reporting.

***RESPONSE** provided by the Secretary, Department of Sustainability and Environment*

The Auditor-General has provided a wide-ranging report regarding Victoria's catchment management arrangements following a request in June 2002 by the former Minister for Environment and Conservation, the Hon. Sherryl Garbutt MP, that the AG review the financial position of the East Gippsland Catchment Management Authority.

The Department of Sustainability and Environment has assisted the Victorian Auditor-General's Office with information for the finalisation of this report. The Department acknowledges the significance of the issues raised, and is giving close attention to these issues.

It is noted that research for the report was undertaken by the Victorian Auditor-General's Office predominantly during the latter half of 2002 following the former Minister's request.

Since that time, the Government has established the Department of Sustainability and Environment to provide a strong policy focus on sustainability as a key objective of Government.

Among the key initiatives identified within the newly formed Department's 2003-06 Corporate Plan, is to improve the governance framework for Catchment Management Authorities (CMAs) and to deliver on a range of sustainability policy outcomes for Victoria's catchments.

Consistent with this framework, the Department has introduced a range of initiatives during the past year relating to arrangements for catchment management, specifically:

- *Release of the Government's Green Paper 'Securing Our Water Future' which canvasses, among other things, institutional and funding arrangements for future catchment management and river health programs. A White Paper providing the Government's policy decisions on these matters will be released in 2004;*

***RESPONSE** provided by Secretary, Department of Sustainability and Environment - continued*

- *The appointment of a Commissioner for Environmental Sustainability responsible for reporting on the state of the environment in Victoria and auditing implementation of environmental management systems by public authorities;*
- *Renewal of Regional Catchment Strategies and development of three-year Regional Catchment Investment Plans for each catchment in conjunction with CMAs;*
- *The appointment of new CMA Boards and the introduction of a Board Performance Appraisal process; and*
- *A comprehensive internal audit of the governance, financial management and business practices of CMAs.*

The Department has also initiated several projects in conjunction with CMAs to improve management, costing, reporting and auditing of CMA natural resource management programs funded by the State and Commonwealth governments, including those under the Natural Heritage Trust (NHT) and the joint Commonwealth/State National Action Plan for Salinity and Water Quality (NAP).

The Department will be further considering the issues raised in the Auditor-General's report to ascertain the extent to which they are being addressed through the Department's current work program and policy initiatives.

Part 3.10

Treasury and Finance

PORTFOLIO OVERVIEW

3.10.1 The Treasury and Finance portfolio comprises the Department of Treasury and Finance and 63 other entities providing a range of financial, superannuation, insurance and regulatory services. The Treasurer of Victoria, Minister for Finance and Minister for WorkCover have responsibility for the Department and specific responsibility for individual entities within the portfolio.

3.10.2 Figure 3.10A profiles portfolio entities with 30 June 2003 balance dates.

FIGURE 3.10A
TYPE AND NUMBER OF AUDITED AGENCIES WITHIN THE TREASURY PORTFOLIO, AT 30 JUNE 2003
(number)

Reporting entity	*Number*
Department	1
Public bodies *(a)*	10
Superannuation funds	3
Companies, trusts and joint ventures	50
Total	**64**

(a) Public bodies include statutory authorities such as the Transport Accident Commission and the Victorian WorkCover Authority.

Source: Victorian Auditor-General's Office.

3.10.3 The Department of Treasury and Finance provides leadership in economic, financial and resource management across the Victorian public sector. It also delivers services associated with government financial reporting and budget, liability and risk management. The Department incorporates the operations of the State Revenue Office, which is the major revenue collection agency for the State, and the Victorian Government Purchasing Board, responsible for procurement and contracting policies and guidelines.

3.10.4 Activities of other portfolio entities include:

- provision of financial services through the Treasury Corporation of Victoria, Victorian Funds Management Corporation, Rural Finance Corporation and State Trustees Limited;
- management of statutory insurance schemes by the Transport Accident Commission, the Victorian WorkCover Authority and the Victorian Managed Insurance Authority;
- superannuation funds for parliamentarians and public sector employees, including the Parliamentary Contributory Superannuation Fund, the State Superannuation Fund and the Emergency Services Superannuation Board;
- regulation of major utilities including the electricity and gas industries by the Essential Services Commission; and

- management of residual financial and other obligations remaining from the privatisation of public sector utilities by the State Electricity Commission of Victoria and Gascor Pty Ltd.

3.10.5 Key financial statistics associated with portfolio responsibilities include:

- State tax collection - around $9 billion;
- Parliamentary appropriation administration - around $24 billion;
- Investment management – around $27 billion; and
- State liability management (including unfunded superannuation liabilities, insurance scheme outstanding claims and the State's debt portfolio) - around $39 billion.

RESULTS OF FINANCIAL AUDITS

Audit opinions issued

3.10.6 Clear audit opinions were issued on the financial statements of all portfolio entities with 30 June 2003 balance dates.

Timeliness of reporting

3.10.7 Figure 3.10B outlines the performance of portfolio entities in meeting the statutory reporting requirement during 2002-03.

FIGURE 3.10B
TIMELINESS OF FINANCIAL STATEMENT COMPLETION, TREASURY AND FINANCE PORTFOLIO *(a)*

Finalisation of audited financial statements (no. of weeks after end of financial period)	*2002-03*		*2001-02*	
	Number	*Per cent (cumulative)*	*Number*	*Per cent (cumulative)*
Less than 8 weeks	4	6	20	30
8 to 10 weeks	31	55	14	51
10 to 12 weeks	23	91	4	57
12 to 14 weeks	1	92	20	87
14 to 16 weeks	-	92	5	94
More than 16 weeks	5	100	4	100
Total	**64**	**-**	**67**	**-**

(a) Includes all audited financial statements as at 31 October 2003.
Source: Victorian Auditor-General's Office.

3.10.8 As indicated above, there has been significant improvement in the timeliness of completion of audited financial statements by entities in this sector, with 91 per cent of entities meeting the statutory 12-week completion time frame (57 per cent in 2001-02). Major reasons for the improvement were the earlier adoption of financial statements by the boards of State Trustees Limited and its associated entities and certain superannuation funds.

3.10.9 The financial statements of the Department of Treasury and Finance were finalised on 21 October 2003. As the Department administers a number of transactions with other Departments on behalf of the State, the finalisation of its statements is reliant on the completion of other departmental financial statements. Improvements in the timeliness of the Department's reporting process will, therefore, largely depend on other agencies meeting reporting targets in the future.

3.10.10 Appendix A to this report shows specific details of financial statements and audit opinions issued.

Quality of financial reporting

3.10.11 During 2002-03, we observed continued improvement in the quality of financial reporting by agencies within the portfolio. In particular:

- major agencies in the superannuation, insurance and finance sectors provided additional disclosure of certain key transactions and balances; and
- the implementation of quality control checklists for management to certify the completeness, accuracy and validity of information incorporated in the financial statements, significantly enhanced the financial reporting process in certain agencies.

3.10.12 Comments on further improvements to financial reporting and disclosure by certain agencies are outlined, where significant, in subsequent paragraphs.

Adequacy of control environment

3.10.13 A key responsibility of the management of each entity is to establish and maintain a sound control environment and an adequate system of internal controls to ensure that:

- the entity's financial records and other information completely and accurately reflect its activities;
- its assets are safeguarded; and
- irregularities are prevented, detected and corrected, should they occur.

3.10.14 Audit procedures designed to assess the control environment and the effectiveness of key entity controls are an integral part of financial statement audits. In this regard, the 2002-03 financial audit process confirmed that the overall control environments established within portfolio entities, and the associated systems of internal control subject to audit examination, were generally sound. Few significant control issues were identified within sector entities. However, agencies commenced action to improve procedures for:

- risk management and monitoring processes;
- budget management for new IT system developments; and
- managing excessive annual leave entitlements.

OTHER ISSUES OF SIGNIFICANCE

3.10.15 Comments follow on a number of other issues of significance arising from the 2002-03 financial audit process.

Superannuation funds

Unfunded defined benefit superannuation funds

3.10.16 At 30 June 2003, the State Superannuation Fund, Emergency Services Superannuation Scheme and the Parliamentary Contributory Superannuation Fund had a combined unfunded superannuation liability of $14 billion.

State Superannuation Fund

3.10.17 Figure 3.10C outlines the State Superannuation Fund's net fund assets, the value of member accrued benefits and resulting unfunded liability of the State.

FIGURE 3.10C
STATE SUPERANNUATION FUND
SUMMARY OF NET FUND ASSETS, ACCRUED BENEFITS AND UNFUNDED LIABILITIES

		*Year ended 30 June **2003***	*Year ended 30 June **2002***
Net fund assets	($000)	7 223 437	6 215 792
Value of members' accrued benefits	($000)	20 881 000	20 202 500
Value of the fund's unfunded liability	($000)	13 657 563	13 986 708
Level of accrued benefits unfunded	(%)	65.54	69.23

Source: State Superannuation Fund annual audited financial statements.

3.10.18 As at 30 June 2003, the Fund's unfunded liability was $13.7 billion, highlighting a slight improvement as a result of additional employer contributions made (relative to benefit accruals) offset partly by poorer than expected investment returns for the year. However, these investment returns were significantly better than in 2001-02.

3.10.19 The State Superannuation Fund's accrued benefits were valued by a recently appointed actuary at $20.9 billion. The actuary, as part of a triennial review (to be completed in December 2003 and undertaken as at 30 June 2003) is considering minor changes to the discount rate and mortality rate assumptions used for the valuation of members' accrued benefits.

Emergency Services Superannuation Scheme

3.10.20 As at 30 June 2003, the Emergency Services Superannuation Scheme reported an unfunded liability of $281 million compared with $71 million at 30 June 2002. The key contributor to this change has been negative returns in certain investment classes, particularly domestic and international equities. In addition, the employers' contribution rate set in respect of Victoria Police has been insufficient over recent years to fund the long-term cost of related benefits. This situation arose as contributions were set based on a previous actuarial surplus for the Victoria Police segment of the Fund.

3.10.21 The Emergency Services Superannuation Board has adopted a strategy that will see employer contributions better reflect the long-term cost of the scheme.

> ***RESPONSE*** *provided by the Chief Executive Officer, Emergency Services Superannuation Board*
>
> *We agree that the key contributor to the change in the unfunded liability was the negative investment returns in domestic and international shares.*
>
> *Employer contribution rates also had a minor impact, and while you are correct in stating that the Victoria Police contribution rate was lower than its long term rate because it was based on an actuarial surplus at 30 June 2001, so were the rates for the MFB, CFA and ASV. Contribution rates lower than the long term are designed to reduce actuarial surpluses and, as this occurs, rates will be increased gradually to the long term.*
>
> *The significant impact on the surpluses by investment returns may in turn require rates to increase to the long term sooner than previously expected. To increase rates, it is important to note that, in accordance with the Emergency Services Superannuation Act, the Board is required to give at least six months' notice to an employer. Therefore, for the year commencing 1 July 2002 employers were notified in December 2001 of their contribution requirements, following which there was considerable deterioration in the equity markets.*
>
> *The Board has also taken into consideration each employers' capacity to manage increases to the contribution rate. A request on behalf of the Victoria Police to increase its contribution rate by 0.5 per cent p.a. was accepted in February 2002.*

Parliamentary Contributory Superannuation Fund

3.10.22 Figure 3.10D outlines that, as at 30 June 2003, the difference between the Parliamentary Contributory Superannuation Fund's assets and its accrued benefits is an unfunded liability of $15.1 million. This fund deficiency has primarily arisen due to the overall decline in the performance of financial markets for the year ended 30 June 2003 and the higher level of benefit payments made following the 2002 State election.

TABLE 3.10D
PARLIAMENTARY CONTRIBUTORY SUPERANNUATION FUND
SUMMARY OF NET FUND ASSETS, ACCRUED BENEFITS AND UNFUNDED LIABILITY

		*12 months ended 30 June **2003***	*12 months ended 30 June **2002***
Net fund assets	*($000)*	184 634	183 935
Liability for members' accrued benefits	*($000)*	199 739	189 511
Value of unfunded liability	*($000)*	15 105	5 576
Members' accrued benefits unfunded	*(%)*	7.56	2.94

Source: Parliamentary Contributory Superannuation Fund annual audited financial statements.

3.10.23 The Fund's actuary has advised that the deficiency in net Fund assets is not a cause for concern. **It is expected that the Fund's deficiency in net assets will be remedied through increased funding recommended by the Fund's actuary and the recovery of financial markets.**

Timing of triennial actuarial valuations for superannuation funds

3.10.24 The triennial actuarial valuations of the state of both the State Superannuation Fund and the Emergency Services Superannuation Scheme as at 30 June 2003 were in progress but were not completed at the time of the finalisation of the 2002-03 financial statements. In the case of the State Superannuation Fund, the triennial valuation was due to be completed in December 2003 and the Emergency Services Superannuation Scheme triennial valuation was due for completion in October 2003, well after the 12-week financial statement completion deadline.

3.10.25 Given the current timing of triennial reviews, a potential risk exists that, due to changes in assumptions used in the triennial review, results may differ from those used to calculate liabilities as disclosed in annual financial statements.

Recommendation

3.10.26 **We recommend that the boards of the Government Superannuation Office and the Emergency Services Superannuation Scheme ensure that future triennial actuarial reviews are timed to allow incorporation of results in financial statements for the year to which the review relates.**

RESPONSE *provided by the Secretary, Department of Treasury and Finance*

The Department of Treasury and Finance (DTF) notes the recommendation that triennial actuarial reviews be timed to ensure that the outcome of the review can be incorporated into the financial statements for the year to which the review relates. Amongst other things, the triennial actuarial review involves an analysis of member data and fund experience over the preceding three years. Given that the State Superannuation Fund is a complex fund and has in excess of 150,000 members, DTF, together with the Government Superannuation Office, and the Fund's actuary, will investigate opportunities to bring forward the timing of the outcome of the triennial review.

With around 15 000 defined benefit members, the Emergency Services Superannuation Scheme (ESSS) is a much smaller fund and completion of future triennial reviews within a timeframe that would allow the results to be incorporated into the annual financial statements appears more feasible. DTF will discuss this matter with the ESSS Board.

RESPONSE *provided by the Chief Executive Officer, Government Superannuation Office*

We confirm our support for revising the timing of triennial actuarial reviews, to allow incorporation of the results in the financial statements for the year in which the review relates. The issue has already been raised with the State Superannuation Fund's Actuary, and a solution will be pursued following completion of the 2003 Triennial Review, due next month.

***RESPONSE** provided by the Chief Executive Officer, Emergency Services Superannuation Board*

> *While we do not anticipate there being issues in meeting the requirements of your recommendation, as the changes in assumptions relate primarily to the valuation of future benefits from 1 July, we consider that the use of the previous assumptions is an accurate reflection of the liabilities at 30 June.*
>
> *Consideration may also be given by the Department of Treasury and Finance to requesting estimates of any impact as part of the budget process in the months prior to a triennial actuarial review.*

Insurance sector

Applicability of APRA guidelines for State insurances

3.10.27 On 1 July 2002, the Australian Prudential Regulatory Authority (APRA) released guidelines for private sector general insurers which require:

- a prudential margin be incorporated in general insurance outstanding claims liability valuation calculations to provide a 75 per cent probability of sufficiency; and
- capital adequacy reserves should be set aside to provide for solvency and other risks.

3.10.28 In addition, work currently underway by the International Accounting Standards Board (IASB) is supporting the utilisation by general insurers of a prudential margin and risk free discount rates in the determination of the net present value of a general insurance entity's outstanding claims liability. In addition, recommendations of the recent HIH Royal Commission support the APRA guidelines and international standards.

3.10.29 The APRA guidelines are not applicable to public sector-based insurers. The Department of Treasury and Finance is consulting with the Transport Accident Commission, Victorian WorkCover Authority and Victorian Managed Insurance Authority as to whether APRA guidelines should be used for State-based insurance schemes.

3.10.30 In the absence of clear guidelines for the government sector, the 3 State insurance bodies currently adopt different philosophies and practices for prudential margins, risk-free discount rates and capital adequacy reserves. While recognising that the operations of the 3 entities may differ, the lack of consistency in these areas precludes effective comparison of performance across the 3 bodies.

Recommendation

3.10.31 **We recommend that an appropriate and consistent liability valuation regime be implemented for the State's insurance bodies. In developing this regime, consideration should be given to the APRA guidelines, developments in international financial reporting standards and the recommendations of the HIH Royal Commission.**

***RESPONSE** provided by the Chief Executive Officer, Victorian Managed Insurance Authority*

The Victorian Managed Insurance Authority (VMIA) values its outstanding claims substantially in accordance with the APRA guidelines. VMIA is advised by its Actuaries that the 25 per cent prudential margin included in its outstanding claims provision produces a result that is broadly equivalent to the APRA guideline that there should be a 75 per cent probability of the reserves proving adequate. VMIA uses risk-free discount rates in the determination of the net present value of its actuarially assessed outstanding claims liability.

The VMIA Board has determined that it is necessary to set aside capital adequacy reserves to provide for solvency and other risks. Since its formation in 1996 VMIA has had a comprehensive Reserving and Solvency Policy which is reviewed at least annually and specifies VMIA's target level of reserves. VMIA's target reserves and solvency margins are considered appropriate at this time.

VMIA has also carried out an assessment of the other prudential standards issued by APRA and has identified those sections that VMIA will voluntarily adopt. A number of these have already been implemented as best practice.

Victorian Managed Insurance Authority - Renegotiation of public healthcare insurance arrangements

3.10.32 My November 2003 *Report on the Finances of the State of Victoria* provided a brief outline of the arrangements in place underpinning the Public Healthcare Insurance Program (PHIP). The Victorian Managed Insurance Authority manages the PHIP on behalf of the Department of Human Services on a "claims made" basis, that is, when a party makes a claim.

3.10.33 At 30 June 2003, the Authority was owed $118.1 million, reflecting the shortfall between funding provided by the Department of Human Services ($117.4 million) and the actuarially assessed liability for outstanding claims of $235.5 million.

3.10.34 The arrangements for the PHIP were due to cease on 30 June 2003. However, the Authority has subsequently extended this arrangement until 1 January 2004, while it renegotiates the arrangement with the Department.

State Electricity Commission of Victoria (SECV) *Equity accounting for Snowy Hydro Limited*

3.10.35 My previous *Report on the Finances of the State of Victoria* commented on the corporatisation of the Snowy Mountains Hydro-electric Authority (SMEHA), which had been established by the Commonwealth Government in 1949.

3.10.36 The "Snowy Scheme" was completed in 1974 and consists of an integrated system of dams, aqueducts and tunnels collecting, storing and diverting the headwaters of 3 catchments – the Murray, Murrumbidgee and Snowy rivers. In addition to the utilisation of the water for irrigation purposes, the water from the Snowy Scheme is used to generate electricity as it passes through a system of hydro-electric power stations. The Snowy Scheme provides valuable back-up electricity supply for the Victorian, NSW and ACT markets.

3.10.37 Under the *Snowy Hydro-electric Power Act* 1949 and subsequent administrative arrangements, NSW was entitled to 58 per cent of the Scheme's electrical energy, Victoria 29 per cent and the Commonwealth Government 13 per cent. In 1997, a new company, Snowy Hydro Trading Pty Ltd (SHTPL), was established by the NSW Government and the State Electricity Commission of Victoria (SECV), as a joint venture, to trade electricity generated by the Snowy Scheme in the new national electricity market regime. The Commonwealth Government formally joined in 2000.

3.10.38 With responsibility for managing residual rights and obligations not directly allocated to the State's privatised electricity business, the SECV had responsibility for electricity supply contracts relating to Victoria's power entitlements associated with the Snowy Scheme. Under this arrangement, the SECV had received annual distributions from SHTPL in proportion to Victoria's 29 per cent entitlement.

3.10.39 On 28 June 2002, SMHEA was corporatised and merged with SHTPL to form Snowy Hydro Limited (SHL). All shares held in SHTPL (held in proportion with entitlements) were transferred under the *Snowy Hydro Corporatisation Act* 1997 to SHL. As a consequence, the SECV recognised a gain of $236.6 million in its 2001-02 financial statements being Victoria's share of the combined net assets held by SHL and SHTPL at the time of corporatisation. This significant gain was also reflected in the Annual Financial Statement of the State of Victoria.

3.10.40 The SECV now accounts for this "investment" using the equity method of accounting by recognising the increment/decrement in the carrying value by reference to SHL's current operating results adjusted for any dividends received. In 2001-02, the SECV had received $38.7 million under the previous arrangements. The SECV received a final settlement sum of $8.7 million during 2002-03 and recognised an amount of $38.2 million being the SECV's share of the 2002-03 operating surplus generated by SHL.

Recommendation

3.10.41 **We recommend that the SECV monitor the trading activities of SHL to ensure that the reported carrying value of its investment in SHL remains fairly stated.**

***RESPONSE** provided by the Secretary, Department of Treasury and Finance*

Consistent with the performance monitoring arrangements for other significant Government Business Enterprises, DTF is responsible for monitoring the State's investment in Snowy Hydro Limited (SHL) and the State Electricity Commission of Victoria. Due to the size of the investment in SHL ($274.9 million at 30 June 2003), it is appropriate for this monitoring to be undertaken centrally by DTF.

Victorian Funds Management Corporation and State Trustees Limited Consolidated reporting of multiple trusts and funds

3.10.42 Consistent with the *Financial Management Act* 1994, separate financial statements have been prepared for each trust and fund managed by the Victorian Fund Management Corporation (8 VFM trusts) and State Trustees Limited (16 individual trusts and funds). Each set of financial statements contains information specific to each trust and fund. However, there is a significant level of information repeated across each set of financial statements.

3.10.43 Of relevance is the evolving better practice of consolidated trust financial statements within the funds management industry. This style of reporting typically involves aggregating common and specific information relevant to each trust in one document. This practice provides efficiencies in the preparation of financial information and facilitates use of this information by readers of annual reports.

Recommendation

3.10.44 We recommend that Victorian Funds Management Corporation and State Trustees Limited investigate the potential for consolidating aspects of trust and fund reporting. A change to this basis of reporting may require consideration of exemptions required from certain reporting provisions of the Financial Management Act.

***RESPONSE** provided by the Secretary, Department of Treasury and Finance*

The Department of Treasury and Finance (DTF) has received advice from State Trustees Limited that any recommendations resulting from a review of this matter will be investigated in conjunction with the Auditor-General's representative.

MANAGEMENT OF MAJOR INJURY CLAIMS BY THE TRANSPORT ACCIDENT COMMISSION - STATUS OF RECOMMENDATIONS MADE IN PREVIOUS PERFORMANCE AUDIT REPORT

Introduction

3.10.45 Victoria’s transport accident compensation scheme, administered by the Transport Accident Commission, is funded from annual compulsory charges levied on owners of registered motor vehicles and from returns generated on investment funds of the Commission. Victoria has one of the few motor vehicle accident compensation schemes that provide no-fault access to comprehensive lifetime care. The benefits and services provided to injured persons under the scheme include the reasonable costs of:

- hospital, medical, and other treatments;

- personal aids, appliances, or support services;
- income replacement; and
- compensation.

3.10.46 At any one time, around 40 000 ongoing claims are managed by the Commission.

Performance audit 2001

3.10.47 In 2001, our Office undertook a performance audit of the *Management of major injury claims by the Transport Accident Commission*. At the time of our 2001 audit, approximately 4.6 per cent of ongoing claims were for clients with major injuries, including:

- acquired brain injury;
- spinal cord injury; and
- amputations, severe burns and other injuries.

3.10.48 The audit focused upon major injury claims due to the lifetime care required, their complexity and the magnitude of cost. Although major injury claimants represent a small proportion of total active claims, they constitute a substantial proportion of the scheme's liabilities (46 per cent, or $1 878 million at the time of the audit). Major injury claims continue to represent a significant proportion of the scheme's liabilities (50 per cent, or $2 374 million at 30 June 2003). The audit examined whether the Commission managed major injury claims efficiently and effectively.

3.10.49 The audit assessed the Commission's compliance with its claims management policies and guidelines, and assessed performance against best practice standards in case management. During the audit, discussions were undertaken with a select number of claimants, service providers and other key stakeholders.

3.10.50 Our Office's performance audit report was tabled in Parliament in October 2001. Recommendations in the report were directed at 3 key areas, namely:

- financial and strategic management;
- maximising claimant outcomes; and
- work practices that supported claimant management.

Outline of our approach to the follow-up review

3.10.51 We recently reviewed the Transport Accident Commission's progress in actioning the recommendations made in the performance audit report. Given that 2 years have passed since the performance audit, we expected to see significant progress towards implementing the recommendations made in the report. It is, however, too early to conduct a follow-up audit. We, therefore, undertook limited additional investigations to assess the accuracy of the information provided.

3.10.52 To assist our review, we provided the Commission with a schedule of the recommendations in our October 2001 report, along with the Commission's published responses. We asked the Commission to review that material and to forward to us details of:

- recommendations which have been acted upon and progress in implementation;
- improvements that have occurred as a result of the actions taken; and
- recommendations that have not been acted upon and the reasons for inaction.

3.10.53 We reviewed the information provided and visited the Commission to discuss progress with key officers involved in the management of major injury claims. We also consulted with a selection of external stakeholders to obtain their perspectives on the action taken by the Commission to address the report's recommendations.

Agency progress with audit recommendations

Financial and strategic management

3.10.54 The Commission's financial performance and its ability to sustain long-term financial viability is affected by the cost and volume of transport accident claims. Our recommendations focused upon long-term cost containment and the development of strategies to reduce the number of claims.

Commission's actions

3.10.55 The Commission has continued to monitor areas of key claims expenditure for major injury claimants, e.g. lifetime care and paramedical payments, on a monthly basis. The Commission advised that average administration costs per claim have reduced from $2 125 in 2000-01 to $1 882 in 2002-03.

3.10.56 Ongoing administration costs are managed by an annual review of Major Injury Division staffing numbers which takes into account the volume of claims being managed by each staff member. Since the audit, a change in structure was implemented to create a more efficient management structure that better responded to claimant and staff needs. Two senior management positions have been removed from the Division.

3.10.57 To reduce the rate of growth of liabilities for one-to-one attendant care, and to improve claimant outcomes, a new service delivery model "Lifetime Support" has been introduced. Specific programs funded under the model, e.g. employment and leisure options, were subjected to internal costing prior to implementation. Financial targets have been established for other programs, e.g. community case management programs, and are regularly monitored.

3.10.58 The Commission has invested in the Victorian Government's *arrive alive!* road safety strategy, which aims to achieve a 20 per cent reduction in the road toll between 2002 and 2007, and has also developed:

- the *Howsafeisyourcar* website;
- the internet-based *Go Melbourne* guide;
- the *Drive Right 1* and *Drive Right 2* reward programs;

- the *Wipe off 5* advertising campaign; and
- a short film produced by young people, for young people, about youth risk-taking behaviour.

3.10.59 The Commission advised that survey data indicate programs are having a positive impact upon consumer attitudes to vehicle purchase and speeding, and average travel speeds on Victorian roads.

Maximising claimant outcomes

3.10.60 In our 2001 report, we recommended that the Commission should ensure that the specific case management requirements of claimants are made adequately and equitably, to maximise claimant outcomes. We also recommended a wide range of actions to address work practices that support claimant management such as:

- exploring innovative ways to deliver better treatment outcomes;
- allocating services to claimants in line with a holistic assessment of need;
- focusing service providers on the delivery of outcomes;
- exploring care options that maximise independence and promote quality of life; and
- increasing the involvement of support co-ordinators and case managers in discharge planning.

Commission's actions

3.10.61 Subsequent to our 2001 audit, the Commission has undertaken a large number of activities aimed at delivering better outcomes for claimants. A major step has been the introduction of the Lifetime Support Initiative. Individual plans are developed for each Major Injury Division claimant based on a holistic needs assessment, which takes into consideration the claimant's:

- personal background prior to the accident;
- personal interests and activities;
- level of ability and capacity to undertake daily activities;
- personal goals; and
- type and level of supports required.

3.10.62 Consideration of key risk factors associated with recovery form part of the claimant's individual plan, i.e.:

- whether the claimant lives with ageing parents;
- the risk of family/informal support breakdown;
- any other medical conditions that existed before, or developed after, the accident; and
- any adverse social circumstances that existed before the accident.

3.10.63 Additional risk factors that may lead to the need for more intensive services are specified in guidelines used by the Major Injury Division.

3.10.64 The Commission has engaged external community case managers to develop the plans for all new claimants. Community case managers are also responsible for co-ordinating claimants' discharge from hospital and for reviewing the progress of claimants as they re-integrate into the community. The community case management program was progressively introduced between June and December 2002, and is now offered to all new Major Injury Division claimants. Existing claimants are being reviewed against standards specified under the Lifetime Support Initiative and assigned a community case manager where appropriate. The Commission anticipates that all existing Major Injury Division claimants will have been reviewed against the standards within the next 6 months.

3.10.65 Claimants' individual plans are initially reviewed by the Lifetime Support Panel, comprising experienced staff from the Major Injury Division, to ensure that a holistic and planned response has been applied to claimant needs, options for maximising independent re-integration into the community have been considered, and appropriate resources have been approved to meet these needs.

3.10.66 The Lifetime Support Initiative also offers claimants a range of "Shared Supported Leisure Options", to promote independence and to maximise quality of life. The options provide a range of community-based leisure choices that may serve as alternatives to one-to-one attendant care, depending upon the specific interests of individual claimants. Under the options, lead agencies are selected to broker a range of community services that meet the identified interests of claimants. For example, one agency has identified an interest in community camps and is currently developing options that will assist individuals to pursue these activities. Agencies also facilitate transport to and from these services for individual claimants, as agreed in their support plans. The Shared Supported Leisure Options program has been provided in partnership with the Department of Human Services, across all metropolitan regions, and its expansion into regional Victoria will be a focus of the Commission over the next 12 months.

3.10.67 The Vocational Pilot Project, a trial employment program, has recently been introduced for claimants with significant disabilities. It offers the potential to build upon recovery outcomes by targeting the ongoing development of specific abilities and skills for individual claimants in the community. The pilot will enable the Commission to investigate realistic outcomes of supported employment for claimants with significant disabilities, and key factors in claimant selection and support that may lead to successful supported or open employment. The findings of this pilot may provide additional information to enable the development of specific return to work programs for major injury claimants.

3.10.68 Planned respite needs for carers are considered in the individual plans completed for all new claimants. Additional or ad hoc requests for respite care are reviewed by the Lifetime Support Panel on an individual basis.

3.10.69 Other actions undertaken by the Commission to maximise claimant outcomes, since our audit in October 2001, include:

- Continued funding of the Victorian Trauma Foundation, to develop a “world class” system for treating trauma through better infrastructure, service co-ordination and integration. The Commission advised that preliminary analysis of data indicates that this is having a positive impact upon treatment outcomes for Victorians;
- Amending contracts with private rehabilitation hospitals to enable routine participation by support co-ordinators and case managers in the discharge planning process. Work practices, including those relating to discharge planning, have also been agreed with the public sector rehabilitation provider. Support co-ordinators and case managers are now able to actively participate in the discharge planning process;
- Introducing a Clinical Justification Program to focus upon measurable and sustainable client outcomes resulting from interventions provided by rehabilitation and disability service providers. This Program initially focused upon the provision of physiotherapy services, and is being progressively introduced to other rehabilitation providers including osteopaths, chiropractors, occupational therapists, speech pathologists and psychologists. Professional bodies are being actively encouraged to investigate specific outcome measures for use with the Commission’s claimants. These outcome-focused initiatives have been supported by the recent publication of core *Principles of Therapy* for the range of rehabilitation providers;
- Implementing a “daily support option” to improve the provision of attendant care to claimants with very high support needs. Under this option, one carer is available to the claimant throughout the day, minimising disruption to the claimant who might otherwise experience multiple carers in any one day, and saving costs to the Commission.

  The Commission has established contracts with a panel of attendant care agencies and is currently in the process of establishing key performance indicators for introduction into the next round of contracts (effective from January 2004). The Commission encourages claimants to discuss any concerns about their attendant care agency with their support co-ordinator. Contracts that include requirements about complaints management are currently in place.

3.10.70 The Commission is also developing options for claimants with stable support needs to purchase their own supports and services, with funds provided by the Commission. Services and supports would be purchased in accordance with an agreed plan that outlines a menu of potential services that may be purchased within a pre-approved budget, further maximising the independence of claimants who choose this option. The self-purchasing option will be piloted from December 2003 to June 2004.

Work practices supporting claimant management

3.10.71 Our recommendations around working practices supporting claimant management focused upon adopting best practice case management, monitoring and review of outcomes, better communication with claimants, building relationships with key stakeholder groups and developing the Commission's staff involved in managing claimants.

Adopting best practice case management

3.10.72 We recommended that the Commission should adopt best practice case management standards for assessing and monitoring claimant outcomes.

Commission's actions

3.10.73 The Commission has adopted a formal definition of case management, endorsed by the Case Management Society of Australia, to guide its program development and evaluation. It has also implemented strategies that encompass the major categories of best practice case management that were developed for our 2001 audit. Case-by-case and aggregate monitoring of these activities occurs via 3 major mechanisms, including:

- Major Injury Division internal audits;
- Lifetime Support Panel Database reviews; and
- reviews by specialist panels, e.g. Medical Panel, Building Modifications Panel.

Monitoring and review of claimant outcomes

3.10.74 We recommended that the Commission continue to explore options for improving its monitoring and review of claimants.

Commission's actions

3.10.75 The Commission undertakes internal file audits and monthly reviews of data to monitor the quality of its service planning, and to identify key cost drivers for Major Injury Division claimants.

3.10.76 In addition, files are monitored for each claimant on an annual basis until their circumstances are deemed to be stable. Claimants who experience a 12-month period of low level and stable support needs are transferred to a monitoring team. Claimants may be reviewed or transferred for more intensive monitoring, at any stage, if their circumstances change.

3.10.77 The Commission monitors the performance of the community case managers to identify key issues, good work practices, and opportunities to enhance the performance of case management services and to provide feedback to case managers. It also seeks feedback from clinical service providers on a regular basis.

3.10.78 The Commission has created a framework for developing outcome measures and research studies investigating key components of the Lifetime Support Initiative. In addition to the Vocational Pilot Project, the Commission has sought 2 independent contractors to (separately) examine:

- the discharge processes experienced by claimants; and
- key outcomes and ongoing measures for claimants who choose to participate in the Shared Supported Leisure Options program.

3.10.79 We look forward to the Commission's evaluation of the effectiveness of the Lifetime Support Initiative as a whole.

Better communication with claimants

3.10.80 We recommended that the Commission should examine the cost-effectiveness of options for better communicating with claimants, especially with respect to their entitlements.

Commission's actions

3.10.81 The Commission has recently revised and enhanced its communication materials for claimants that outline entitlements under the scheme, such as its TAC*Info* brochures, and developed material on what to expect from the Lifetime Support Initiative. The brochures are provided to claimants, and discussed during their face-to-face meetings with support co-ordinators. The provision of relevant information is monitored as part of the file review process for all new and existing claimants. Although no internal compliance audit has been undertaken relating to the timely provision of re-written information, capacity exists within the Major Injury Division databases to undertake such activity.

3.10.82 Introduction of the *empower* newsletter enables the Commission to share important experiences of claimants, and to inform claimants about key issues and opportunities for exploring community resources.

3.10.83 Our follow-up review has indicated that there is further room for improvement in the provision of timely information to claimants. We recommend that a formal assessment of the timeliness with which the re-written information is provided to claimants is undertaken as part of the normal Major Injury Division file audit program.

3.10.84 The Commission conducts research into the overall impact, specific recall of material, personal attitude, and suggested improvements to information material. Claimant and family feedback has been positive in relation to the re-developed TAC*Info* brochures. The Commission advised that other research has indicated that written material has a wider rate of uptake than other forms of communication, e.g. web-based products. Further development of written information provided to children and families is planned. The Commission has decided not to adopt pre-determined time periods of claimant contact (including a practice of annual home visits) recommended in our audit report, as it considers this approach to be inconsistent with the aims of modern disability philosophy, i.e. to respect the rights of individual claimants and to cease to continue offering support when it is no longer required.

Building relationships with key stakeholder groups

3.10.85 We recommended that the Commission develop expertise in disability service delivery through building sound relationships with key parties and involving stakeholder groups in formulating practices and responsive strategies for meeting the needs of major injury claimants.

Commission's actions

3.10.86 The Commission has undertaken extensive work in this area which includes:

- Developing the Lifetime Support Initiative which is aligned with, and supports, the Victorian State Disability Plan;
- Establishing a Disability Advisory Committee to review major initiatives, proposals and communication products for claimants with disabilities. The Committee is comprised of Commission representatives, key sector stakeholders, and expert advisors including 2 members who experience disabilities who are Commission claimants, and 2 members who experience disabilities who are not Commission claimants;
- Creating the position of Staff Development Officer to inform support co-ordinators in disability issues and the Lifetime Support Initiative and to develop their skills;
- Sponsoring and/or conducting conferences, seminars and workshops for key stakeholders;
- Visiting service providers and peak bodies to receive and discuss feedback; and
- Implementing shared supported leisure options with key community agencies.

3.10.87 Our review indicates that regular opportunities for communication with the Commission and stakeholders enhances the development of better strategies for meeting the needs of major injury claimants. Stakeholders believe that their concerns are being listened to and acted upon.

Developing the Commission's staff

3.10.88 We recommended that the Commission should:

- undertake an assessment of skills and competencies of support co-ordinators with a view to providing appropriate training and development where gaps in expertise are identified, to enhance the knowledge and skills, including in respect of long-term management of claimants;
- provide opportunities for staff to participate in innovative learning through secondment placements in the relevant community sectors;
- continue to seek and evaluate staff attitudes and opinions and put in place strategies to address emerging issues; and
- communicate to support co-ordinators its expectations of their role and responsibilities in the management of claimants and maintenance of scheme viability.

Commission's actions

3.10.89 We found that the Commission undertakes a range of activities to support the knowledge and skills of support co-ordinators, including:

- identifying individual areas for learning in annual performance and development reviews;
- providing information at regular and planned training and development sessions where staff can identify topics for presentation;
- providing ongoing one-on-one support by senior support co-ordinators and team managers;
- providing specific training about the Lifetime Support Initiative; and
- providing regular feedback about benefit management and the Lifetime Support Initiative from the Major Injury Division's audit process and data reviews.

3.10.90 The Commission is developing an on-line version of training for the Lifetime Support Initiative, to be made available to new support co-ordinators. The Commission has also provided training opportunities to enhance the skills and knowledge of community case managers. Opportunities for specific staff secondments into the community sector will be explored over the next year.

Summary of agency progress

3.10.91 The Commission has made significant progress in implementing the recommendations made in our 2001 performance audit report.

***RESPONSE** provided by the Chief Executive Officer, Transport Accident Commission*

Thank you for providing the Transport Accident Commission with an opportunity to respond to the above report. The Commission welcomes this report and its validation of the many actions the Commission has taken to improve the way we provide support to those seriously injured on our roads.

Two years ago, the Commission commenced a major review of its approach to supporting and improving the lives of clients needing long-term care. This led to the development the new Lifetime Support model. The philosophy behind Lifetime Support is to fund the right support for clients living with disabilities to rebuild their lives and participate in the life of the community. In essence, it is about shifting the focus from a medical model to a social model – placing the client at the centre of everything we do and helping them to re-connect with their local community. Already, we have seen more than 110 clients engaged in various work, leisure and home options under the new model – and clients are telling us that it is making a real difference to their lives. At the same time, the rate of growth of liabilities has slowed. It is very gratifying, therefore, to have the significant progress we have made over the past 2 years recognised and independently verified through this report.

A primary objective of the Commission is to build effective partnerships with its clients and their families to respond to their unique care, support and treatment needs. We note the finding at 3.10.87 that: "Stakeholders believe that their concerns are being listened to and acted upon". Equally we acknowledge and accept the report's single follow-up recommendation at 3.10.83 that the Commission implement, as part of the normal Major Injury Division file audit program, a formal assessment of the timeliness with which re-written information is provided to clients.

Finally, we also welcome the report's reference at 3.10.58 and 3.10.59 to the Commission's investment in the Victorian Government's arrive alive! road safety strategy. It is worth noting that Victoria has just recorded it's lowest-ever financial year road toll – with 83 fewer deaths than the previous 12 months and a 6 per cent reduction in hospitalised claims.

Thank you again for the opportunity to respond to your comprehensive report.

Part 3.11

Victorian Communities

PORTFOLIO OVERVIEW

3.11.1 The Victorian Communities portfolio comprises the Department for Victorian Communities, together with 101 local government sector entities and 7 smaller entities with specific event or service delivery responsibilities within the portfolio.

3.11.2 While administrative responsibility for the local government sector rests with the Victorian Communities portfolio, given its size and nature, we have separately reported on the key issues arising from our financial audits in this sector in a later part of this report.

3.11.3 Figure 3.11A provides a profile of portfolio entities (excluding local government) with 30 June 2003 balance dates, for which we have audit responsibility.

FIGURE 3.11A
TYPE AND NUMBER OF AUDITED AGENCIES WITHIN THE VICTORIAN COMMUNITIES PORTFOLIO (EXCLUDING LOCAL GOVERNMENT), AT 30 JUNE 2003

Reporting entity	*Number*
Department	1
Statutory authority	1
Companies, trusts and joint ventures	6
Total	**8**

Source: Victorian Auditor-General's Office.

3.11.4 The Department for Victorian Communities was established on 1 January 2003 as part of the machinery of government changes announced by the Government in December 2002. The aim of the Department is to "build cohesive communities" through a more integrated approach to planning, funding and delivering of services at the local level. The Department provides support to a diverse range of ministerial portfolios, including:

- Victorian Communities
- Employment and Youth Affairs
- Multicultural Affairs
- Women's Affairs
- Aboriginal Affairs
- Local Government
- Sport and Recreation
- Commonwealth Games

3.11.5 A range of responsibilities were transferred to the Department from other government departments as from 1 January 2003 as a result of the machinery of government changes, as outlined in Figure 3.11B.

FIGURE 3.11B
RESPONSIBILITIES TRANSFERRED TO THE DEPARTMENT OF VICTORIAN COMMUNITIES, 1 JANUARY 2003

Transferring department	*Responsibility transferred*
Department of Premier and Cabinet	• Victorian Multicultural Commission • Victorian Office of Multicultural Affairs • Office of Women's Policy • Public Records Office of Victoria • Government and Community Information • Community Support Fund • Community Building
Department of Infrastructure	• Local Government
Department of Innovation, Industry and Regional Development	• Employment Programs
Department of Natural Resources and Environment	• Aboriginal Affairs • Community Programs
Department of Education and Training	• Youth Affairs
Department of Justice	• Registry of Births, Deaths and Marriages

3.11.6 The activities of the other portfolio entities are as follows:

- Melbourne 2006 Commonwealth Games Pty Ltd[1] - responsibility for scoping and planning the operational requirements, including the negotiation of a number of key contracts, for the Melbourne 2006 Commonwealth Games;
- Melbourne and Olympic Parks Trust, and State Sports Centre Trust - responsibility for the care, improvement, use and promotion of sports facilities, including Melbourne Park, Olympic Park, Melbourne Sports and Aquatic Centre, and the State Netball and Hockey Centre;
- Victorian Institute of Sport and Victorian Institute of Sport Ltd - provision of an environment in which talented athletes have the opportunity to achieve at the highest level;
- Queen Victoria Women's Centre Trust - as custodian of the Queen Victoria site, manage the redevelopment of the site and resource, inform and encourage women throughout the community; and
- VITS Languagelink – provision of interpreting and translating services.

3.11.7 Some of the key annual financial statistics associated with portfolio responsibilities include:

- grant and other payment administration - around $214 million;

[1] The Company has been replaced by the Melbourne Commonwealth Games Corporation which was established on 7 October 2003 in accordance with the *Commonwealth Games Arrangements (Governance) Act* 2003.

- sporting infrastructure asset management – around $436 million; and
- heritage asset management - around $140 million.

RESULTS OF FINANCIAL AUDITS

Audit opinions issued

3.11.8 Clear audit opinions were issued on all financial statements of portfolio entities with 30 June 2003 balance dates, with the exception of the Melbourne and Olympic Parks Trust. The Trust's financial statements were subject to qualification due to the overstatement of current liabilities of $7 million as at 30 June 2003. This is a continuing qualification from prior years.

3.11.9 In particular, the Trust has recorded a liability in its financial statements for the past 3 years in relation to a future commitment to contribute to the building of the State Training Velodrome at Northcote. A tripartite funding agreement between the Government, the Trust and the City of Darebin (which will control the asset on completion) was entered into in December 2001, which requires the Trust to pay the City of Darebin for works that have been completed in relation to the Velodrome. In our view, this represents a reciprocal transaction whereby the Trust is only required to make progress payments as the Velodrome is constructed.

3.11.10 Prior to the completion of construction milestones we contend there is no present obligation that justifies the need to recognise a liability. Accordingly, the Trust's treatment of the $7 million as a liability at 30 June 2003 does not, in our view, satisfy the liability definition criteria contained in the Statement of Accounting Concepts SAC 4: *Definition and Recognition of the Elements of Financial Statements*.

Recommendation

3.11.11 **Given the ongoing nature of the qualification, we recommended the Trust reconsider its position in relation to the recognition of any remaining obligation at the end of the coming year, in order to enhance user confidence in the quality of its financial statements.**

RESPONSE *provided by the Secretary of Department for Victorian Communities*

> *Your comments in relation to this issue are noted and I understand the Trust has advised you of its reasoning for the accounting treatment. The Department will review the issue with the Trust as part of preparing the 2003-04 accounts.*

Timeliness of reporting

3.11.12 Figure 3.11C outlines the performance of portfolio entities in completing their financial statements for the 2002-03 reporting cycle.

FIGURE 3.11C
TIMELINESS OF FINANCIAL STATEMENT COMPLETION, VICTORIAN COMMUNITIES PORTFOLIO (EXCLUDING LOCAL GOVERNMENT)

Finalisation of audited financial statements (no. of weeks after end of financial period)	*2002-03*		*2001-02*	
	Number	*Per cent (cumulative)*	*Number*	*Per cent (cumulative)*
Less than 8 weeks	2	25	-	0
8 to 10 weeks	4	75	4	57
10 to 12 weeks	1	88	1	71
12 to 14 weeks	-	88	2	100
14 to 16 weeks	-	88	-	100
More than 16 weeks	1	100	-	100
Total	**8**	**-**	**7**	**-**

Source: Victorian Auditor-General's Office.

3.11.13 As indicated in Figure 3.11C, **there was an improvement in the overall timeliness of completion of audited financial statements by entities in this portfolio, with 88 per cent of entities meeting the 12-week statutory completion time frame (71 per cent in 2001-02)**. Appendix A to this report shows specific details of the financial statements and the issue of the audit opinions.

3.11.14 **The Department for Victorian Communities was the only entity within the portfolio not to meet the statutory deadline of 22 September 2003**. Final financial statements were signed by the Department on 22 October and the audit opinion issued on 27 October 2003. The key factors contributing to the Department's failure to meet the 12-week time frame included:

- additional accounting and other requirements arising from the January 2002 machinery of government changes;
- reliance this year on other departments for financial information in order to prepare the financial statements; and
- difficulties encountered in the restructure of the Department.

3.11.15 As these factors are mainly attributable to the machinery of government changes, they are not likely to result in any ongoing difficulties in reporting.

Quality of financial reporting and adequacy of the control environment

3.11.16 A key responsibility of the management of each entity is to establish and maintain a sound control environment and an adequate system of internal controls to ensure that:

- the entity's financial records and other information completely and accurately reflected its activities;
- its assets are safeguarded; and
- irregularities are prevented, detected and corrected, should they occur.

3.11.17 The quality of reporting by entities within the portfolio was maintained at a satisfactory level this year.

3.11.18 The 2002-03 financial audit process also confirmed that the overall control environment established within portfolio entities, and the associated systems of internal control subject to audit examination, were satisfactory. Various matters were, however, identified which required management attention. The most significant issues related to:

- the currency of valuations of fixed assets (Department for Victorian Communities, Melbourne and Olympic Parks Trust, and Queen Victoria Women's Centre Trust);
- the need for updated policy and procedures in relation to financial management and information technology security (Victorian Institute of Sport); and
- the absence of updated risk management and fraud control plans (Queen Victoria Women's Centre Trust).

3.11.19 In relation to asset valuations, the portfolio entities collectively manage significant sporting infrastructure, cultural and heritage assets. It is important that the values of these assets be reviewed regularly to ensure that the carrying amounts in the financial statements reflect their fair values.

Recommendation

3.11.20 **We recommend that all entities in the portfolio review their processes for obtaining timely and reliable information on the current values of their physical assets**.

***RESPONSE** provided by the Secretary of Department for Victorian Communities*

Currency of asset valuations

While the values of the assets concerned are reviewed on a regular basis, the Auditor-General's comments are noted and all entities detailed within the report will review their asset valuations during 2003-04.

Part 3.12

Local Government

SECTOR OVERVIEW

3.12.1 Local government is responsible for the delivery of a wide range of services to local communities. It also plays a major role in the provision of infrastructure, environmental management and leadership to local communities.

3.12.2 Constitutional responsibility for local government rests with the State which, through the *Local Government Act* 1989, has established the legal framework within which local governments operate. The Act establishes the purposes, objectives, functions and powers of local councils. Local Government Victoria, a Division of the Department for Victorian Communities, has responsibility for administering the Act.

3.12.3 While administrative responsibility for the local government sector rests within the Victorian Communities portfolio, given its size and nature, we have separately reported on the key issues in local government arising from our financial audits in this part of the report.

3.12.4 Figure 3.12A provides a profile of local government entities with 30 June 2003 balance dates, for which we have audit responsibility.

FIGURE 3.12A
TYPE AND NUMBER OF AUDITED AGENCIES WITHIN LOCAL GOVERNMENT, AT 30 JUNE 2003

Reporting entity	*2003*	*2002*
Municipal councils *(a)*	79	78
Regional library corporations *(b)*	14	15
Companies, trusts and joint ventures *(c)*	8	6
Total	**101**	**99**

(a) The former Delatite Shire Council was separated into the Benalla and Mansfield Shire Councils from 28 October 2002.
(b) The Hume-Moonee Valley Regional Library Corporation was wound-up as at 31 December 2002.
(c) Two new entities, the Sustainable Melbourne Fund Trust and the New City Library Joint Venture have been added this year.
Source: Victorian Auditor-General's Office.

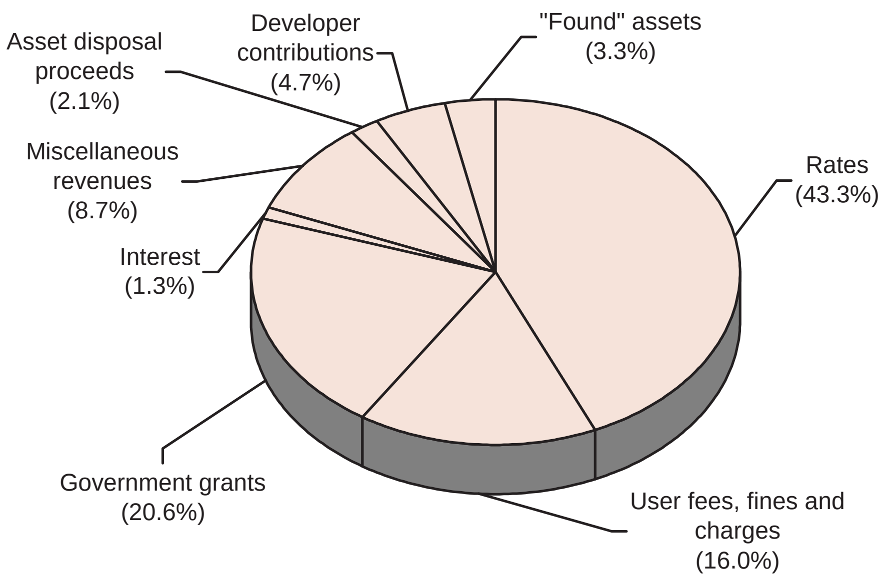
3.12.5 In addition to the audit of the financial statements of the above entities, we also have responsibility for the audit of performance statements prepared by the 79 municipal councils.

Outline of financial performance and position

3.12.6 In 2002-03, local government revenues were approximately $4.5 billion, while operating expenditures totalled around $4.2 billion. Sector entities managed some $34 billion in infrastructure and other non-current assets, together with $1.5 billion of current assets - mainly cash.

3.12.7 Figures 3.12B and 3.12C provide a dissection of the major sources or revenue and expenditure of municipal councils and related entities in 2002-03.

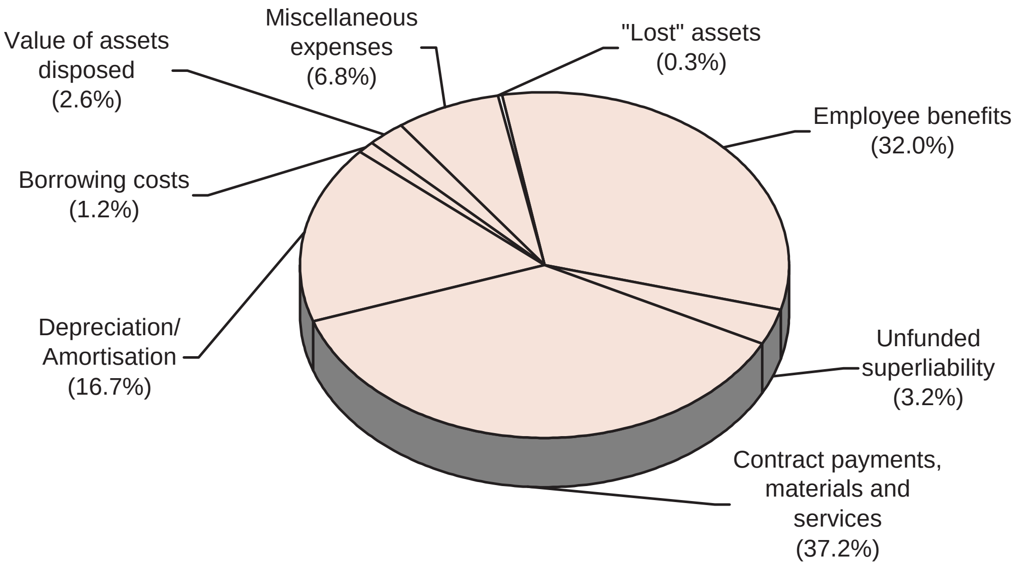
FIGURE 3.12B
SOURCES OF MUNICIPAL COUNCIL REVENUES, 2002-03



3.12.8 Rates, together with user fees and charges, are the main sources of revenue generated by councils from their operations. The extent of reliance on other sources of revenue (predominantly grants) varies according to the geographic location of each council. Country Victorian councils rely more heavily on grants than metropolitan councils.

3.12.9 In Figure 3.12B, “found” assets represent assets already owned and/or controlled by Councils which had not been previously recorded in the financial statements. Developer contributions are assets that have been provided to councils at no cost, as part of agreements with developers. The accounting standards require these assets to be treated as revenues when first recognised in the financial statements.

FIGURE 3.12C
SOURCES OF MUNICIPAL COUNCIL EXPENDITURES, 2002-03



3.12.10 Figure 3.12C sets out the principal proportions of expenditure in municipal councils in 2002-03. Employee-related expenses (salaries, wages, superannuation and leave) represent the single largest operating cost to local government. They include an amount of $113.7 million associated with the "unfunded superannuation liability" of the Local Authorities Superannuation Fund as at 30 June 2003, relating to council employees. The sector employs in excess of 30 000 staff.

3.12.11 The "lost" assets expense relates to the value of assets transferred to other entities at no charge, and assets that no longer exist or are not controlled and, accordingly, were written out of the accounting records of the Council in the year.

Financial viability assessment

3.12.12 **The combined net operating result for all municipal councils and related entities for 2002-03 was $334.4 million, which is equivalent to 4 per cent of total revenues in the year. However, as indicated in Figures 3.12B and 3.12C, both "developer contributions" and "found assets" contributed significantly to total revenues, while "lost" assets impacted to a lesser extent on total expenditures. Excluding these items from the operating result produces an overall "underlying operating deficit" for municipal councils and related entities of $15.1 million in the year.**

3.12.13 The combined revenues for all regional library corporations for the year totalled $55.2 million. The major sources of revenue were contributions from member councils (48 per cent) and government grants (45 per cent). **All but one regional library corporation reported an operating deficit for the year, with the combined deficits totalling $3.1 million. The inability to generate substantial revenues directly from their own operations and the annual operating deficits that characterise these entities mean that all are reliant on external support for their continuing operation**.

3.12.14 The cash position of both municipal councils and regional library corporations was satisfactory at year-end, with councils collectively holding approximately $1 billion in cash and cash equivalents and regional library corporations holding around $11 million in such assets. This represented around 3 months' operating expenditure on average for both groups.

3.12.15 The overall combined "current" ratios of the 2 groups (the ratio of current assets to current liabilities) were also satisfactory, with a ratio of 2.1 to 1 for municipal councils and 1.6 to 1 for regional library corporations. The current ratio is one indicator of the ability of an entity to pay its existing liabilities in the next 12 months. A ratio in excess of 1 to 1 is regarded generally as satisfactory. Only one municipal council had a current ratio less than 1 to 1 at year-end.

3.12.16 As indicated above, **the overall financial position of the local government sector and of individual councils at year-end is satisfactory**. In addition to the positive "current" ratios, levels of debt and associated servicing costs are generally low (around one per cent of revenues), with many councils debt free.

3.12.17 **However, the overall "underlying deficit" for the sector indicates that the financial performance of some councils for the year requires further examination. Operating deficits indicate councils are not generating sufficient revenue to cover their expenses.**

3.12.18 Thirty-two councils reported an operating deficit in 2002-03 (combined total deficits of $47.1 million). This number increases to 50 of the 79 municipal councils when operating results are adjusted to obtain the "underlying" result (combined total deficits of $152.9 million). Most "underlying deficits" were small, around 3 per cent on average, when compared with total "underlying revenues". However, 9 councils reported deficits that exceeded 10 per cent of their underlying revenues.

3.12.19 During the year, the sector was advised of its obligation to make-up a shortfall in the local authorities defined benefit superannuation scheme of $113.7 million. This was in addition to the normal annual contribution. The requirement for the sector to contribute to this shortfall had a major impact on the financial results for this year. This expense was on average 3.2 per cent of underlying revenues, and explains most of the reported deficits for the year.

3.12.20 Operating deficits are not sustainable over the medium to long-term for any entity. A key governance responsibility of councillors is to ensure the ongoing financial sustainability of council operations**. Those councils that experienced underlying operating deficits in 2002-03, particularly where this has been a recurring pattern in recent years, need to carefully scrutinise their underlying financial performance.**

Recommendation

3.12.21 **We recommend close consideration be given by councils to key indicators of short to medium financial health, including projected trends in the councils' future operating results, "current" ratios and the cash position.**

3.12.22 One factor that has the potential to impact on the long-term sustainability of the sector is the "asset renewal gap"; that is, the difference (if any) between the rate of consumption of the service potential provided by existing assets and the rate of renewal or replacement of this service potential. Councils need to be able to retain sufficient funds from their own operations or be able to source external funds through either grants or borrowings, to replace assets as they are used up. If they are unable to generate sufficient funds, councils will either need to keep assets in service beyond their intended lives, with the potential for degradation in service levels, or incur increasingly costly repairs and maintenance to maintain service levels.

3.12.23 A proxy indicator used by the sector to measure the renewal gap is the relationship between the annual depreciation charge and annual capital expenditure. This indicator is based on the expectation that, over the long-term, the amount spent on the renewal or replacement of assets should equal or exceed the depreciation charge. On an annual basis, this indicator is less satisfactory because:

- depreciation accounts for the past consumption of service potential, which is not necessarily the expenditure required in the future to replace that service potential;
- the depreciation method utilised by all councils only approximates the actual consumption of service potential (it is based on a straight-line calculation), whereas actual consumption is likely to increase as assets age; and
- it is necessary to distinguish between capital expenditure that is for renewal or replacement of existing assets from that which relates to new assets or added capacity.

3.12.24 Notwithstanding these limitations, we undertook an analysis of reported figures for 2002-03. The resulting ratio of capital expenditure to depreciation was calculated to be 1.2 to 1 for all municipal councils combined. This is a favourable outcome, indicating that more was spent on asset additions this year than the combined depreciation charge. However, within the combined result, it was noted that 17 councils had an unfavourable renewal ratio for the year of less than 1 to 1. In 2 cases, the ratio was 0.49 to 1.

Recommendation

3.12.25 Given the significance of infrastructure assets to council operations and expenditures, and to their sustainability, we recommend councils develop appropriate indicators of their actual asset renewal gap to replace the proxy depreciation indicator.

RESULTS OF FINANCIAL AUDITS

3.12.26 A major governance responsibility of councils is the preparation and timely presentation in external reports of reliable financial and performance information. These reports are an important component of the public sector accountability framework and facilitate councillors' reporting on their stewardship of local government resources. This section of the report discusses the outcomes of our financial audits, and the timeliness and quality of the reporting processes adopted by councils.

Audit opinions issued

3.12.27 **Clear audit opinions were issued on all municipal councils with 30 June 2003 balance dates, except for the Swan Hill Rural City Council.**

3.12.28 Consistent with the previous year, the financial statements of the Swan Hill Rural City Council were qualified in 2002-03 because of its failure to undertake condition assessments for a significant proportion of its infrastructure assets. The absence of condition assessments means that the council was not able to adequately demonstrate that its estimates of the remaining useful lives of the affected assets were reliable. Accordingly, it was possible that the carrying values of those assets may have been materially misstated. The council has undertaken to carry out the necessary condition assessments as part of its revaluation of the relevant assets during the 2003-04 financial year.

3.12.29 It is pleasing to note that no new financial report qualifications were required for 2002-03 and previous audit qualifications were removed from the financial reports of 7 municipal councils, including the removal of one of the elements of the previous qualification of the financial report for the Swan Hill Rural City Council.

3.12.30 The removal of the 7 qualified audit opinions this year reflects, in part, the increasing maturity and reliability of asset management data. Most councils have now overcome, or are actively addressing, data problems associated with their "legacy" asset management and accounting systems. They have also completed at least one round of condition assessments for significant asset classes. However, in this regard, councils face a new challenge in maintaining the currency of their asset valuations.

3.12.31 **Clear audit opinions were issued on 74 of the 79 municipal council performance statements**.

3.12.32 Two new audit qualifications on performance statements were required for the Glenelg and Surf Coast Shire Councils respectively, for their failure to provide performance targets in their annual business plans for the 2002-03 year. There were also 3 continuing qualifications issued in relation to the performance statements of the Horsham Rural City, Buloke Shire and Wodonga City Councils. The first 2 of these councils failed to submit a corporate plan including a business plan, in accordance with the requirements of the *Local Government Act* 1989. In the case of the Buloke Shire Council, this has been a matter for qualification for the past 3 years. The Wodonga Rural City Council failed to maintain sufficient and appropriate records with which to establish actual performance for a significant proportion of its performance measures.

3.12.33 The qualifications of the performance statements of 6 other municipal councils were removed.

Recommendation

3.12.34 **We recommend that councils subject to ongoing and new qualifications:**

- **review their business planning processes, including the processes for the development of performance measures and targets; and**
- **integrate these measures and targets into their statutory business plans.**

3.12.35 **The continuing failure of councils to submit a corporate plan incorporating a business plan and performance targets to the Minister as required by the Local Government Act is unsatisfactory. It is a significant matter of non-compliance with the legislative framework governing the sector, and reflects a breakdown in good governance.**

Recommendation

3.12.36 **We recommend that councils submit the documentation required by the Act in accordance with the specified time frames.**

3.12.37 The financial reports of the 6 companies and joint venture entities associated with municipal councils that had been finalised at the time of preparation of this report were unqualified (also in 2001-02), as were the financial reports of all the regional library corporations in both years.

Timeliness and quality of reporting

3.12.38 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 and audited financial statements, to the Minister for Local Government within 3 months of the end of the financial year. The annual report is also required to include an audited performance statement.

3.12.39 Figures 3.12D and 3.12E outline the performance of municipal councils and regional library corporations in meeting this statutory requirement for the 2002-03 reporting cycle. Appendix A to this report shows specific details of the financial statements and related audit opinions.

FIGURE 3.12D
TIMELINESS OF FINANCIAL STATEMENT COMPLETION, MUNICIPAL COUNCILS *(a)*

Finalisation of audited financial statements (months after end of year)	*2002-03*		*2001-02*	
	Number	*Per cent (cumulative)*	*Number*	*Per cent (cumulative)*
Less than and up to 2 months	-	-	-	-
2 to 3 months	77	97	60	77
3 to 4 months	1	99	12	92
More than 4 months	1	100	6	100
Total	**79**	**-**	**78**	**-**

(a) Includes all audited financial statements as at 31 October 2003.
Source: Victorian Auditor-General's Office.

3.12.40 Two municipal councils, the Alpine and Buloke Shires, were granted an extension of the 30 September 2003 deadline by the Minister for Local Government, to 31 October 2003 and 15 November 2003, respectively. The remaining 77 councils met the 30 September deadline for financial statement certification. Only one of these councils, Ballarat City, failed to meet the statutory deadline for the certification of its performance statement.

3.12.41 As shown in Figure 3.12E, all regional library corporations met the 3-month reporting requirement for the 2002-03 reporting cycle.

FIGURE 3.12E
TIMELINESS OF FINANCIAL STATEMENT COMPLETION, REGIONAL LIBRARY CORPORATIONS *(a)*

Finalisation of audited financial statements (months after end of year)	*2002-03*		*2001-02*	
	Number	*Per cent (cumulative)*	*Number*	*Per cent (cumulative)*
Less than and up to 2 months	1	7	-	-
2 to 3 months	13	100	9	60
3 to 4 months	-	-	6	100
Total	**14**	**-**	**15**	**-**

(a) Includes all audited financial statements as at 31 October 2003.

Source: Victorian Auditor-General's Office.

3.12.42 Finally, 5 (62.5 per cent) of the 8 associated companies, trusts and joint venture entities also met the 30 September timetable. The financial statements of the Regent Management Company Pty Ltd, which is jointly owned by the Melbourne City Council and the State of Victoria, were certified by management on 27 October 2003 (19 December 2002 in the previous year) and an unqualified audit opinion was issued on 31 October 2003. The financial statements of the Sustainable Melbourne Fund Trust and the New City Library Joint Venture were yet to be finalised at the time of preparation of this report.

3.12.43 The above figures indicate that **there was significant improvement by municipal councils and regional library corporations in meeting their statutory time frames during 2002-03, reflecting substantial effort by sector agencies in enhancing the timeliness of reporting.**

3.12.44 **However, we noted that only 2 councils were able to finalise and certify their financial statements prior to September 2003. Accordingly, there remains considerable scope to improve the timeliness of financial reporting.**

3.12.45 **Timely reporting is a characteristic of an effective accountability process. It is, therefore, important that councils seek to continuously improve their processes both to improve timeliness, and reduce the cost, of financial reporting.**

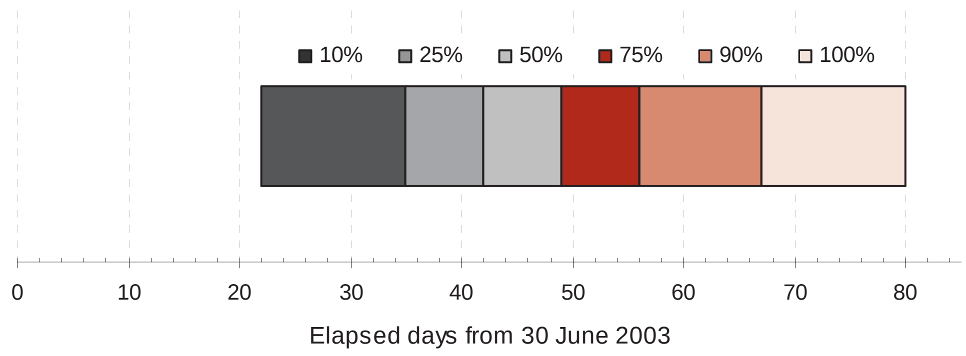
3.12.46 Consideration of the financial reporting process indicates there are a number of major milestones in the external reporting cycle that impact on the ability of local government entities to meet or better statutory reporting time frames. Some critical milestones being:

- preparation and provision of a first draft financial statements to the external auditor;
- verbal audit clearance of the final draft financial statements after all audit queries and proposed audit adjustments have been made;
- “in-principle” approval of the final draft financial statements by the council;
- certification of the financial statements; and
- provision of the audit opinion on the certified financial statements.

3.12.47 Each of these milestones represents a possible delay point in the reporting process that can impact on cycle times. However, the starting point is the receipt by the auditor of “acceptable” first draft financial statements from the council.

3.12.48 An analysis of the performance of municipal councils in relation to this milestone for the 2002-03 cycle is depicted in Figure 3.12F. The figure shows the elapsed time from the end of the financial year to the provision to audit of draft financial statements by municipal councils, by percentile bands.

FIGURE 3.12F
CYCLE TIMES TO PROVIDE DRAFT FINANCIAL STATEMENTS TO AUDITORS - MUNICIPAL COUNCILS, 2002-03



3.12.49 Seven weeks (or 49 days) was the average elapsed time for the receipt of draft financial statements by auditors. However, the last of the 77 municipal councils which met the 30 September deadline, provided draft financial statements on 18 September 2003, some 80 days from the end of the financial year.

3.12.50 **Based on the above analysis, it is clear that it is possible for most councils to achieve earlier finalisation of their financial statements**. Good practice, using the above result for the 10 percentile band (35 days), indicates that all councils could finalise their draft financial statements by the first week of August, which would result in the receipt of audit certification before the end of the second week of September.

3.12.51 Where councils experienced delays in preparation of their financial reports, some common contributing factors noted were:

- lack of planning for the year-end reporting process;
- lack of planning and insufficient lead-times allowed for activities that support financial report preparation, especially in relation to the revaluation of assets;
- lack of qualified staff involved in preparing financial reports and, in particular, a lack of understanding of the requirements of new and revised accounting standards; and
- insufficient resources devoted to the external reporting function.

Recommendation

3.12.52 **We recommend that councils whose performance was outside the 50 percentile band (49 days) critically review their year-end close-off and external reporting processes to identify opportunities for reduced cycle times. Particular regard should be given to planning for, and resourcing of, this process.**

SIGNIFICANT FINANCIAL REPORTING ISSUES

3.12.53 This section of the report identifies the major financial reporting and accounting issues faced by municipal councils in the preparation of their 2002-03 financial reports.

Valuation of infrastructure assets

3.12.54 Property (land and buildings), infrastructure (road networks, footpaths, drains, bridges) and plant and equipment, dominate the "balance sheets" of municipal councils. They comprise around 96 per cent of the total non-current assets of the sector. The carrying value of non-current assets at 30 June 2003 was $32.6 billion, compared with total non-current liabilities of $769 million. The depreciation expense attributable to these assets for 2002-03 was $694 million, which represented around 17 per cent of total operating expenditures. Collectively, councils invested $808 million during 2002-03 on replacement, renewal and addition of physical assets.

3.12.55 Apart from minor plant and equipment, the physical assets of councils are generally long-lived and complex in nature. However, with the exception of land, all assets have finite lives and require ongoing repair and maintenance in order to maintain satisfactory service levels and achieve intended design lives.

3.12.56 Valuation is the major challenge for councils in accounting for, and reporting on, physical assets. Councils have adopted the valuation basis for measuring their major classes of assets rather than historic cost. For such assets, the Australian Accounting Standards now require that they be valued at "fair value" whenever a revaluation is undertaken. The Standards also provide that all such assets must be revalued and stated at their fair values by 30 June 2005. For infrastructure assets, this typically involves establishing a "written-down replacement cost" - that is, the current cost of purchasing or constructing a new asset, reduced to take account of the expired life of the existing asset.

3.12.57 Our analysis shows that most councils had established fair values for at least one class, if not most classes, of their physical assets at 30 June 2003. Where this had occurred, the analysis indicates that the carrying value of these assets was approximately 75 per cent of their gross replacement cost. This suggests that, on average across the sector, these assets are one-quarter through their lives. However, there will be significant variation between councils in this regard, depending on the age profile of their assets.

3.12.58 **Those councils which have not yet revalued their infrastructure assets to fair value face a significant challenge in meeting the 30 June 2005 timetable, given the typically long lead-times required to plan, execute and report on a valuation exercise. In this regard, we noted that a small number of councils have yet to finalise plans to support their progressive revaluation strategies.**

3.12.59 The challenge for all councils will be maintaining the currency of their valuations once they are at fair value. In 2002-03, this was an issue for a small number of councils that had already recorded assets at fair value at 30 June 2002. It will be an issue for many more councils in 2003-04, where fair values were determined for the first time in 2002-03.

Recommendation

3.12.60 **We recommend that councils finalise plans for the progressive revaluation of their assets, and establish a systematic approach to annually reviewing the carrying value of their assets to ensure the currency of these values.**

3.12.61 A related issue, observed in 18 of the councils that revalued assets in 2002-03, was the lack of effective communication between the preparers of the financial statements and the personnel who undertook the valuations (both in-house and external).

3.12.62 The most common cause for concern was the lack of clear, formal instructions to the valuers. Many councils provided only verbal instructions to their valuers. Councils risk incurring costs on a valuation exercise that does not provide them with the data they require. It is important that valuers are made aware of the basis (fair value) and purpose (external financial reporting) of the valuation and that they are advised of any matters that may affect the valuation, such as the planned sale or rezoning of assets. Formally documented instructions also provide clarity in the allocation of responsibility - for example, whether the valuer is responsible for establishing the completeness and accuracy of the asset register as part of the valuation exercise.

3.12.63 It was also observed at some councils that valuation reports were inadequate, in that they did not confirm or state the basis of the valuation, did not state any significant assumptions or limitations, or did not document the valuation process. This lack of documentation limits the usefulness of the valuation exercise as an input to the subsequent annual re-assessment process and future formal valuations.

Recommendation

3.12.64 **To maximise the utility of asset valuations, we recommend that councils ensure that sufficient and appropriate instructions are provided to valuers, including specification of the form and content of valuation reports.**

Debt collection

3.12.65 In 2002-03, councils generated some $101 million in revenues from parking fines and related charges, representing 2.7 per cent of total sector revenues. The inner-metropolitan councils collect the majority of this revenue ($89 million or 75 per cent).

3.12.66 However, not all fines are paid when issued. At 30 June 2003 there was approximately $105 million in unpaid fines across all councils, of which $60 million (or 57 per cent) was provided for by councils as doubtful debts.

3.12.67 Based on the annual charge to the provision for doubtful debts, and discussions with councils, **there is evidence that at least 10 per cent of parking and related fines are never collected. This represents an annual revenue leakage from the sector of around $10 million.**

3.12.68 Councils must weigh the cost of recovery of outstanding debts against the likely return from their recovery actions. Most councils that issue parking fines have standard recovery actions, including the issue of "courtesy" reminder letters and final letters of demand, before they refer the matter to the courts for enforcement. Some councils are considering taking, or have taken, a more pro-active approach to debt recovery of fines prior to court action, including issuing reminder notices earlier when debts first become overdue, and the employment of mercantile agents to pursue outstanding debts. While these actions have an associated cost, they can prove cost-effective if they improve recovery rates.

3.12.69 As parking fines are issued in the form of infringement notices, unpaid fines can be referred to the Penalty Enforcement by Registration of Infringement Notice (PERIN) Court, which is a venue of the Magistrates Court. Unless unpaid fines are referred within 12 months of the infringement notice being issued, they are not able to be enforced through the PERIN system. Councils are required to pay an up-front fee when the fine is referred to the PERIN Court. This fee is returned to a council only when fines are paid.

3.12.70 The experience of councils has been that the recovery rate of unpaid fines after referral to the PERIN Court is very low because of the nature and age of the debt, and the lack of previous success in recovery. Accordingly, councils typically provide for the majority, if not all, of this class of outstanding debt as doubtful.

Recommendation

3.12.71 **We recommend that councils with significant unpaid fine debtor balances consider whether taking a more pro-active approach to the recovery process would provide net benefit. A key consideration is whether any initiatives will be more cost-effective when compared with traditional recovery methods that rely ultimately on legal enforcement.**

Unfunded superannuation liability

3.12.72 The total liabilities of local government entities increased in 2002-03 as a result of a call for additional funding made by the Local Authorities Superannuation Fund. The Fund identified a shortfall of $127 million in its net assets, arising from an actuarial assessment carried out at 31 December 2002 of the defined benefit plan that it administers on behalf of local government entities and other local authorities. The local government share of this shortfall was determined to be $113.7 million. Consequently, the Fund invoiced local governments for this amount, grossed-up by a factor of 1.1765 (total $133.8 million) to take into account the 15 per cent federal contributions tax payable on superannuation contributions.

3.12.73 The local authorities superannuation defined benefit plan was constituted under the *Local Authorities Superannuation Act* 1988. As a defined benefit plan, the superannuation liability of participating employers (such as councils) is tied to the final average salary of each member and their period of membership, rather than the amount of their contributions and earnings. While the plan is not open to new entrants, all past and present member entitlements continue in force and local authorities are required to provide sufficient funds to finance the superannuation entitlements of the members.

3.12.74 The traditional method of financing an actuarial shortfall is to increase the employer contribution rate. However, this was deemed by the Trustee of the Fund not to be a realistic option for a closed pension fund, as the number of active members as a proportion of total members will naturally decline over time. Consequently, local councils were invoiced the unfunded liability at 30 June 2003 and are required to repay the debt over a maximum 10 year period. Entities were given the option to repay the amount in full or to pay by instalments. The minimum annual instalment is one-tenth of the initial outstanding liability, with interest chargeable on a monthly basis for the amount unpaid, based on the Fund's net earning rate.

3.12.75 At 30 June 2003, the majority of local government entities had either elected to pay the debt by instalments and/or to adopt a "wait and see" approach in terms of both the monthly Fund net earning rate and the future performance of the Fund. It is understood that at least 10 councils repaid the debt in full in the first quarter of the 2003-04 financial year. Five of these councils borrowed funds to finance the repayment. The rationale for borrowing funds, where internal reserves were not considered sufficient, was that the interest rate for commercial debt was expected to be less than the earnings rate of the Fund.

Recommendation

3.12.76 **We recommend that councils which have yet to pay their share of the unfunded superannuation shortfall develop payment and funding strategies, and regularly review these strategies, in light of the current and future earning rates of the Fund.**

Employee benefits provisions

3.12.77 The combined employee benefits provisions of all councils totalled $250 million (17 per cent of total liabilities) at 30 June 2003, representing a significant liability requiring careful management by councils.

3.12.78 The issue of excessive annual leave balances in local government has been ongoing for a number of years. In the current year, it was again noted that significant numbers of staff in 19 councils had an accrued liability for their annual leave in excess of 8 weeks (the equivalent to 2 years of entitlements).

3.12.79 As councils must pay staff leave entitlements at the salary rates applicable at the time leave is taken, the accrual of excessive leave balances has the potential to impact adversely on future operating costs, due to future pay rises. Further, there are potential issues of productivity and occupational health and safety where staff are working for extended periods without availing themselves of leave.

3.12.80 In 2002-03, the annual leave liability across all councils grew on average by 14.2 per cent ($14.6 million), from $102.3 million to $116.9 million. While the growth in this liability is partly explained by a change in accounting standards during 2002 -03 (under which annual leave entitlements are now required to be valued at the estimated rates of pay when they are expected to be settled, rather than the rates of pay applicable at balance date), it is clear that the majority of the increase is a result of the accrual of additional leave balances.

Recommendation

3.12.81 **Given that employee leave entitlements represent a significant component of council liabilities, we recommend that councils more actively manage the accumulation and settlement of these entitlements to ensure the associated costs are minimised.**

CONTROL STRUCTURE ISSUES

3.12.82 This section of the report outlines our observations on the internal control structures that operate at municipal councils.

3.12.83 An effective control structure is designed to ensure:

- effectiveness and efficiency of agency operations;
- agency assets are safeguarded;
- reliability of financial reporting, and
- compliance with applicable laws and regulations.

3.12.84 Councillors, as members of the governing body, together with management, are responsible for ensuring that appropriate control structures operate within the council and that these structures are effective in achieving their objectives. The various functions and processes that make up the control structure of an entity can generally be categorised as part of one of the following elements of control[1]:

- the control environment;
- risk assessment;
- control activities;
- information and communication, and
- monitoring and review.

The control environment

3.12.85 The control environment sets the tone of an organisation, influencing the control consciousness of its people. It is the foundation for all other components of internal control, providing discipline and structure. Control environment factors include the integrity, ethical values and competence of the entity's people; management's philosophy and operating style; the way management assigns authority and responsibility, and organises and develops its people; and the attention and direction provided by the governing body.

3.12.86 The audit committee is a key influence in the control environment. Its operation can strongly effect control consciousness and help to ensure local government entities produce reliable external financial information. The audit committee, comprising councillors and, in many cases, external members, is the major vehicle through which the external auditor communicates directly with the governing body. As part of the 2002-03 financial audit process, we reviewed the relationship between the audit committee and the external auditor.

Operation of audit committees

3.12.87 The June 2000 Best Practice Guidelines *Audit Committees and Internal Audit* issued by the Department for Victorian Communities, promote the establishment and effective operation of audit committees for local government entities and include, as part of the objectives for an audit committee:

- improving the credibility and objectivity of financial reporting; and
- improving the effectiveness of external audit and the effectiveness of communication between external audit and the entity.

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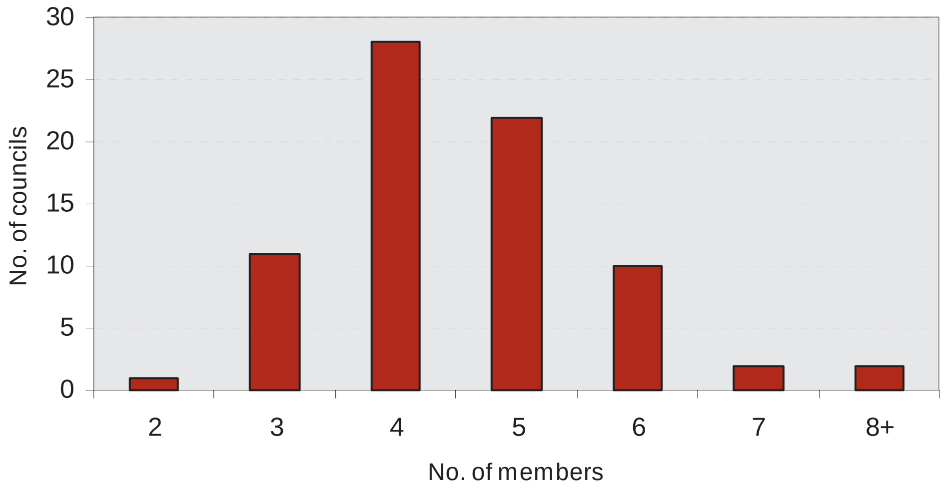
[1] *Internal Control - Integrated Framework*, 1992, Committee of Sponsoring Organizations of the Treadway Commission.

3.12.88 The guidelines recommend that the external auditor should have a right to attend committee meetings. They also provide that the committee liaise with, and monitor issues raised by, external audit. They indicate that it is good practice to meet with the external auditor at the start of each audit to discuss the engagement, and during the course of the year to discuss audit findings in relation to internal control and the financial statements. Finally, it recommends that audit committee members meet at least once privately with the external auditor without the presence of management or the executive to provide an opportunity to discuss openly any issues concerning management. The following findings are presented against these recommended better practices.

3.12.89 Most local government entities have now established an audit committee. While some councils established audit committees during the past year, only 2 councils (3 per cent) did not have a committee at year-end – Buloke and Horsham Shire Councils.

3.12.90 Figure 3.12G provides a summary of the range of total committee membership numbers across all municipal councils.

FIGURE 3.12G
MUNICIPAL COUNCIL AUDIT COMMITTEE MEMBERSHIP NUMBERS, AT 30 JUNE 2003



3.12.91 As shown, the number of members for audit committees averaged between 4 and 5 members. Two councils included all councillors on their audit committees and the smallest committee had 2 members. All but 4 council audit committees had at least one external member, with 2 being the average number of external members across all committees.

3.12.92 While almost all municipal councils have operational audit committees, there were indications that not all committees were fully effective. Issues raised with some councils in this regard included:

- lack of experience and knowledge of some members, particularly in relation to financial reporting (financial literacy);
- the inclusion of the chief executive officer and/or chief financial officer as voting members of the committee, rather than as observers;

- fewer audit committee meetings held than specified in the committee's charter, and
- narrow role and responsibilities for the audit committee, limited to consideration of only certain aspects of the internal control structure and/or financial reporting.

3.12.93 **These were isolated instances and not representative of the sector as a whole.**

Recommendation

3.12.94 **We recommend that all committees consider the extent to which these findings might apply to them and what impact they may have on the committee's overall effectiveness.**

3.12.95 The quality of the relationship between the external auditor and the audit committee is an important factor in the effectiveness of the audit committee. During the past financial year, the external auditor (our staff or authorised agents) attended, on average, only one audit committee meeting per council. For only 2 councils, the external auditor attended all audit committee meetings held. In 9 councils, the external auditor did not attend any audit committee meetings.

3.12.96 In 11 councils, the external auditor was not offered the opportunity to present the results of the financial audit to the audit committee prior to the financial statements being certified by the council.

3.12.97 **These findings suggest a lack of understanding in some councils in their dealings with the external auditor and the financial reporting process.**

Recommendation

3.12.98 **We recommend that all councils review the relationship between the external auditor and their audit committee to ensure that the committee is best placed to achieve its objectives.**

Risk assessment – fraud management

3.12.99 Most councils undertake a variety of activities and operations, ranging from planning and approval, inspection and enforcement, waste management, the provision of child care, home and aged care, and the operation of swimming pools. Many of these activities are inherently susceptible to fraud, due to the involvement of cash and other attractive assets, and due to the possibility of inducement for personal gain or benefit. As part of the 2002-03 financial audit process, we assessed the approach taken by councils to fraud risk assessment and control.

3.12.100 The incidence of fraud reported to audit during 2002-03 was low. Fraudulent activity or alleged activity was noted in 4 councils, relating to:

- misappropriation of revenues from remote cash collection sites (2 instances); and
- alteration or falsification of records (2 instances).

3.12.101 These and 11 other councils did not have a fraud control plan and had not recently undertaken or updated a fraud risk assessment.

Recommendation

3.12.102 **We recommend that all councils incorporate a fraud risk assessment and develop fraud control plans as part of their risk management frameworks.**

Control activities

3.12.103 Control activities are the policies and procedures that help ensure management directives are carried out. They include a range of activities as diverse as approvals, authorisations, verifications, reconciliations, reviews of operating performance, security of assets and segregation of duties.

3.12.104 The audit of local government financial statements may include, as required, a review of certain control activities to ensure that they were effective in terms of their design, implementation and operation throughout the year. We are pleased to report that no major weaknesses or significant breakdowns in control activities were identified in local government entities as part of the financial statement audit this year.

Information and communication

3.12.105 Relevant and reliable information must be captured, recorded and communicated in a form and time frame that enables councils and their staff to effectively and efficiently carry out their responsibilities. Information systems of local government entities produce reports containing operational, financial and compliance-related information, that make it possible to run and control these substantial and complex businesses.

3.12.106 The control objectives for information systems include ensuring the integrity, availability and confidentiality of data. Our financial audits of local governments identified a number of control issues in relation information and communication systems, relating to information security and information continuity. Further comment on these follows.

Information security

3.12.107 By far, the most common control weaknesses identified by audit related to access controls over operating systems and end-user applications. It was observed in several councils that one or more of the following control deficiencies existed during the year:

- sharing of passwords;
- no minimum password standards implemented (e.g. length of password, frequency of changes to passwords);

- passwords not being changed regularly and no system enforced intervals to force password changes;
- number of incorrect log-in attempts in a single session not restricted; and
- "super-user" access to accounting applications over-riding physical separation of incompatible duties.

3.12.108 **Failure to maintain appropriate security over information systems has the potential to jeopardise the integrity, availability and confidentiality of data held by local government entities.**

Recommendation

3.12.109 **We recommend that all councils review their information security regularly against an updated risk and threat assessment. This should include a review of the effectiveness of the operation of the controls established by management.**

Information continuity

3.12.110 We observed that 5 councils had not established, or had not updated, business continuity plans, including disaster recovery plans for the potential loss of information systems and associated data.

3.12.111 The absence of a current (and tested) disaster recovery plan exposes councils not only to possible loss of data but, consequentially, to loss of revenues and increased operating costs.

Recommendation

3.12.112 **We recommend that all councils review their business continuity management plans, including their disaster recovery plans, as their circumstances change (e.g. relocation of premises, introduction of new systems), and regularly test the effectiveness of these plans.**

Monitoring and review

3.12.113 Internal control systems need to be monitored to ensure that they remain effective. This is generally accomplished through ongoing monitoring activities, separate evaluations, or a combination of the 2.

Operation of internal audit functions

3.12.114 As part of fulfilling their governance responsibilities, it is common practice for the governing body (though the audit committee) and the chief executive officer of an entity to obtain assurance on the effectiveness of control systems through the internal audit process. In the absence of an internal audit function, it is incumbent on management and the governing body to seek alternative means of obtaining the necessary level of assurance on the operation of the control structure within their entity.

3.12.115 We identified that 12 councils either had no internal audit or a limited internal audit function operating throughout the past financial year. It was not apparent within these councils what other monitoring and review mechanisms had been established to inform management and the council on the effectiveness of internal control.

Recommendation

3.12.116 **We recommend that all councils periodically assess their monitoring and review activities to satisfy themselves that they are obtaining sufficient, appropriate and timely information on the effectiveness of internal control processes.**

COMPLIANCE ISSUES

3.12.117 Local governments are subject to the provisions of the *Local Government Act* 1989 and the supporting Local Government Regulations. Like all other entities, other laws including taxation law, workplace relations law, and occupational health and safety laws establish further compliance obligations.

3.12.118 Councillors and council management are responsible for ensuring compliance with the legislative and regulatory framework. The audit opinion on the financial reports of local government entities is not required to, and does not, provide assurance in relation to whether or not local government entities complied with the Local Government Act or the associated Regulations. However, during the course of our audit, where we identify matters of non-compliance, these are brought to the attention of the relevant entity. Below are comments relating to one such issue identified during the course of our audits.

Regulatory non-compliance - long service leave accounts

3.12.119 Regulation 18 of the Local Government (Long Service Leave) Regulations 2002 requires the establishment of a separate bank and/or investment account by all councils to provide sufficient cash to fund the long service leave entitlements of staff. Cash held in these accounts is annotated as a restricted asset in the financial reports of the relevant entities.

3.12.120 These accounts must have, at least once each year as a minimum balance, an amount equal to the long service leave liability calculated using a formula set out in the Regulations. Funds are only able to be transferred out of the long service leave bank and investment accounts to pay long service leave entitlements.

3.12.121 It was observed during 2002-03 that the following councils did not maintain separate bank or investment accounts in accordance with the requirements of the Regulations:

- Darebin City Council;
- Hume City Council;

- Horsham Rural City Council;
- Knox City Council;
- Mornington Peninsula Shire Council;
- Moyne Shire Council;
- Wyndham City Council, and
- Wodonga City Council.

3.12.122 Apart from Horsham Rural City Council, which indicated that it misinterpreted the requirement to maintain a separate account, the other mentioned councils intentionally do not maintain separate long service leave accounts. The rationale provided to support this position is that they are able to generate a better return on their invested balances where the funds are pooled with other general funds, or that they have scarce working capital and do not want cash "locked up" during the year that will not be required to be paid out until future years.

3.12.123 Most of the councils that do not maintain separate bank or investment accounts do, however, maintain a separate "ledger" account in the accounting records for the liability, so that they can manage and report separately on the long service leave cash balance.

Recommendation

3.12.124 We recommend that those councils which do not comply with the requirements of the regulations review and amend their practices.

3.12.125 We also noted that 8 councils, in addition to those mentioned above, did not maintain minimum balances in their bank and investment accounts equal to the amount determined in accordance with the statutory formula. However, in most cases the differences were minor.

3.12.126 It was also observed that the amount determined under the statutory formula differs from the requirements of the Accounting Standards. The statutory formula utilises average remuneration rates for the prior year, whereas the standard requires the use of expected future rates of remuneration to determine the long service leave liability in the financial reports of councils. The liability in the financial statements is accordingly greater at year-end than that determined by the formula.

Recommendation

3.12.127 Given the revised requirements of the Accounting Standards, we recommend the need for and/or the basis of the statutory formula in the Regulations be reviewed.

***RESPONSE** provided by the Secretary of Department for Victorian Communities*

> *Local Government Victoria will consider the anomaly given the revised requirements of the Accounting Standards in any subsequent review of the Local Government Long Service Leave Regulations.*

RECENT DEVELOPMENTS

The Local Government (Democratic Reform) Bill

3.12.128 In October 2003, the Government introduced the Local Government (Democratic Reform) Bill to Parliament. The Bill proposes a wide range of changes to the *Local Government Act* 1989, including changes to the planning, accountability and financial management provisions of that Act.

3.12.129 The more significant changes proposed by the Bill in the areas of planning, accountability and financial management, include the establishment of legislative requirements for councils to:

- discharge their resource management responsibilities in line with principles of sound financial management, similar to those which apply to the Victorian Government under the *Financial Management Act* 1994, including the prudent management of financial risks, ensuring that decisions are made having regard to their financial effects on future generations, and ensuring accurate and timely disclosure of information;
- establish a Council Plan which addresses a 4-year period and incorporates the Council's strategic objectives, a strategic resource plan and strategic indicators for monitoring the achievement of the objectives; and
- establish an audit committee.

3.12.130 An important feature of the Bill is the proposal to establish a requirement for council strategic resource plans (which cover a 4-year period), annual budgets and annual reports to all incorporate a set of standard financial statements, with the intention of facilitating greater transparency and accountability.

3.12.131 **It is important that councils and regional library corporations familiarise themselves with the Local Government (Democratic Reform) Bill and consider its implications in terms of their resource planning and financial management activities. This is particularly significant, given that the Bill proposes implementation of a range of reforms in these areas in the 2003-04 financial year.**

***RESPONSE** provided by Secretary of Department for Victorian Communities*

> *The Department is generally in agreement with the thrust of the recommendations for local government made in the report.*
>
> *Councils can be congratulated for improving the timeliness and quality of their reporting as signified by a reduction in the number of financial audit qualifications from 6 in 2002 to 1 in 2003.*
>
> *The improvement in the local government accountability framework introduced by the Local Government (Democratic Reform) Bill will assist in resolving issues regarding councils' planning.*

Appendix A

Status of audits with 30 June 2003 balance dates

PARLIAMENT

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
Parliament	4 Sep. 2003	✔	8 Sep. 2003
Victorian Auditor-General's Office *(a)*	8 Sep. 2003	✔	8 Sep. 2003

(a) The Victorian Auditor-General's Office was audited by a private sector auditor.

EDUCATION AND TRAINING

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
Department of Education and Training	3 Oct. 2003	✔	3 Oct. 2003
EDUCATION AND TRAINING			
Adult, Community and Further Education Board	19 Sep. 2003	✔	19 Sep. 2003
Victorian Curriculum and Assessment Authority	15 Sep. 2003	✔	19 Sep. 2003
Victorian Institute of Teaching	8 Oct. 2003	✔	9 Oct. 2003
Victorian Learning and Employment Skills Commission	22 Sep. 2003	✔	22 Sep. 2003
Victorian Qualifications Authority	1 Oct. 2003	✔	6 Oct. 2003
COMPLETED AUDITS – WITH OTHER BALANCE DATES *(a)*			
ACN 056 641 420 Pty Ltd (period 1 Jan 2002 to 15 Dec 2002)	1 Sep. 2003	✔	2 Sep. 2003
Dealdrum Pty Ltd (period 1 Jan 2002 to 15 Dec 2002)	1 Sep. 2003	✔	2 Sep. 2003
Dentire Pty Ltd (period 1 Jan 2002 to 15 Dec 2002)	1 Sep. 2003	✔	2 Sep. 2003
Kerbridge Pty Ltd (period 1 Jan 2002 to 15 Dec 2002)	1 Sep. 2003	✔	2 Sep. 2003
Meltech Services Ltd	30 May 2003	✔	12 Jun. 2003
Monash Commercial Pty Ltd	31 Mar. 2003	✔	10 Jun. 2003
Audit report contained an "emphasis of matter": *There was inherent uncertainty regarding continuation of a controlled entity as a going concern.*			
Monash ED Pty Ltd	16 Apr. 2003	✔	28 May 2003
Audit report contained an "emphasis of matter": *There was inherent uncertainty regarding continuation of entity as a going concern.*			
Monash Learningfast Pty Ltd	31 Mar. 2003	✔	28 May 2003
Audit report contained an "emphasis of matter": *There was inherent uncertainty regarding continuation of entity as a going concern.*			
Montores Pty Ltd (period 1 Jan 2002 to 15 Dec 2002)	1 Sep. 2003	✔	2 Sep. 2003
Monyx Pty Ltd (period 1Jan 2002 to 31 Dec 2002)	25 Aug. 2003	✔	19 Sep. 2003
Rinal Pty Ltd (period 1 Jan 2002 to 15 Dec 2002)	1 Sep. 2003	✔	2 Sep. 2003
RMIT International University Vietnam (RIUV) (period 1 Jan 2001 to 31 Dec 2001)	1 May 2002	✔	12 May 2002
RMIT International University Vietnam (RIUV) (period 1 Jan 2002 to 31 Dec 2002)	10 Mar. 2003	✔	22 Jul. 2003
RMIT Training Pty Ltd	23 May 2003	✔	26 May 2003

EDUCATION AND TRAINING- *continued*

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – WITH OTHER BALANCE DATES *(a)*			
RMIT Union	17 Apr. 2003	Qualified	12 Jun. 2003
Reason for qualification: *Inadequate accounting records due to deficiencies in the Academic Management System.*			
RMIT Vietnam Holdings Pty Ltd	16 Jun. 2003	✔	18 Jun. 2003
Rondole Pty Ltd (period 1 Jan 2002 to 15 Dec 2002)	1 Sep. 2003	✔	2 Sep. 2003
SouthWal Pty Ltd (period 1 Jan 2002 to 15 Dec 2002)	1 Sep. 2003	✔	2 Sep. 2003

INCOMPLETE AUDITS – AS AT 31 OCTOBER 2003	
Copyrat Pty Ltd *(b)* (period 1 January 2001 to 16 October 2001)	*Financial statements, covering period up to change in ownership, not yet prepared.*
Maccine Pty Ltd *(b)* (period 1 January 2001 to 30 November 2001)	*Financial statements, covering period up to change in ownership, not yet prepared.*
Victorian Tertiary Admissions Centre	*Audited financial statements yet to be finalised.*

(a) Financial statements with 31 December 2002 balance dates, unless otherwise indicated.

(b) Majority shareholdings changed in 2001 and, as a consequence, the entity is no longer controlled by the relevant university.

HUMAN SERVICES

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
Department of Human Services	10 Sep. 2003	✔	15 Sep. 2003
HEALTH			
Ambulance Service Victoria - Metropolitan Region	25 Aug. 2003	✔	27 Aug. 2003
Chinese Medicine Registration Board of Victoria	16 Sep. 2003	✔	16 Sep. 2003
Chiropractors Registration Board of Victoria	15 Sep. 2003	✔	19 Sep. 2003
Dental Practice Board of Victoria	8 Sep. 2003	✔	8 Sep. 2003
Health Purchasing Victoria	20 Aug. 2003	✔	20 Aug. 2003
Infertility Treatment Authority	4 Aug. 2003	✔	4 Aug. 2003
Mental Health Review Board	1 Sep. 2003	✔	1 Sep. 2003
Nurses Board of Victoria	17 Sep. 2003	✔	17 Sep. 2003
Optometrists Registration Board of Victoria	15 Sep. 2003	✔	15 Sep. 2003
Osteopaths Registration Board of Victoria	9 Sep. 2003	✔	16 Sep. 2003
Pharmacy Board of Victoria	20 Aug. 2003	✔	20 Aug. 2003
Physiotherapists Registration Board of Victoria	14 Aug. 2003	✔	14 Aug. 2003
Podiatrists Registration Board of Victoria	9 Sep. 2003	✔	22 Sep. 2003
Psychosurgery Review Board	8 Sep. 2003	✔	8 Sep. 2003
Rural Ambulance Victoria	1 Sep. 2003	✔	10 Sep. 2003
Victorian Health Promotion Foundation	17 Sep. 2003	✔	17 Sep. 2003
Victorian Institute of Forensic Mental Health	29 Jul. 2003	✔	15 Aug. 2003
Victorian Relief Committee	27 Aug. 2003	✔	1 Sep. 2003
PUBLIC HOSPITALS AND ASSOCIATED ENTITIES			
Alexandra District Hospital	22 Sep. 2003	✔	25 Sep. 2003
Alpine Health	26 Sep. 2003	✔	3 Oct. 2003
Austin and Repatriation Medical Centre	12 Sep. 2003	✔	17 Sep. 2003
Bairnsdale Regional Health Service	22 Sep. 2003	✔	25 Sep. 2003
Ballarat Health Services	28 Aug. 2003	✔	15 Sep. 2003
Barwon Health	10 Sep. 2003	✔	15 Sep. 2003
Bass Coast Regional Health *(a)*	9 Sep. 2003	✔	19 Sep. 2003
Bayside Health	25 Sep. 2003	✔	30 Sep. 2003
Beaufort and Skipton Health Service	19 Sep. 2003	✔	24 Sep. 2003
Beechworth Health Services	25 Sep. 2003	✔	2 Oct. 2003
Benalla and District Memorial Hospital	3 Oct. 2003	✔	3 Oct. 2003
Bendigo Health Care Group	15 Sep. 2003	Qualified	18 Sep. 2003
Reason for qualification: *Failure to revalue non-current physical assets.*			

HUMAN SERVICES - *continued*

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
Boort District Hospital	16 Sep. 2003	✔	18 Sep. 2003
Caritas Christi Hospice Limited	18 Sep. 2003	✔	18 Sep. 2003
Casterton Memorial Hospital	11 Sep. 2003	✔	12 Sep. 2003
Central Gippsland Health Service	22 Sep. 2003	✔	26 Sep. 2003
Cobram District Hospital	18 Sep. 2003	✔	22 Sep. 2003
Cohuna District Hospital	18 Sep. 2003	Qualified	19 Sep. 2003
Reason for qualification: *Failure to consolidate a "controlled" entity.*			
Colac Area Health	16 Sep. 2003	✔	22 Sep. 2003
Coleraine District Health Services	5 Sep. 2003	✔	11 Sep. 2003
Dental Health Services Victoria	17 Sep. 2003	✔	22 Sep. 2003
Djerriwarrh Health Services	9 Sep. 2003	✔	15 Sep. 2003
Dunmunkle Health Services	19 Sep. 2003	✔	22 Sep. 2003
East Grampians Health Service	25 Sep. 2003	✔	2 Oct. 2003
East Wimmera Health Service	22 Sep. 2003	✔	23 Sep. 2003
Eastern Health	30 Sep. 2003	✔	2 Oct. 2003
Echuca Regional Health	3 Sep. 2003	✔	16 Sep. 2003
Edenhope and District Memorial Hospital	18 Sep. 2003	✔	22 Sep. 2003
Gippsland Southern Health Service	9 Sep. 2003	✔	18 Sep. 2003
Goulburn Valley Health	9 Sep. 2003	✔	19 Sep. 2003
Hepburn Health Service	24 Sep. 2003	✔	24 Sep. 2003
Hesse Rural Health Service	23 Sep. 2003	✔	26 Sep. 2003
Heywood Rural Health	11 Sep. 2003	✔	12 Sep. 2003
Inglewood and Districts Health Service	18 Sep. 2003	✔	19 Sep. 2003
Kerang and District Hospital	17 Sep. 2003	✔	19 Sep. 2003
Kilmore and District Hospital	27 Aug. 2003	✔	11 Sep. 2003
Kitaya Holdings Pty Ltd	4 Sep. 2003	✔	22 Sep. 2003
Kooweerup Regional Health Service	10 Sep. 2003	✔	18 Sep. 2003
Kyabram and District Memorial Community Hospital	22 Sep. 2003	✔	25 Sep. 2003
Kyneton District Health Service	17 Sep. 2003	✔	18 Sep. 2003
Latrobe Regional Hospital	18 Sep. 2003	✔	22 Sep. 2003

HUMAN SERVICES - *continued*

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
Lorne Community Hospital	15 Sep. 2003	✔	18 Sep. 2003
Maldon Hospital	17 Sep. 2003	✔	17 Sep. 2003
Mallee Track Health and Community Service	30 Sep. 2003	✔	30 Sep. 2003
Manangatang and District Hospital	22 Sep. 2003	✔	22 Sep. 2003
Mansfield District Hospital	27 Oct. 2003	✔	30 Oct. 2003
Maryborough District Health Service	17 Sep. 2003	✔	18 Sep. 2003
McIvor Health and Community Services	18 Sep. 2003	✔	18 Sep. 2003
Mercy Public Hospitals Inc.	15 Sep. 2003	Qualified	16 Sep. 2003
Reason for qualification: *Failure to consolidate a "controlled" entity.*			
Mildura Base Hospital	30 Jun. 2003	✔	1 Jul. 2003
Moyne Health Services	5 Sep. 2003	✔	11 Sep. 2003
Mt Alexander Hospital	17 Sep. 2003	✔	19 Sep. 2003
Nathalia District Hospital	18 Sep. 2003	✔	18 Sep. 2003
Northeast Health Wangaratta *(b)*	24 Sep. 2003	Qualified	3 Oct. 2003
Reason for qualification: *Inappropriate disclosure of non-reciprocal grants.*			
Northern Health	15 Oct. 2003	✔	20 Oct. 2003
Numurkah District Health Service	18 Sep. 2003	✔	26 Sep. 2003
O'Connell Family Centre (Grey Sisters) Inc.	15 Sep. 2003	✔	16 Sep. 2003
Omeo District Hospital	23 Sep. 2003	Qualified	24 Sep. 2003
Reason for qualification: *Inappropriate disclosure of non-reciprocal grants.*			
Orbost Regional Health	1 Oct. 2003	✔	6 Oct. 2003
Otway Health and Community Services	16 Sep. 2003	✔	18 Sep. 2003
Peninsula Health	12 Sep. 2003	✔	16 Sep. 2003
Peter MacCallum Cancer Institute	9 Sep. 2003	✔	9 Sep. 2003
Portland and District Hospital	15 Sep. 2003	✔	19 Sep. 2003
Queen Elizabeth Centre	16 Aug. 2003	Qualified	11 Sep. 2003
Reason for qualification: *Failure to consolidate a "controlled" entity.*			
Robinvale District Health Services	16 Sep. 2003	✔	18 Sep. 2003
Rochester and Elmore District Health Service	18 Sep. 2003	✔	22 Sep. 2003
Royal Victorian Eye and Ear Hospital	9 Sep. 2003	✔	15 Sep. 2003
Seymour District Memorial Hospital	17 Sep. 2003	✔	19 Sep. 2003

HUMAN SERVICES - *continued*

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
South Gippsland Hospital	4 Sep. 2003	✔	10 Sep. 2003
South West Health Care	9 Sep. 2003	✔	10 Sep. 2003
Southern Health	18 Sep. 2003	✔	22 Sep. 2003
St Georges Health Service Limited	18 Sep. 2003	✔	18 Sep. 2003
St Vincent's Hospital (Melbourne) Limited	18 Sep. 2003	Qualified	23 Sep. 2003
Reason for qualification: *Inappropriate recognition of certain debtors.*			
Stawell Regional Health	18 Sep. 2003	✔	22 Sep. 2003
Swan Hill District Hospital	18 Sep. 2003	✔	22 Sep. 2003
Tallangatta Health Service	29 Sep. 2003	✔	3 Oct. 2003
Terang and Mortlake Health Service	4 Sep. 2003	✔	15 Sep. 2003
Timboon and District Healthcare Service	29 Aug. 2003	✔	11 Sep. 2003
Tweddle Child and Family Health Service	16 Sep. 2003	✔	16 Sep. 2003
Upper Murray Health and Community Services	26 Sep. 2003	✔	3 Oct. 2003
Western District Health Service	28 Aug. 2003	✔	11 Sep. 2003
West Gippsland Healthcare Group	15 Sep. 2003	✔	19 Sep. 2003
Western Health	21 Oct. 2003	✔	27 Oct. 2003
West Wimmera Health Service	1 Oct. 2003	✔	2 Oct. 2003
Wimmera Health Care Group	18 Sep. 2003	✔	22 Sep. 2003
Wodonga Regional Health Service	17 Sep. 2003	Qualified	22 Sep. 2003
Reason for qualification: *Inappropriate disclosure of non-reciprocal grants.*			
Women's and Children's Health	29 Aug. 2003	✔	18 Sep. 2003
Yarram and District Health Service	25 Sep. 2003	✔	8 Oct. 2003
Yarrawonga District Health Service	23 Sep. 2003	✔	3 Oct. 2003
Yea and District Memorial Hospital	18 Sep. 2003	✔	19 Sep. 2003

HUMAN SERVICES *- continued*

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – WITH OTHER BALANCE DATES			
Calvary Health Care Bethlehem (financial year ended 26 June 2003)	25 Sep.2003	✔	3 Oct. 2003
Mildura Base Hospital (financial year ended 30 June 2002)	28 Mar. 2003	✔	10 Jun. 2003
Wyndham Cemeteries Trust (financial year ended 31 December 2002)	10 Jun. 2003	✔	18 Jun. 2003

INCOMPLETE AUDITS – AS AT 31 OCTOBER 2003	
Alexandra and District Ambulance Service	*Audited financial statements yet to be finalised*
Melbourne Health	*Audited financial statements yet to be finalised*
Rural Northwest Health (financial year ended 30 June 2003)	*Audited financial statements yet to be finalised.*

(a) Formerly the Wonthaggi and District Hospital.
(b) Formerly the Wangaratta District Base Hospital.

INNOVATION, INDUSTRY AND REGIONAL DEVELOPMENT

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
Department of Innovation, Industry and Regional Development	10 Oct. 2003	✔	17 Oct. 2003
INNOVATION, STATE AND REGIONAL DEVELOPMENT			
Overseas Projects Corporation of Victoria Ltd	27 Oct. 2003	✔	31 Oct. 2003
Victorian Medical Consortium Pty Ltd	17 Sep. 2003	✔	29 Sep. 2003
Federation Square Management Pty Ltd	31 Oct. 2003	✔	31 Oct. 2003
Prince Henry's Institute of Medical Research *(a)*	19 Sep. 2003	✔	26 Sep. 2003
TOURISM			
Australian Grand Prix Corporation	22 Sep. 2003	✔	22 Sep. 2003
Emerald Tourist Railway Board	15 Sep. 2003	✔	19 Sep. 2003
Melbourne Convention and Exhibition Trust	31 Aug. 2003	✔	15 Sep. 2003
Tourism Victoria	23 Sep. 2003	✔	24 Sep. 2003
INCOMPLETE AUDITS – AS AT 31 OCTOBER 2003			
Victoria Trade and Investment Office Pty Ltd (financial year ended 30 June 2003)	*Awaiting audited financial statements.*		

(a) Financial Report for the 18 month period ended 30 June 2003.

INFRASTRUCTURE

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
Department of Infrastructure	24 Oct. 2003	✔	27 Oct. 2003
ENERGY INDUSTRIES			
Network Tariff Rebate Trust Fund	18 Aug. 2003	✔	21 Aug. 2003
Office of Gas Safety	19 Sep. 2003	✔	19 Sep. 2003
Office of Chief Electrical Inspector	28 Aug. 2003	✔	29 Aug. 2003
Special Power Payment Trust	18 Aug. 2003	✔	21 Aug. 2003
Victoria Energy Networks Corporation	18 Aug. 2003	✔	21 Aug. 2003
TRANSPORT			
Hastings Port (Holding) Corporation	19 Sep. 2003	✔	24 Sep. 2003
Melbourne Port Corporation	25 Sep. 2003	✔	29 Sep. 2003
Public Transport Corporation	12 Sep. 2003	✔	17 Sep. 2003
Roads Corporation	26 Sep. 2003	✔	2 Oct. 2003
Rolling Stock Holdings Limited (Victoria) P/L	24 Oct. 2003	✔	27 Oct. 2003
Rolling Stock (Victoria – VL) P/L	24 Oct. 2003	✔	27 Oct. 2003
Rolling Stock (VL – 1) P/L	24 Oct. 2003	Qualified	27 Oct. 2003
Reason for qualification: *Prior year comparative balances had not previously been audited.*			
Rolling Stock (VL – 2) P/L	24 Oct. 2003	Qualified	27 Oct. 2003
Reason for qualification: *Prior year comparative balances had not previously been audited.*			
Rolling Stock (VL – 3) P/L	24 Oct. 2003	Qualified	27 Oct. 2003
Reason for qualification: *Prior year comparative balances had not previously been audited.*			
Spencer Street Station Authority	23 Sep. 2003	✔	24 Sep. 2003
Victorian Channels Authority	29 Aug. 2003	✔	10 Sep. 2003
Victorian Rail Track	10 Oct. 2003	✔	27 Oct. 2003

INCOMPLETE AUDITS – AS AT 31 OCTOBER 2003	
Docklands Authority *(a)*	*Awaiting audited financial statements.*
Public Transport Ticketing Body *(b)*	*Financial reporting Period extended*
Urban and Regional Land Corporation *(a)*	*Awaiting audited financial statements.*
Victorian Rail Services Pty Ltd (Financial year ended 30 June 2003)	*Awaiting audited financial statements.*

(a) Pursuant to determinations issued by the Minister for Finance under the provisions of the *Financial Management Act* 1994, the final financial year for the Docklands Authority and the Urban and Regional Land Corporation was a 13 month period ending 31 July 2003. These entities ceased to operate on that date and their responsibilities have been assigned to the newly created Victorian Urban Development Authority.

(b) The entity was established in June 2003. At the date of preparation of this report, the entity had sought approval for its first reporting period to cover the 13 months to June 2004.

JUSTICE

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
Department of Justice	8 Oct. 2003	✔	10 Oct. 2003
ATTORNEY-GENERAL			
Equal Opportunity Commission	10 Sep. 2003	✔	10 Sep. 2003
Legal Practice Board	28 Aug. 2003	✔	1 Sep. 2003
Legal Practitioners Liability Committee	16 Sep. 2003	✔	17 Sep. 2003
Office of Public Prosecutions	9 Sep. 2003	✔	10 Sep. 2003
Office of the Legal Ombudsman	15 Aug. 2003	✔	18 Aug. 2003
Office of the Public Advocate	10 Sep. 2003	✔	10 Sep. 2003
Office of the Victorian Privacy Commissioner	14 Oct. 2003	✔	14 Oct. 2003
Senior Master of the Supreme Court	25 Aug. 2003	✔	28 Aug. 2003
Victorian Electoral Commission	12 Sep. 2003	✔	15 Sep. 2003
Victorian Institute of Forensic Medicine	9 Sep. 2003	✔	12 Sep. 2003
Victoria Legal Aid	8 Aug. 2003	✔	12 Aug. 2003
Victorian Law Reform Commission	12 Sep. 2003	✔	16 Sep. 2003
CONSUMER AFFAIRS			
Domestic Building (HIH) Indemnity Fund	20 Sep. 2003	✔	29 Sep. 2003
Residential Tenancies Bond Authority	15 Sep. 2003	✔	1 Oct. 2003
GAMING AND RACING			
Footy Consortium Pty Ltd	25 Sep. 2003	✔	26 Sep. 2003
Gambling Research Panel	9 Oct. 2003	✔	17 Oct. 2003
Tattersall's Club Keno Pty Ltd	25 Sep. 2003	✔	26 Sep. 2003
Tattersall's Gaming Pty Ltd	25 Sep. 2003	✔	26 Sep. 2003
Tattersall's Sweeps Pty Ltd	25 Sep. 2003	✔	26 Sep. 2003
Victorian Casino and Gaming Authority	26 Aug. 2003	✔	26 Aug. 2003
Greyhound Racing Victoria	16 Sep. 2003	✔	17 Sep. 2003
Harness Racing Victoria	10 Sep. 2003	✔	15 Sep. 2003

JUSTICE- *continued*

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
POLICE AND EMERGENCY SERVICES			
Australasian Police Multicultural Advisory Bureau	12 Sep. 2003	✔	17 Sep. 2003
Country Fire Authority	27 Aug. 2003	✔	1 Sep. 2003
Emergency Communications Victoria	18 Aug. 2003	✔	21 Aug. 2003
Metropolitan Fire and Emergency Services Board	11 Sep. 2003	✔	16 Sep. 2003
National Institute of Forensic Science	12 Sep. 2003	✔	17 Sep. 2003
Office of the Chief Commissioner of Police	12 Sep. 2003	✔	16 Sep. 2003
The Fire Services College	3 Sep. 2003	✔	9 Oct. 2003

SUSTAINABILITY AND ENVIRONMENT

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
Department of Sustainability and Environment	13 Oct. 2003	✔	13 Oct. 2003
PLANNING			
Architects' Registration Board of Victoria	12 Aug. 2003	✔	2 Sep. 2003
Building Commission	5 Aug. 2003	✔	5 Aug. 2003
Heritage Council	16 Sep. 2003	✔	17 Sep. 2003
Plumbing Industry Commission	23 Sep. 2003	✔	24 Sep. 2003
ENVIRONMENT AND WATER			
Alpine Resort Co-ordinating Council	20 Aug. 2003	✔	18 Sep. 2003
Barwon Regional Waste Management Group	26 Sep. 2003	✔	30 Sep. 2003
Barwon Region Water Authority	20 Aug. 2003	✔	3 Sep. 2003
Calder Regional Waste Management Group	29 Sep. 2003	✔	30 Sep. 2003
Casey's Weir and Major Creek Rural Water Authority	28 Aug. 2003	✔	28 Aug. 2003
Audit report contained an "emphasis of matter": *There was inherent uncertainty as to whether the Authority would continue to exist as a separate entity.*			
Central Gippsland Region Water Authority	29 Aug. 2003	✔	10 Sep. 2003
Central Highlands Region Timber Pty Ltd	23 Sep. 2003	✔	23 Oct. 2003
Central Highlands Region Water Authority	23 Sep. 2003	✔	3 Oct. 2003
Central Murray Regional Waste Management Group	4 Aug. 2003	✔	23 Sep. 2003
City West Water Ltd	26 Aug. 2003	✔	26 Aug. 2003
Coliban Region Water Authority	25 Sep. 2003	✔	25 Sep. 2003
Corangamite Catchment Management Authority	12 Sep. 2003	✔	12 Sep. 2003
Desert Fringe Regional Waste Management Group	28 Aug. 2003	✔	22 Sep. 2003
Eastern Regional Waste Management Group	12 Sep. 2003	✔	16 Sep. 2003
East Gippsland Catchment Management Authority	9 Sep. 2003	✔	12 Sep. 2003
East Gippsland Region Water Authority	27 Aug. 2003	✔	3 Sep. 2003
Eco Recycle Victoria	21 Aug. 2003	✔	21 Aug. 2003
Environment Protection Authority	30 Sep. 2003	✔	30 Sep. 2003
Gippsland and Southern Rural Water Authority	22 Aug. 2003	✔	10 Sep. 2003
Gippsland Regional Waste Management Group	9 Sep. 2003	✔	10 Sep. 2003
Glenelg Region Water Authority	8 Aug. 2003	✔	1 Sep. 2003
Glenelg-Hopkins Catchment Management Authority	10 Sep. 2003	✔	12 Sep. 2003

SUSTAINABILITY AND ENVIRONMENT - *continued*

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
Goulburn Broken Catchment Management Authority	5 Sep. 2003	✔	22 Sep. 2003
Goulburn-Murray Rural Water Authority	21 Aug. 2003	✔	21 Aug. 2003
Goulburn Valley Region Water Authority	1 Sep. 2003	✔	16 Sep. 2003
Goulburn Valley Regional Waste Management Group	17 Sep. 2003	✔	3 Oct. 2003
Grampians Region Water Authority	18 Sep. 2003	✔	25 Sep. 2003
Grampians Regional Waste Management Group	24 Sep. 2003	✔	25 Sep. 2003
Highlands Regional Waste Management Group	25 Sep. 2003	✔	29 Sep. 2003
Lower Murray Region Water Authority	18 Sep. 2003	✔	25 Sep. 2003
Mallee Catchment Management Authority	24 Sep. 2003	✔	29 Sep. 2003
Melbourne Water Corporation	22 Aug. 2003	✔	22 Aug. 2003
Mildura Regional Waste Management Group	2 Oct. 2003	✔	9 Oct. 2003
Mornington Peninsula Regional Waste Management Group	19 Sep. 2003	✔	3 Oct. 2003
North Central Catchment Management Authority	1 Sep. 2003	✔	16 Sep. 2003
North East Catchment Management Authority	19 Sep. 2003	✔	29 Sep. 2003
North East Region Water Authority	8 Sep. 2003	✔	18 Sep. 2003
North East Regional Waste Management Group	15 Oct. 2003	✔	16 Oct. 2003
Northern Regional Waste Management Group	9 Oct. 2003	✔	13 Oct. 2003
Parks Victoria	22 Aug. 2003	✔	22 Aug. 2003
Phillip Island Nature Park Board of Management	30 Sep. 2003	✔	1 Oct. 2003
Portland Coast Region Water Authority	4 Sep. 2003	✔	9 Sep. 2003
Port Phillip and Westernport CMA	9 Oct. 2003	✔	10 Oct. 2003
Royal Botanic Gardens Board	19 Aug. 2003	✔	29 Aug. 2003
Shrine of Remembrance Trustees	30 Sep. 2003	✔	30 Sep. 2003
South East Water Limited	25 Aug. 2003	✔	25 Aug. 2003
South Eastern Regional Waste Management Group	21 Aug. 2003	✔	16 Sep. 2003
South Gippsland Region Water Authority	28 Aug. 2003	✔	12 Sep. 2003
South West Water Authority	4 Sep. 2003	✔	8 Sep. 2003
South Western Regional Waste Management Group	6 Oct. 2003	✔	7 Oct. 2003

SUSTAINABILITY AND ENVIRONMENT *- continued*

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
Sunraysia Rural Water Authority	25 Sep. 2003	✔	3 Oct. 2003
Surveyors Board of Victoria	18 Sep. 2003	✔	19 Sep. 2003
Sustainable Energy Authority Victoria	2 Oct. 2003	✔	3 Oct. 2003
Trust for Nature (Victoria)	5 Sep. 2003	✔	22 Sep. 2003
Victorian Plantations Corporation	12 Sep. 2003	✔	15 Sep. 2003
West Gippsland Catchment Management Authority	19 Sep. 2003	✔	26 Sep. 2003
Western Region Water Authority	29 Aug. 2003	✔	1 Sep. 2003
Western Regional Waste Management Group	9 Sep. 2003	✔	9 Sep. 2003
Westernport Region Water Authority	17 Sep. 2003	✔	25 Sep. 2003
Wimmera Catchment Management Authority	12 Sep. 2003	✔	22 Sep. 2003
Wimmera Mallee Rural Water Authority	3 Sep. 2003	✔	9 Sep. 2003
Yarra Bend Park Trust	2 Oct. 2003	✔	7 Oct. 2003
Yarra Valley Water Limited	20 Aug. 2003	✔	20 Aug. 2003
Zoological Parks and Gardens Board	5 Sep. 2003	✔	16 Sep. 2003

INCOMPLETE AUDITS – AS AT 31 OCTOBER 2003	
Victorian Dairy Industry Authority *(a)* (period 1 July 2000 to 29 September 2000)	*Audited financial statements yet to be finalised.*
First Mildura Irrigation Trust	*Audited financial statements yet to be finalised.*
Smart Water Fund	*Audited financial statements yet to be finalised.*

(a) Authority ceased operations on 29 September 2000.

PRIMARY INDUSTRIES

Entity	Financial statements signed	Clear opinion issued	Auditor-General's report signed
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
Department of Primary Industries	26 Sep. 2003	✔	26 Sep. 2003
AGRICULTURE			
Agriculture Victoria Services Pty Ltd	10 Sep. 2003	✔	19 Sep. 2003
Australian Food Industry Science Centre	6 Oct. 2003	✔	9 Oct. 2003
Dairy Food Safety Victoria	27 Aug. 2003	✔	2 Oct. 2003
Food Science Australia	6 Oct. 2003	✔	9 Oct. 2003
Greater Victoria Wine Grape Industry Development Committee	19 Aug. 2003	✔	6 Oct. 2003
Melbourne Market Authority	22 Sep. 2003	✔	22 Sep. 2003
Murray Valley Citrus Marketing	30 Sep. 2003	✔	6 Oct. 2003
Murray Valley Wine Grape Industry Development Committee	12 Sep. 2003	✔	23 Sep. 2003
Phytogene Pty Ltd	5 Sep. 2003	✔	17 Sep. 2003
Victorian Meat Authority	14 Aug. 2003	✔	25 Aug. 2003
Veterinary Practitioners Registration Board	17 Sep. 2003	✔	17 Sep. 2003
Victorian Strawberry Industry Development Committee	25 Sep. 2003	✔	26 Sep.2003

INCOMPLETE AUDITS – AS AT 31 OCTOBER 2003	
Northern Victorian Fresh Tomato Industry Development Committee	*Audited financial statements yet to be finalised.*

PREMIER AND CABINET

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
Department of Premier and Cabinet	19 Sep. 2003	✔	22 Sep. 2003
ARTS			
Australian Centre for the Moving Image	6 Oct. 2003	✔	20 Oct. 2003
Council of Trustees of the National Gallery of Victoria	22 Sep. 2003	✔	22 Sep. 2003
Film Victoria	23 Sep. 2003	✔	26 Sep. 2003
Geelong Performing Arts Centre Trust	22 Sep. 2003	✔	22 Sep. 2003
Library Board of Victoria	14 Aug. 2003	✔	22 Sep. 2003
Museums Board of Victoria	8 Sep. 2003	✔	22 Sep. 2003
State Library of Victoria Foundation	14 Aug. 2003	✔	22 Sep. 2003
Victorian Arts Centre Trust	30 Sep. 2003	✔	2 Oct. 2003
PREMIER			
Office of the Ombudsman	8 Sep. 2003	✔	10 Sep. 2003
Office of Public Employment	22 Sep. 2003	✔	22 Sep. 2003

TREASURY AND FINANCE

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
Department of Treasury and Finance	17 Oct. 2003	✔	21 Oct. 2003
FINANCE			
Emergency Services Superannuation Scheme	5 Sep. 2003	✔	5 Sep. 2003
Government Superannuation Office	16 Sep. 2003	✔	16 Sep. 2003
Parliamentary Contributory Superannuation Fund	9 Oct. 2003	✔	10 Oct. 2003
Essential Services Commission	29 Sep. 2003	✔	9 Oct. 2003
State Superannuation Fund	16 Sep. 2003	✔	16 Sep. 2003
Victorian Managed Insurance Authority	22 Aug. 2003	✔	29 Aug. 2003
TREASURER			
Gas Release Co. Pty Ltd	23 Jul. 2003	✔	25 Jul. 2003
Gascor Holdings No. 1 Pty Ltd *(a)*	27 Aug. 2003	✔	29 Aug. 2003
Gascor Holdings No. 2 Pty Ltd *(a)*	27 Aug. 2003	✔	29 Aug. 2003
Gascor Holdings No. 3 Pty Ltd *(a)*	27 Aug. 2003	✔	29 Aug. 2003
Gascor EPL Pty Ltd *(a)*	27 Aug. 2003	✔	29 Aug. 2003
Gascor IEPL Pty Ltd *(a)*	27 Aug. 2003	✔	29 Aug. 2003
Gascor KEPL Pty Ltd *(a)*	27 Aug. 2003	✔	29 Aug. 2003
Gascor MAPL Pty Ltd *(a)*	27 Aug. 2003	✔	29 Aug. 2003
Gascor MGPL Pty Ltd *(a)*	27 Aug. 2003	✔	29 Aug. 2003
Gascor Pty Ltd	23 Jul. 2003	✔	25 Jul. 2003
Gascor SAPL Pty Ltd *(a)*	27 Aug. 2003	✔	29 Aug. 2003
Gascor SNPL Pty Ltd *(a)*	27 Aug. 2003	✔	29 Aug. 2003
Gascor (T No.1) Pty Ltd *(a)*	27 Aug. 2003	✔	29 Aug. 2003
Gascor (TH) Pty Ltd *(a)*	27 Aug. 2003	✔	29 Aug. 2003
Gascor WAPL Pty Ltd *(a)*	27 Aug. 2003	✔	29 Aug. 2003
Gascor WPL Pty Ltd *(a)*	27 Aug. 2003	✔	29 Aug. 2003
Industry Supervision Fund	19 Sep. 2003	✔	22 Sep. 2003
Land Aggregation Program Trust Fund	19 Aug. 2003	✔	19 Aug. 2003
Paragon Warehouse Trust No.1	18 Sep. 2003	✔	18 Sep. 2003
Paragon Warehouse Trust No. 2	18 Sep. 2003	✔	18 Sep. 2003
Rural Finance Corporation	19 Aug. 2003	✔	19 Aug. 2003
South Eastern Medical Complex Limited	9 Oct. 2003	✔	9 Oct. 2003
State Electricity Commission of Victoria	18 Sep. 2003	✔	18 Sep. 2003
State Trustees Limited	18 Sep. 2003	✔	18 Sep. 2003
State Trustees Common Fund No. 1	18 Sep. 2003	✔	18 Sep. 2003
State Trustees Common Fund No. 2	18 Sep. 2003	✔	18 Sep. 2003

TREASURY AND FINANCE - *continued*

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
TREASURER			
State Trustees Common Fund No. 3	18 Sep. 2003	✔	18 Sep. 2003
State Trustees Common Fund No. 4	18 Sep. 2003	✔	18 Sep. 2003
State Trustees Common Fund No. 5	18 Sep. 2003	✔	18 Sep. 2003
State Trustees Common Fund No. 6	18 Sep. 2003	✔	18 Sep. 2003
State Trustees Common Fund No. 10	18 Sep. 2003	✔	18 Sep. 2003
State Trustees Premium Cash Fund	18 Sep. 2003	✔	18 Sep. 2003
State Trustees Premium Diversified Fund	18 Sep. 2003	✔	18 Sep. 2003
State Trustees Premium Equity Fund	18 Sep. 2003	✔	18 Sep. 2003
State Trustees Premium Fixed Interest Fund	18 Sep. 2003	✔	18 Sep. 2003
State Trustees Premium International Fund	18 Sep. 2003	✔	18 Sep. 2003
State Trustees Premium Mortgage Fund	18 Sep. 2003	✔	18 Sep. 2003
State Trustees Premium Property Fund	18 Sep. 2003	✔	18 Sep. 2003
STL Financial Services Limited	18 Sep. 2003	✔	18 Sep. 2003
Treasury Corporation of Victoria	10 Sep. 2003	✔	10 Sep. 2003
Vicfleet Pty Ltd	31 Jul. 2003	✔	2 Oct. 2003
Victoria 2003 Bushfire Recovery Fund	22 Sep. 2003	✔	24 Sep. 2003
Victorian Funds Management Corporation	28 Aug. 2003	✔	28 Aug. 2003
VFM Australian Equities Trust	28 Aug. 2003	✔	28 Aug. 2003
VFM Australian Fixed Interest Trust	28 Aug. 2003	✔	28 Aug. 2003
VFM Global Bond Trust	28 Aug. 2003	✔	28 Aug. 2003
VFM Global Small Companies Trust	28 Aug. 2003	✔	28 Aug. 2003
VFM Hedged International Equities Trust	28 Aug. 2003	✔	28 Aug. 2003
VFM Indexed Bonds Trust	28 Aug. 2003	✔	28 Aug. 2003
VFM International Equities Trust	28 Aug. 2003	✔	28 Aug. 2003
VFM Short Term Money Market Trust	28 Aug. 2003	✔	28 Aug. 2003

TREASURY AND FINANCE - *continued*

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS – 30 JUNE 2003 BALANCE DATES			
WORKCOVER			
Accident Compensation and Conciliation Service	27 Aug. 2003	✔	29 Aug. 2003
TAC Law Pty Ltd	29 Aug. 2003	✔	4 Sep. 2003
Transport Accident Commission	29 Aug. 2003	✔	29 Aug. 2003
Victorian Trauma Foundation	29 Aug. 2003	✔	4 Sep. 2003
Victorian Trauma Foundation Pty Ltd	29 Aug. 2003	✔	4 Sep. 2003
Victorian WorkCover Authority	27 Aug. 2003	✔	29 Aug. 2003

INCOMPLETE AUDITS – AS AT 31 OCTOBER 2003	
Arada Trust (financial year ended 30 June 2002)	*Audited financial statements yet to be finalised.*
Roslin Pty Ltd *(b)* (financial year ended 30 June 2001)	*Audited financial statements yet to be finalised.*

(a) "Shell companies" of previous gas industry entities.

(b) Final audit.

VICTORIAN COMMUNITIES
(excluding local government)

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
COMPLETED AUDITS			
Department for Victorian Communities	22 Oct. 2003	✔	27 Oct. 2003
COMMONWEALTH GAMES AND SPORT & RECREATION			
Melbourne and Olympic Parks Trust	18 Aug. 2003	Qualified	22 Aug. 2003
Reason for qualification: *Incorrect recognition of an expense and an associated liability.*			
Melbourne 2006 Commonwealth Games	15 Aug. 2003	✔	15 Aug. 2003
State Sport Centres Trust	17 Sep. 2003	✔	17 Sep. 2003
Victorian Institute of Sport Ltd	20 Aug. 2003	✔	29 Aug. 2003
Victorian Institute of Sport Trust	20 Aug. 2003	✔	29 Aug. 2003
MULTICULTURAL AFFAIRS			
VITS Languagelink	5 Sep. 2003	✔	8 Sep. 2003
WOMEN'S AFFAIRS			
Queen Victoria Women's Centre Trust	21 Aug. 2003	✔	2 Sep. 2003

INCOMPLETE AUDITS – AS AT 31 OCTOBER 2003	
Melbourne 2002 World Masters Games Limited (period 1 July 2001 to 30 November 2002)	*Audited financial statements yet to be finalised.*

LOCAL GOVERNMENT

Entity	Financial statements signed	Clear opinion issued		Auditor-General's report signed
		Financial statements	Performance statement	
COMPLETED AUDITS				
MUNICIPAL COUNCILS AND ASSOCIATED COMPANIES				
Alpine Shire Council	28 Oct. 2003	✔	✔	29 Oct. 2003
Ararat Rural City Council	1 Sep. 2003	✔	✔	11 Sep. 2003
Ballarat City Council	17 Sep. 2003	✔	✔	29 Sep. 2003
Banyule City Council	8 Sep. 2003	✔	✔	12 Sep. 2003
Bass Coast Shire Council	10 Sep. 2003	✔	✔	17 Sep. 2003
Baw Baw Shire Council	8 Sep. 2003	✔	✔	11 Sep. 2003
Bayside City Council	22 Sep. 2003	✔	✔	23 Sep. 2003
Benalla Rural City Council (b)	24 Sep. 2003	✔	✔	25 Sep. 2003
Boroondara City Council	2 Sep. 2003	✔	✔	8 Sep. 2003
Borough of Queenscliffe	8 Sep. 2003	✔	✔	11 Sep. 2003
Brimbank City Council	15 Sep. 2003	✔	✔	22 Sep. 2003
Campaspe Shire Council	9 Sep. 2003	✔	✔	15 Sep. 2003
Cardinia Shire Council	8 Sep. 2003	✔	✔	11 Sep. 2003
Casey City Council	18 Sep. 2003	✔	✔	19 Sep. 2003
Central Goldfields Shire Council	12 Sep. 2003	✔	✔	17 Sep. 2003
CityWide Service Solutions Pty Ltd	16 Sep. 2003	✔	n/a	17 Sep. 2003
Colac-Otway Shire Council	3 Sep. 2003	✔	✔	17 Sep. 2003
Corangamite Shire Council	9 Sep. 2003	✔	✔	15 Sep. 2003
Darebin City Council	29 Sep. 2003	✔	✔	29 Sep. 2003
East Gippsland Shire Council	10 Sep. 2003	✔	✔	16 Sep. 2003
Frankston City Council	10 Sep. 2003	✔	✔	12 Sep. 2003
Gannawarra Shire Council	24 Sep. 2003	✔	✔	26 Sep. 2003
Glen Eira City Council	9 Sep. 2003	✔	✔	10 Sep. 2003
Glenelg Shire Council	26 Aug. 2003	✔	Qualified	15 Sep. 2003
***Reason for qualification**: Business plan for 2002-03 did not include performance targets for 8 performance measures.*				
Golden Plains Shire Council	22 Sep. 2003	✔	✔	23 Sep. 2003
Greater Bendigo City Council	18 Sep. 2003	✔	✔	25 Sep. 2003
Greater Dandenong City Council	15 Sep. 2003	✔	✔	17 Sep. 2003
Greater Geelong City Council	16 Sep. 2003	✔	✔	19 Sep. 2003
Greater Shepparton City Council	24 Sep. 2003	✔	✔	25 Sep. 2003
Hepburn Shire Council	23 Sep. 2003	✔	✔	26 Sep. 2003

LOCAL GOVERNMENT - *continued*

Entity	*Financial statements signed*	*Clear opinion issued*		*Auditor-General's report signed*
		Financial statements	*Performance statement*	
COMPLETED AUDITS				
MUNICIPAL COUNCILS AND ASSOCIATED COMPANIES				
Hindmarsh Shire Council	29 Sep. 2003	✔	✔	29 Sep. 2003
Hobsons Bay City Council	23 Sep. 2003	✔	✔	24 Sep. 2003
Horsham Rural City Council	9 Sep. 2003	✔	Qualified	15 Sep. 2003
Reason for qualification *Corporate plan for 2002-2005 did not include a business plan for 2002-03 or performance targets and measures in relation to 2002-03.*				
Hume City Council	8 Sep. 2003	✔	✔	18 Sep. 2003
Indigo Shire Council	15 Sep. 2003	✔	✔	19 Sep. 2003
Kingston City Council	25 Sep. 2003	✔	✔	25 Sep. 2003
Knox City Council	23 Sep. 2003	✔	✔	24 Sep. 2003
Latrobe City Council	22 Sep. 2003	✔	✔	25 Sep. 2003
Loddon Shire Council	16 Sep. 2003	✔	✔	22 Sep. 2003
Macedon Ranges Shire Council	17 Sep. 2003	✔	✔	22 Sep. 2003
Manningham City Council	23 Sep. 2003	✔	✔	25 Sep. 2003
Maribyrnong City Council	4 Sep. 2003	✔	✔	5 Sep. 2003
Maroondah City Council	26 Sep. 2003	✔	✔	26 Sep. 2003
Melbourne City Council	25 Sep. 2003	✔	✔	25 Sep. 2003
Mansfield Shire Council *(b)*	16 Sep. 2003	✔	✔	18 Sep. 2003
Melbourne Wholesale Fish Market Pty Ltd	18 Sep. 2003	✔	n/a	19 Sep. 2003
Melton Shire Council	11 Sep. 2003	✔	✔	12 Sep. 2003
Mildura Rural City Council	23 Sep. 2003	✔	✔	25 Sep. 2003
Mitchell Shire Council	11 Sep. 2003	✔	✔	15 Sep. 2003
Moira Shire Council	22 Sep. 2003	✔	✔	25 Sep. 2003
Monash City Council	24 Sep. 2003	✔	✔	25 Sep. 2003
Moonee Valley City Council	19 Sep. 2003	✔	✔	19 Sep. 2003
Moorabool Shire Council	24 Sep. 2003	✔	✔	26 Sep. 2003
Moreland City Council	22 Sep. 2003	✔	✔	23 Sep. 2003
Mornington Peninsula Shire Council	25 Sep. 2003	✔	✔	26 Sep. 2003
Mount Alexander Shire Council	10 Sep. 2003	✔	✔	12 Sep. 2003
Moyne Shire Council	9 Sep. 2003	✔	✔	12 Sep. 2003
Murrundindi Shire Council	16 Sep. 2003	✔	✔	18 Sep. 2003
Nillumbik Shire Council	25 Sep. 2003	✔	✔	26 Sep. 2003

LOCAL GOVERNMENT - *continued*

Entity	*Financial statements signed*	*Clear opinion issued*		*Auditor-General's report signed*
		Financial statements	*Performance statement*	
COMPLETED AUDITS				
MUNICIPAL COUNCILS AND ASSOCIATED COMPANIES				
Northern Grampians Shire Council	9 Sep. 2003	✔	✔	15 Sep. 2003
Port Phillip City Council	22 Sep. 2003	✔	✔	24 Sep. 2003
Prahran Market Pty Ltd	18 Sep. 2003	✔	n/a	29 Sep. 2003
Pyrenees Shire Council	19 Aug. 2003	✔	✔	29 Sep. 2003
Queen Victoria Market Pty Ltd	18 Sep. 2003	✔	n/a	19 Sep. 2003
Regent Management Company Pty Ltd	27 Oct. 2003	✔	n/a	31 Oct. 2003
South Gippsland Shire Council	10 Sep. 2003	✔	✔	17 Sep. 2003
Southern Grampians Shire Council	12 Sep. 2003	✔	✔	16 Sep. 2003
Stonnington City Council	15 Sep. 2003	✔	✔	17 Sep. 2003
Strathbogie Shire Council	16 Sep. 2003	✔	✔	18 Sep. 2003
Streetsahead Cleaning Services	15 Sep. 2003	✔	n/a	17 Sep. 2003
Surf Coast Shire Council	2 Sep. 2003	✔	Qualified	18 Sep. 2003
***Reason for qualification**: Business plan for 2002-03 did not include a substantial proportion of the performance measures and targets set out in Council's business plan.*				
Swan Hill Rural City Council	22 Sep. 2003	Qualified	✔	29 Sep. 2003
***Reason for qualification:** Failure to undertake condition assessments for a significant proportion of its infrastructure assets.*				
Towong Shire Council	12 Sep. 2003	✔	✔	19 Sep. 2003
Wangaratta Rural City Council	10 Sep. 2003	✔	✔	15 Sep. 2003
Warrnambool City Council	11 Sep. 2003	✔	✔	12 Sep. 2003
Wellington Shire Council	16 Sep. 2003	✔	✔	17 Sep. 2003
West Wimmera Shire Council	12 Sep. 2003	✔	✔	16 Sep. 2003
Whitehorse City Council	11 Sep. 2003	✔	✔	17 Sep. 2003
Whittlesea City Council	16 Sep. 2003	✔	✔	24 Sep. 2003
Wodonga Rural City Council	8 Sep. 2003	✔	Qualified	22 Sep. 2003
***Reason for qualification :** Results reported in respect of certain performance measures were not supported by sufficient and appropriate evidence.*				
Wyndham City Council	19 Sep. 2003	✔	✔	23 Sep. 2003
Yarra City Council	11 Sep. 2003	✔	✔	12 Sep. 2003
Yarra Ranges Shire Council	29 Aug. 2003	✔	✔	8 Sep. 2003
Yarriambiack Shire Council	8 Sep. 2003	✔	✔	18 Sep. 2003

LOCAL GOVERNMENT - *continued*

Entity	*Financial statements signed*	*Clear opinion issued*	*Auditor-General's report signed*
REGIONAL LIBRARY CORPORATIONS			
Casey - Cardinia Regional Library Corporation	3 Sep. 2003	✔	9 Sep. 2003
Central Highlands Regional Library Corporation	28 Aug. 2003	✔	12 Sep. 2003
Corangamite Regional Library Corporation	28 Aug. 2003	✔	29 Aug. 2003
Eastern Regional Library Corporation	18 Sep. 2003	✔	18 Sep. 2003
Geelong Regional Library Corporation	22 Sep. 2003	✔	22 Sep. 2003
Glenelg Regional Library Corporation	1 Sep. 2003	✔	15 Sep. 2003
Goulburn Valley Regional Library Corporation	29 Sep. 2003	✔	30 Sep. 2003
High Country Regional Library Corporation	9 Sep. 2003	✔	12 Sep. 2003
North Central Goldfields Regional Library Corporation	25 Sep. 2003	✔	30 Sep. 2003
West Gippsland Regional Library Corporation	9 Sep. 2003	✔	10 Sep. 2003
Whitehorse Manningham Regional Library Corporation	24 Sep. 2003	✔	24 Sep. 2003
Wimmera Regional Library Corporation	18 Sep. 2003	✔	24 Sep. 2003
Yarra Melbourne Regional Library Corporation	18 Sep. 2003	✔	24 Sep. 2003
Yarra Plenty Regional Library Corporation	9 Sep. 2003	✔	15 Sep. 2003

COMPLETED AUDITS-WITH OTHER BALANCE DATES

Delatite Shire Council (period 1 July 2002 to 27 October 2002)	28 Jan. 2003	✔	18 Feb.2003
Hume-Moonee Valley Regional Library Corporation (period 1 July 2002 to 31 December 2002)	12 Jun. 2003	✔	16 Jul. 2003

INCOMPLETE AUDITS – AS AT 31 OCTOBER 2003 *(a)*

Buloke Shire Council	*Audited financial statements yet to be finalised.*
New City Library Joint Venture	*Audited financial statements yet to be finalised.*
Sustainable Melbourne Trust Fund	*Audited financial statements yet to be finalised.*

(a) Financial period 30 June 2003, unless otherwise indicated.
(b) Financial Period 28 October 2002 to 30 June 2003.
n/a Not applicable, as agencies were not required by legislation to produce a performance statement.

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VICTORIA

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