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Management of Specific Purpose Funds by Public Health Services

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Auditing in the Public Interest

The Hon. Robert Smith MLC
President
Legislative Council
Parliament House
Melbourne

The Hon. Jenny Lindell MP
Speaker
Legislative Assembly
Parliament House
Melbourne

Dear Presiding Officers

Under the provisions of section 16AB of the *Audit Act 1994*, I transmit my report on
Management of Specific Purpose Funds by Public Health Services.

Yours faithfully



DDR PEARSON
Auditor-General

10 October 2007

Foreword

Specific Purpose Funds (SPFs) are moneys and property received by public health services from various sources and may include donations, bequests and research funding.

At the end of June 2007, public health services disclosed in excess of \$255 million in SPF reserves and more than \$45 million in trust funds in their financial statements. SPF reserves include amounts designated by management as being for a specific purpose and amounts contributed by external parties which are required to be spent for purposes specified by the providers. Our audit focused on these latter funds which are referred to as restricted SPFs.

Public health services are obliged to manage these funds in line with the conditions set by the providers. This is to meet their contractual obligations and accountability responsibilities under the *Financial Management Act 1994*.

We examined how well 4 public health services managed such funds during 2006-07, with overall satisfactory results. We found no evidence that conditions set by the providers of restricted SPFs had been breached.

Nevertheless, we identified several areas where health services could improve their financial management policies and internal controls over the management of SPFs. We also identified opportunities for the Department of Human Services (DHS) to enhance the guidance provided to the health service sector in this area.



DDR PEARSON
Auditor-General

10 October 2007

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1 Executive summary

1.1 Overview

Specific Purpose Funds (SPFs) are moneys and property received by public health services from various sources and may include donations, bequests and research funding.

Public health services disclosed in excess of \$255 million in SPF reserves and more than \$45 million in trust funds in their 30 June 2007 financial statements. Our audit covered 4 public health services which disclosed a total of around \$118 million in SPF reserves and \$28 million in trust funds in their financial statements.

There are two categories of SPFs. The first category comprises amounts designated by the management of a health service as being for a specific purpose (referred to as internally managed SPFs). The second involves amounts contributed by external parties which are required to be spent for purposes specified by the providers (referred to as restricted SPFs). Our audit focussed on restricted SPFs which must be spent for specific purposes, such as the construction of physical facilities, the creation of an ongoing prize or award and the conduct of research associated with pharmaceuticals.

To meet contractual obligations and satisfy the provisions of the *Financial Management Act 1994*, public health services should ensure that restricted SPFs are accounted for separately and used in accordance with the conditions set by the providers of those funds.

We examined how well 4 public health services managed such funds for the period May 2006 through April 2007. For the purposes of the audit, we included “trust funds”, which are predominantly comprised of aged care accommodation bonds, within our definition of restricted SPFs. Moneys held in trust also need to be separately accounted for and cannot be used to meet the general operating costs of health services.

We also reviewed the role played by the Department of Human Services (DHS) in providing guidance about SPFs.

Audit conclusions

We found that all 4 public health services examined had complied with the conditions set by the providers of restricted SPFs.

However, the interpretation and application of DHS guidelines for management of SPFs varied across health services. There was also variability in the management practices and systems in place for such funds across the 4 public health services.

We identified several areas where the health services could improve their financial management policies and internal controls over the management of SPFs, specifically:

- none of the health services had documented internal policies that were fully consistent with, and comprehensively addressed, all matters included in the guidelines for SPFs issued by DHS
- there were inconsistencies in the identification and classification of SPFs across and within the 4 health services
- only one of the health services examined provided monthly reports to the board of management which clearly distinguished whether cash and liquidity figures included restricted SPFs. Senior finance staff were, however, aware of the importance of monitoring the management of SPFs and were exercising adequate oversight of these funds.

We also identified opportunities for DHS to enhance the guidance provided to the health service sector in this area.

We found that aged care accommodation bonds held by the health services had been managed in accordance with the applicable requirements.

At 30 June 2007, restricted SPFs were adequately backed by sufficiently liquid assets and investments at each of the health services examined as part of this audit. Notwithstanding this, these liquid assets and investments are also required to address many other claims against them such as operating expenses and employee entitlements.

We also found that trust funds, including aged care accommodation bonds, were adequately backed by sufficiently liquid assets and investments at 30 June 2007. In the case of aged care accommodation bonds, there are prudential requirements imposed by Commonwealth legislation aimed at protecting these funds and ensuring that the bonds are able to be refunded as required. Our audit indicated that the 3 health services examined which held these bonds were complying with the prudential requirements.

We found that all the health services examined had appropriately reported on restricted SPFs in their annual financial statements.

We have included a self assessment checklist for public health services managing restricted SPFs in Appendix A. The purpose of this checklist is to serve as a quick reference guide on good management practices for the sector in this important area.

1.2 Recommendations

- Health services should review and update their internal policies and procedures to ensure they are consistent with the guidelines issued by DHS. **(Recommendation 3.1)**
- DHS should undertake a review of the guidelines in consultation with the sector and periodically review compliance. **(Recommendation 3.2)**
- Health services should review and update their internal policies and procedures to ensure they are comprehensive. **(Recommendation 4.1)**
- Health services should review their procedures for ensuring reliable classification of SPFs at the time they are received and recorded. **(Recommendation 4.2)**
- Health services should ensure that monthly reports to the board of management clearly identify the extent to which restricted SPFs are backed by sufficiently liquid assets and the impact of these funds on the overall liquidity position of the organisation. **(Recommendation 4.3)**

RESPONSE provided by the Secretary, Department of Human Services

Recommendations 3.1 and 4.1

The Department of Human Services accepts these recommendations. It is important that hospitals properly record and report on specific purpose funds, and documented internal policies and procedures are integral to the appropriate management of these funds.

Recommendation 3.2

The department partially accepts this recommendation. The department agrees that it is appropriate to undertake a review of the guidelines in consultation with the sector. The department sees compliance with the guidelines as a responsibility for hospitals and their boards of management.

Recommendation 4.2

The department accepts this recommendation. The department agrees that specific purpose funds should be reliably classified at the time they are received to ensure that they are appropriately reported and managed.

Recommendation 4.3

The department accepts this recommendation. Hospital boards of management should be regularly informed of the funds held for specific purposes and the extent to which they are backed by sufficiently liquid assets.

RESPONSE provided by Chief Executive Officer, Barwon Health

Overall we found the report to accurately and fairly reflect the management of funds within Barwon Health. We welcome the report and the opportunity it provides to strengthen the management and reporting processes.

Recommendations 3.1 and 4.1

Barwon Health accepts these recommendations. The availability of comprehensive policies and procedures will provide guidance to staff in the management of funds. We accept the finding that some of our policies and procedures require updating, and this will be a priority task.

Recommendation 4.2

Barwon Health accepts this recommendation. Procedures to establish special purpose funds enable staff to ensure that funds are correctly classified according to their source and restrictions placed on their use. Procedures are currently in place, but will be reviewed and updated to ensure correct classification of funds.

Recommendation 4.3

Barwon Health accepts this recommendation. Reporting of specific purpose funds to management allows better financial management to be undertaken. As noted in section 4 of the report, Barwon Health currently reports as recommended.



2 Background

2.1 What are specific purpose funds?

Public health services¹ receive funding from a variety of public and private sources. They receive recurrent operating and capital grants from government. They also receive payments from the public in exchange for some of the services they provide.

Public health services may also receive funds from various sources which are required to be spent for specified purposes in accordance with the providers' expressed wishes. These latter funds generally take the form of donations, bequests and research grants, and are commonly referred to as "Specific Purpose Funds" (SPFs). In addition, health services may receive money to hold for others, known as "trust funds". For example, aged care facilities operated by health services may receive accommodation bonds from residents. These bonds are subject to prudential requirements set out in Commonwealth legislation and are ultimately required to be refunded to the resident or their estate. Moneys held in trust need to be separately accounted for and are not available to meet the general operating costs of health services.

Certain public hospitals also operate private practice arrangements. The majority of funds generated from these arrangements also become SPFs, in accordance with the agreements between hospitals and relevant medical staff.

The Ministerial Review of Health Care Networks undertaken in 1999-2000 identified a number of unsatisfactory aspects of the management of SPFs by public hospitals and health services, including:

- reliance on SPF revenues to support operations over a period of years, with the result that liquid asset backing for a number of SPF balances had been substantially eroded in many cases
- inappropriate accounting practices which had not matched revenue to expenditure across funds over a number of years
- inadequate recognition of the "trust" nature of a number of SPFs
- failure to differentiate between the types of SPFs
- the impact on hospital/health service management of arbitrary restraints in the expenditure of SPF balances and cash management, which were not adequately understood by agencies and the Department of Human Services (DHS).

¹ Public health services are defined in the *Health Services Act 1988*. They provide acute inpatient, non-admitted and emergency, mental health, aged care, community health and public health services to the community.

In response to the matters identified by the ministerial review, the government determined that DHS should develop and issue guidelines on the management and usage of SPF cash flows to ensure that hospitals meet SPF liabilities as and when they fall due.

In December 2001, DHS issued *Guidelines for the identification and establishment of Specific Purpose Funds*, for implementation by all public hospitals/health services. These guidelines were prepared to assist agencies to:

- identify and categorise SPFs
- develop business rules to manage SPFs such as recording, matching of revenue and expenses, and reporting
- formulate accounting policy, recording and reporting frameworks relevant to SPF accounts
- monitor the asset backing and liquidity of SPFs to ensure that they are able to meet their obligations on SPFs as and when they fall due
- “clean up” existing SPFs.

The guidelines were not issued as a formal direction by the Minister for Health under the *Health Services Act 1988*, but did state that all public hospitals and health services were expected to implement the guidelines by 30 June 2002.

The guidelines provide for 2 categories of specific purpose funds, namely:

- *restricted* – which are received from external sources with specific conditions attached, giving rise to legal and/or moral obligations that dictate how the funds or assets should be used. These conditions may vary - ranging from a general statement of intended use, through to having a repayment requirement if funds cannot be used as intended
- *internally-managed* – which are restricted only by virtue of a management decision to apply them in a certain manner. These can arise from broad purpose fundraising activities, commercial ventures and internal financial management decisions.

At 30 June 2007, health services disclosed in excess of \$255 million in specific purpose reserves in their financial statements. These reserves comprise both restricted SPFs and internally managed SPFs.

Restricted SPFs are not a material component of the total income or net assets of most public health services. However, they are an important supplement to the general funding available to public health services to improve their services and facilities, and generally represent a significant portion of their liquid assets.

By their nature, restricted SPFs warrant particular attention by health services to ensure that conditions are met and appropriate probity and control measures are implemented for their investment and expenditure. Transparent and effective management is important to assure stakeholders that improper use has not occurred and to maintain public confidence that future contributions will be used for the purposes specified.

2.2 Audit objective and evaluation criteria

The overall objective of the audit was to assess whether selected public health services had:

- complied with the conditions applicable to restricted SPFs
- adequate systems and processes in place to effectively manage their restricted SPFs.

When assessing compliance, we examined whether the funds had been recognised, recorded, spent and invested consistent with any relevant conditions and restrictions, and any applicable policy and guideline requirements, including:

- statutory, trust or other administrative requirements and conditions specified by the provider of the funding
- the DHS guidelines.

As part of our examination, we considered the adequacy of the guidelines issued by DHS on the management of SPFs.

When assessing the adequacy of systems and processes in place at the selected public health services, we examined whether:

- there were comprehensive policies and procedures in place for SPFs and relevant staff were aware of, and complying with, the policies and procedures
- the purposes, conditions, and restrictions attaching to SPFs were documented, and periodically re-assessed to ensure they remain relevant
- restricted SPFs were separately identified and appropriately classified in the financial records
- restricted SPF balances were periodically reconciled and reviewed by management
- restricted SPFs and trust funds, were adequately backed by assets or liquidity, consistent with any provider requirements, to ensure that required future disbursements can be met
- there was adequate oversight and reporting of restricted SPF balances by senior management and the board of management
- there was appropriate reporting of restricted SPFs in the agencies' annual financial statements and annual report.

2.3 Audit scope

The audit reviewed restricted SPFs. For the purposes of the audit, we included “trust funds”, which are predominantly comprised of aged care accommodation bonds, within our definition of restricted SPFs on the basis that moneys held in trust need to be separately accounted for and are not available to meet the general operating costs of health services.

In 1991 and 1997, we examined and reported on the operation of private practice arrangements at certain public hospitals². In 1997, we acknowledged the improvements made by hospitals in the accountability arrangements for private practice activity since 1991, but identified the need to further improve documentation and strengthen control procedures. Examination of the operation of private practice arrangements did not form part of this audit.

Public health services may raise or hold funds under the provisions of specific legislation, such as the *Aged Care Act 1997*, *Fundraising Appeals Act 1996* and *Gambling Regulation Act 2003*. This audit did not examine the extent to which the public health services have complied with relevant registration, licensing and other administrative requirements of these Acts.

We audited the management of restricted SPFs, including trust funds, over the period 1 May 2006 to 30 April 2007 by the Ballarat Health Services³, Barwon Health⁴, Melbourne Health⁵, and the Peter MacCallum Cancer Centre⁶.

These 4 public health services disclosed a total of around \$118 million in SPF reserves and \$28 million in trust funds (including aged care accommodation bonds) in their 30 June 2007 financial statements. Over \$38 million of the \$118 million in SPF reserves disclosed by these health services related to restricted SPFs.

Audit approach

The audit was undertaken in 2 stages:

- the first involved a review and preliminary assessment of the central policy and procedural requirements, and the gathering of relevant information to inform our audit approach, and the selection of 4 health services to be subject to audit

² Victorian Auditor-General's Office, 1997, *Report on Ministerial Portfolios*, May 1997, Victorian Government Printer, Melbourne, pages 62-65.

³ Comprised of Ballarat Base Hospital, Queen Elizabeth Centre and several other entities.

⁴ Comprised of Geelong Hospital, McKellar Centre, Surf Coast Community Health Centre, Geelong Community Health Centre and Corio Community Health Centre.

⁵ Comprised of The Royal Melbourne Hospital (City and Royal Park Campuses), Northwestern Mental Health, North West Dialysis Service, Infrastructure Services Group and Victorian Infectious Diseases Reference Laboratory.

⁶ Comprised of campuses in East Melbourne, Bendigo, Box Hill, Moorabbin and in partnership with the Tattersall's Cancer Centre at Epworth.

- the second phase of the audit involved detailed examination of relevant documentation on the management of restricted SPFs at each of the selected health services.

The audit was performed in accordance with Australian auditing standards.

The total cost of the audit, including the preparation and printing of this report, was \$150 000.

3 Compliance with conditions and guidelines

At a glance

Background

To meet contractual obligations and the provisions of the *Financial Management Act* 1994, health services should ensure that restricted Specific Purpose Funds (SPFs) are used in accordance with the conditions set by the providers of those funds.

In 2001, the Department of Human Services (DHS) issued guidelines to assist public health services in this area.

Key findings

- All 4 public health services examined had satisfied the conditions set by the providers of the restricted SPFs reviewed as part of this audit.
- None of the health services had documented internal policies which were fully consistent with, and comprehensively addressed, all matters included in the guidelines for SPFs issued by DHS.
- While we found that the guidelines issued by DHS in December 2001 generally contained adequate guidance, and are, therefore, fit-for-purpose, there are opportunities for DHS to enhance this guidance. Our audit identified some variability in the interpretation of the guidelines across the health services examined.

Key recommendations

- 3.1 Health services should review and update their internal policies and procedures to ensure they are consistent with the guidelines issued by DHS.
- 3.2 DHS should undertake a review of the guidelines in consultation with the sector and periodically review compliance.

3.1 Introduction

The primary objective of the audit was to determine whether health services had complied with the conditions applicable to their restricted SPFs. As part of the compliance objective, we also assessed the extent to which health services had complied with the DHS guidelines.

3.2 Did health services comply with externally-imposed conditions?

We examined a representative sample of restricted SPFs and trust funds, including aged care accommodation bonds, at each of the selected public health services. We found that the health services had recognised, recorded, spent and invested these funds consistent with conditions specified by the funding providers and other applicable requirements.

3.3 Did health services comply with DHS guidelines?

None of the health services examined had documented internal policies which were fully consistent with, and had comprehensively addressed, all matters included in the guidelines. Issues covered in the DHS guidelines but not addressed in any of the internal policies developed by the health services included the treatment of income derived from the investment of SPFs, and administration costs associated with the management of SPF accounts.

Barwon Health had applied the DHS guidelines most consistently in terms of the extent to which reporting to the board of management followed the guidelines, and the retention of clear documentation on the establishment of SPFs.

The DHS guidelines state that all individual SPFs should be scrutinised and properly reconciled at least annually and, if necessary, adjustments made, so that their correct position may be understood. Other than Ballarat Health Service, the health services did not have documentation to evidence the conduct of annual reviews of all SPF balances or an explicit policy on the level and detail of this review and reconciliation.

Other areas of identified non-compliance with the guidelines related to classification of SPFs between internally-managed and restricted and reporting to the board of management on the asset backing for restricted SPFs. These matters are dealt with in Part 4 of this report.

Our audit identified that some of the non-compliance was unintentional and resulted from variability in the interpretation of the guidelines across the health services examined. Areas of most variability in the interpretation of the guidelines were the initial classification of SPFs (as either internally-managed or restricted), and the extent and nature of reporting on SPFs to the boards of management of health services.

We found that the guidelines issued by DHS in December 2001 generally contained adequate guidance on the aspects of SPF management outlined above and are, therefore, fit-for-purpose. However, the variability of interpretation and application of the guidelines indicates that it would be beneficial for DHS to review the guidelines in consultation with the sector. There are also opportunities for DHS to enhance the guidance provided to health services on the management of SPFs. Areas warranting enhancement and additions to the guidelines include:

- additional guidance on the acquittal processes for SPFs
- guidance on regular reconciliations of SPF reserve balances and related assets or investments to highlight any liquidity issues
- further guidance on the conduct of regular reviews and reconciliations of SPF accounts covering balances and documentation on fund purpose and expenditure
- guidance on how to deal with on-costs or overheads and ongoing operational costs associated with capital additions financed by restricted SPFs.

DHS does not currently undertake any systemic monitoring of compliance by public health services with the guidelines. DHS advised that it sees its role as supporting the sector through the provision of the guidelines. DHS rightly sees it as the responsibility of the board of management for each public health service to ensure that adequate policies, procedures and controls are established and operational for the management of SPFs and all other funding sources utilised by the health service.

Notwithstanding this, it is our view that where DHS has issued guidelines on matters such as the management of SPFs, it should undertake periodic reviews of compliance with the guidelines to obtain assurance about levels of compliance and identify opportunities to further enhance the guidelines. In this way, DHS can satisfy itself and assure the sector that the guidelines remain current and relevant.

Recommendations

- 3.1 Health services should review and update their internal policies and procedures to ensure they are consistent with the guidelines issued by DHS.
 - 3.2 DHS should undertake a review of the guidelines in consultation with the sector and periodically review compliance.
-

4 Adequacy of systems and processes

At a glance

Background

The boards of management of public health services need assurance that their organisations have adequate systems and processes to support the proper administration and management of Specific Purpose Funds (SPFs).

Key findings

- We found some weaknesses in health services' systems and processes for the management of SPFs.
- All health services examined had documented policies on the management of SPFs, however, none were comprehensive.
- There were some inconsistencies in the identification and classification of SPFs.
- At June 2007, restricted SPFs and trust funds were adequately backed by liquid assets and investments at each of the health services examined.
- Only Barwon Health provided monthly reports to the board of management which clearly distinguished whether cash and liquidity figures included restricted SPFs. Senior finance staff at all health services were aware of the importance of monitoring the management of SPFs and were exercising adequate oversight of these funds.
- All the health services examined had appropriately reported on restricted SPFs in their annual financial statements.

Key recommendations

- 4.1 Health services should review and update their internal policies and procedures to ensure they are comprehensive.
- 4.2 Health services should review their procedures for ensuring reliable classification of SPFs at the time they are received and recorded.
- 4.3 Health services should ensure that monthly reports to the board of management clearly identify the extent to which restricted SPFs are backed by sufficiently liquid assets and the impact of these funds on the overall liquidity position of the organisation.

4.1 Introduction

An objective of the audit was to determine whether health services had established adequate systems and processes to support the effective administration and management of SPFs.

In assessing whether the audited health services maintained adequate systems and processes, we examined whether there were comprehensive policies and procedures operating for the receipt, recording, disbursement, investment, management and reporting of restricted SPFs.

As a part of this assessment we specifically examined whether:

- the purposes, conditions, and restrictions attaching to restricted SPFs were documented and periodically re-assessed
- restricted SPFs were separately identified and appropriately classified in the financial records
- restricted SPF balances were periodically reconciled and reviewed by management
- restricted SPFs and trust funds, including aged care accommodation bonds, were adequately backed by sufficiently liquid assets, consistent with any provider requirements, to ensure that required future disbursements can be met
- there was adequate oversight of restricted SPF balances by senior management and adequate reporting to the board of management
- there was appropriate reporting of restricted SPFs in the health services' annual financial statements and annual report.

4.2 Were there comprehensive policies and procedures in operation?

We found that all of the health services we examined had documented policies on the management of SPFs.

However, none had policies which were fully consistent with, and comprehensively addressed, all matters included in the Department of Human Services (DHS) guidelines. We also found that the operational procedures developed to effect SPF policies were generally not documented, formally approved or periodically reviewed.

The health services generally lacked formally documented and approved policies and procedures on the investment of SPFs (including the treatment of investment income), charging of administration costs to SPFs and acquittal of SPF expenditure.

Of the four health services examined, Barwon Health, Ballarat Health Services and Melbourne Health held aged care accommodation bonds. We found that accommodation bonds had been managed in accordance with the applicable requirements by each of these health services. We also found that Ballarat Health Services and Melbourne Health had documented appropriate policies and procedures for the management of accommodation bonds.

At Barwon Health, formal policies and procedures were not documented and authorised on the recording and management of aged care accommodation bonds. Controls over the processing of aged care accommodation bonds could be improved by establishing a formal agreement with the service provider engaged to undertake this activity.

Peter MacCallum Cancer Centre had undertaken a detailed review of its policies on and management of restricted SPFs in 2005 and reported the results of this review to the board of management. The review identified:

- cost centres classified as restricted SPFs when in fact the providers of these funds had not set any conditions or specific restrictions for their use (i.e. general donations)
- a lack of consistency in accounting practices due to staff turnover
- a lack of ongoing review of restricted fund balances
- a lack of adequate or appropriate documentation supporting the establishment of SPFs and detailing their individual purpose.

Management advised that the findings from the 2005 review were used as the basis for improvements in the management of restricted SPFs. Our audit indicated that some of the matters identified in management's 2005 review had not been fully addressed, such as the need to maintain clear documentation on the purpose and management of all SPFs and the need to retain clear evidence of the ongoing review of all restricted SPF balances.

Recommendation

- 4.1 Health services should review and update their internal policies and procedures to ensure they are comprehensive.

4.3 Are the purposes, conditions and restrictions attaching to SPFs documented and periodically re-assessed?

At each health service, we assessed whether the purposes, conditions and restrictions attaching to restricted SPFs were documented, and periodically re-assessed to determine whether they had been complied with and were still relevant.

We found that:

- apart from Barwon Health, there were instances at each health service where documentation on the purpose and management of SPFs was not maintained for some funds. In the absence of such documentation, it is difficult to provide assurance that SPFs have been managed in accordance with management's policies and procedures and the conditions set by providers of funds
- at Ballarat Health Services, there was clear evidence of an annual review process on all SPFs to assess the relevant conditions and purposes to determine whether they had been complied with and were still relevant
- at Peter MacCallum and Melbourne Health, the only SPFs where there was clear evidence available of regular reconciliations and reviews were research funds. Both health services identified compensating controls over both research and non-research restricted SPFs which partly addressed this issue, but there was limited evidence available on the operation of these compensating controls.

Audit testing, however, did not disclose any breached conditions.

4.4 Are SPFs separately identified and appropriately classified in the financial records?

We assessed whether SPFs were separately identified and appropriately classified in the financial records at each of the selected health services.

The key issue was whether SPFs were classified as internally-managed or restricted. SPFs wrongly classified as internally-managed may be re-allocated at management's discretion, thereby creating an increased risk of non-compliance with externally-imposed conditions.

We found inconsistencies in the identification and classification of SPFs across and within the health services, and a small number of instances where health services had misclassified SPFs between internally-managed and restricted. These instances of misclassification were not significant in terms of the overall level of SPFs managed by the health services.

Ballarat Health Services has a policy of recording all SPFs as internally-managed unless the funds are under the control of an external board and/or there is a clearly documented requirement for the health service to repay funds in the event they cannot be used for the specified purpose. While this position may be literally arguable under the DHS guidelines, it does not seem consistent with the spirit of the guidelines which indicate that where an agency has possession or title to the funds but has no discretion to amend the restriction and/or condition underlying the funds, then the SPFs should be regarded as restricted.

At Melbourne Health we identified funds classified and recorded as restricted SPFs which, in fact, were sourced from general fundraising activities and were, therefore, able to be spent for purposes determined by the health service. This exposes Melbourne Health to the risk that unrestricted funds incorrectly classified as restricted are “parked” and not made available for use by the entity. We also found 2 donations which had been classified as internally-managed SPFs but there was insufficient supporting documentation to determine whether this classification was correct.

Recommendation

4.2 Health services should review their procedures for ensuring reliable classification of SPFs at the time they are received and recorded.

4.5 Are SPF balances periodically reconciled and reviewed by management?

At each health service examined, we sought evidence of regular reconciliation and review of SPF balances by management to ensure accurate recording of revenue and expenditure associated with these funds, and control over their use. These reconciliations are important for assuring restricted SPFs are only used for the specified purposes.

We found:

- at Ballarat Health Services there was clear evidence of an annual review and reconciliation process on all SPFs
- at Peter MacCallum and Melbourne Health the only SPFs where there was clear evidence available of regular reconciliations and reviews were research funds. Both health services identified compensating controls which partly addressed this issue, but there was limited evidence available on the operation of these compensating controls
- at Barwon Health not all SPFs were subject to adequate and regular review and reconciliation, and this was evidenced by a small number of funds with negative balances. We brought these to the attention of management and a new quarterly review procedure was implemented to identify and manage funds nearing or in a negative balance.

4.6 Are restricted SPFs adequately backed by assets or liquidity?

Health services need to maintain sufficiently liquid assets to be able to meet their obligations arising from restricted SPFs and trust funds. The guidelines issued by DHS in December 2001 provide clear guidance that:

- all restricted SPFs if not technically a “trust”, are of a trust nature and as such there should be adequate assets backing these funds

- restricted SPFs may contain non-current, and non-liquid, assets and liabilities according to the circumstances and nature of the fund. Where the health service wishes to treat the assets of the fund globally with the other assets of the entity for cash management or similar purposes, the interests of the fund must be protected by recognising the rights of the fund in internal management reporting and making the treatment clear in reporting fund and liquidity balances to the board of management
- it is important that the board of management is fully aware that the liquid assets backing restricted SPFs have been fully or partly used to calculate liquidity ratios.

At 30 June 2007, restricted SPFs were adequately backed by sufficiently liquid assets and investments at each of the health services examined as part of this audit.

Notwithstanding this, these liquid assets and investments are also required to address many other claims against them such as operating expenses and employee entitlements.

We also found that trust funds, including aged care accommodation bonds, were adequately backed by sufficiently liquid assets and investments at 30 June 2007. In the case of aged care accommodation bonds, there are prudential requirements imposed by Commonwealth legislation aimed at protecting these funds and ensuring that the bonds are able to be refunded as required. Our audit indicated that the 3 health services examined which held these bonds were complying with the prudential requirements.

4.7 Is there adequate oversight of SPF balances by senior management and adequate reporting to the board of management?

Senior management and the board of management for each health service make decisions on future directions and the allocation of resources. The quality of these decisions is influenced by the quality and completeness of information they receive.

We found that, with the exception of Barwon Health, the health services examined did not provide monthly reports to the board of management which clearly distinguished whether cash and liquidity figures included restricted SPFs and on this basis the reporting was not consistent with the DHS guidelines.

However, we did find at all health services examined that senior finance staff were aware of the importance of monitoring the management of SPFs and were exercising adequate operational oversight of these funds.

Critical to any entity is its ability to monitor and control its cash flows and available liquidity. Under the *Health Services Act 1988*, one of the functions of the board of a public health service is to monitor the performance of the health service to ensure that its audit and accounting systems accurately reflect the financial position and viability of the organisation. In turn, one of the functions of the chief executive officer of a public health service is to ensure that the board and its committees are assisted and provided with relevant information to enable them to perform their functions effectively and efficiently. To discharge these functions effectively, the chief executive officer and board of each public health service need a clear understanding of the restricted SPFs under their control and the impact of these funds on the actual liquidity of the entity.

The guidelines issued by DHS in December 2001 are clear on the issue of reporting to the board of management on restricted SPFs. The guidelines indicate that while the nature and detail of reporting to the board is a matter for each agency, it is important to recognise that there is a minimum amount of information which the board must have to be able to perform its review and monitoring functions. On this basis, the guidelines recommend that the liquidity ratios and asset backing for restricted SPFs should be advised to the board at least monthly.

Recommendation

- 4.3 Health services should ensure that monthly reports to the board of management clearly identify the extent to which restricted SPFs are backed by sufficiently liquid assets and the impact of these funds on the overall liquidity position of the organisation.

4.8 Is there appropriate reporting of SPFs in the annual financial statements?

External financial reports by public health services are required to be prepared in line with the requirements of the Australian accounting standards and the *Financial Management Act 1994*. The guidelines issued by DHS in December 2001 on SPFs include guidance on external financial reporting of restricted SPFs. In essence, they are to be recognised as revenue on receipt and reported as part of equity in the health service balance sheet.

We found that all of the health services examined had appropriately reported on restricted SPFs in their annual financial statements.

Appendix A

Self assessment checklist for public health services managing restricted SPFs

Self assessment checklist

The purpose of this self assessment checklist is to serve as a quick reference guide on good management practices for public health services managing restricted SPFs.

Public health services managing restricted SPFs should:

- establish and maintain comprehensive policies and procedures for the management of SPFs
- ensure that SPFs are correctly classified as either internally-managed or restricted at their inception and that appropriate documentation is maintained on this classification
- periodically review and reconcile SPF balances
- ensure that restricted SPFs are adequately backed by sufficiently liquid assets and investments
- provide monthly reports to the board of management which clearly distinguish whether cash and liquidity figures include restricted SPFs
- ensure appropriate disclosure of restricted SPFs in annual financial statements.

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