Portfolio Departments: Interim Results of the 2009–10 Audits

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V I C T O R I A

Victorian
Auditor-General

Portfolio Departments: Interim Results of the 2009–10 Audits

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Victorian Auditor-General's Office

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 *Portfolio Departments: Interim Results of the 2009–10 Audits*.

Yours faithfully

D D R PEARSON
Auditor-General

28 July 2010

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Audit summary

Background

This report informs Parliament about internal control issues arising from our interim financial audit of the 11 portfolio departments and recommends improvement in their internal controls.

All portfolio departments operate adequate internal controls to assure the reliability of their financial reporting, the efficiency and effectiveness of their operations and their compliance with all relevant laws and regulations. In our annual financial audit however, we focus on the internal controls that relate to financial reporting. While it is not our responsibility to form an opinion on internal controls, we nevertheless raise with management any control weaknesses or breakdowns we identify.

Overall conclusion

Weaknesses identified in the information technology (IT) controls at portfolio departments should be addressed, particularly the oversight of outsourced IT providers, system wide security and aspects around the protection of personal information.

Controls over the identification, declaration and management of conflicts of interest should also be strengthened.

While overall we found that portfolio departments have adequate procurement policies, improvements to contract recording and controls over payments are required.

Findings

Common internal control weaknesses

The audit evaluation of the design and effectiveness of the control environment at portfolio departments includes a review of IT controls over those financial systems that provide information for the annual financial statements. Three common IT control weaknesses were identified in portfolio departments.

We found that three portfolio departments were not adequately monitoring the performance of outsourced IT providers and service level agreements were not in place for the outsourced IT functions in a further two portfolio departments.

IT system security had weaknesses including poor controls over password and remote system access, with limited monitoring of the integrity of the operation of security systems. This situation increases the risk of unauthorised access to departmental information.

The confidentiality of personal information is not adequately recognised as a risk in the risk register of three portfolio departments. Also, in one shared services environment affecting three portfolio departments, actual personal information was used when conducting systems development and testing. This situation heightens the risk of misuse of personal information, identity theft and fraud.

Controls over declarations of interest

A cyclical approach to reviewing internal controls relating to significant annual financial report balances and disclosures consistent with Australian Auditing Standards is used. This year we reviewed key management controls over declarations of interest in all 11 portfolio departments.

Conflicts of interest are important issues for portfolio departments as the 'business of government' relies on employees acting and being seen to act honestly and impartially at all times. Portfolio departments are required to operate in a manner which either avoids any conflict of interest or, when they arise or can be perceived to arise, manages them with integrity.

We found that management controls should be improved as:

- Seven portfolio departments did not take a systematic approach to gathering, recording and managing declarations of interest. This makes conflicts more difficult to manage and less transparent.
- Five portfolio departments did not have a consolidated conflicts of interest policy. Therefore, departmental officers do not have a central source of information outlining their responsibilities and procedures to follow if they have, or might have, a conflict.
- Six portfolio departments had separate conflicts of interest policies. However, these could be improved by including the actions required to manage conflicts, consequences for non compliance with the policy, and procedures for maintaining the privacy of information.

There is a pervasive lack of training on conflict identification and management. No portfolio department is conducting regular staff training. This issue was also raised by the Ombudsman in his June 2010 report, *Ombudsman investigation into the probity of the Kew Residential Services and St Kilda Triangle developments.*

Controls over procurement

In 2009–10 the general government sector was expected to procure goods and services of $13 885 million and spend $5 228 million on fixed assets. The Minister for Finance’s standing directions require portfolio departments to implement and maintain an effective internal control framework for procurement. Such a framework should assure procurement satisfies business needs and occurs in line with documented policies and procedures.

We examined a selection of 22 contracts across the 11 portfolio departments. Contracts were selected from departmental records covering goods, services and construction projects. We found that good practice was followed for 20 of them but there are areas for improvement.

- Officers need written guidance about exactly what is ‘high risk’, ‘high value’ or ‘complex’ so that there is consistency within and between portfolio departments as to when a strategic procurement plan is required.
- The functions of probity advisor and probity auditor should be performed by different parties.
- Contract details should be recorded on registers by portfolio departments.
- Penetration testing of critical IT networks should be conducted annually to evaluate the risk of unauthorised access and fraud.

Financial reporting framework

For 2009–10 there were three significant changes to the financial reporting framework.

- The presentation of financial statements has changed with a new format for the operating statement and more disclosure required when the comparative information from prior periods is restated.
- A staggered approach to adopting fair value for infrastructure assets means that ports and metropolitan water entities will report infrastructure assets at fair value in 2009–10, while rail and regional water agencies will do so in 2010–11. This is notwithstanding the fair value requirement in AASB 1049, at the whole of government level, was first foreshadowed in May 2007.
- All land under roads will be recognised as an asset and reported at fair value by VicRoads for the first time in 2009–10.

A key feature of the *Public Finance and Accountability Bill* (the bill) is the proposed classification of public sector entities into four categories with different reporting and auditing requirements. The Australian Accounting Standards Board has also mandated a differential reporting framework, however, this has only two categories. It is important that these two differential reporting frameworks reconcile so that the accountability for, and transparency of, the use of taxpayer funds is maintained.

As the bill was not passed before 1 July 2010, the shortened annual reporting time frames proposed in the bill may not be mandatory for the year ending 30 June 2011. However, the timeliness of annual reporting by public sector agencies would be improved if the shortened time frames proposed in the bill, and which are consistent with those adopted for 2009–10, were adopted for the year ending 30 June 2011.

The International Public Sector Accounting Standards Board has issued a consultation paper recommending governments report on the long-term sustainability of public finances. Although this is a preliminary view, it would be opportune for the Department of Treasury and Finance to consider these proposals when developing the proposed Ministerial directions to underpin the bill.

Recommendations

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1.	Portfolio departments should assess their policies and procedures against the commonly identified internal control weaknesses to assure they are operating in a reliable and cost effective manner.	10
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Submissions and comments received

In addition to progressive engagement during the course of the audit, in accordance with section 16(3) of the *Audit Act 1994* a copy of this report, or relevant extracts from the report, was provided to all relevant entities with a request for comments or submissions.

Agency views have been considered in reaching our audit conclusions and are represented to the extent relevant and warranted in preparing this report. Those Section 16(3) comments and submissions provided are included in Appendix B.

Audit conduct

Audits of the 11 portfolio departments were undertaken in accordance with Australian Auditing Standards.

The total cost of preparing and printing this report was $180 000.

1 Background

1.1 Introduction

The state election is scheduled for 27 November 2010 with Parliament rising in early October 2010. This shortens our time line for reporting on the annual financial statement audit of all 11 portfolio departments. Accordingly, we have produced this interim report on the annual financial statement audit of the portfolio departments and will provide a final acquittal report in February 2011.

This report is the first of seven reports to be presented to Parliament covering the results of the audits of public sector financial and performance reports. Figure 1A shows the intended reports and time frames.

This report also comments on the effectiveness of internal controls and the management controls relating to declarations of interest and procurement in portfolio departments.

Figure 1A
VAGO reports on the results of the 2009–10 financial audits

Report	Description
Portfolio Departments: Interim Results of the 2009–10 Audits *(this report)*	This report has the interim results of audits of the 11 portfolio departments. It examines the effectiveness of internal controls for IT systems; for identifying, declaring and managing conflicts of interest; and for procurement. It also makes comment on financial reporting developments.
Local Government: Interim Results of the 2009–10 Audits	The report will provide the interim results of audits of 79 local governments, 13 agencies they control and 12 regional library corporations. It will examine the effectiveness of internal controls, aspects of council governance and IT change management. *Proposed to be tabled in Parliament in August 2010.*
Water Entities: Interim Results of the 2009–10 Audits	The report will provide interim results of audits of 19 water entities. It will examine the effectiveness of internal control supporting the preparation of the financial reports and aspects of how they manage capital projects and creditors. *Proposed to be tabled in Parliament in August 2010.*

Figure 1A
VAGO reports on the results of the 2009–10 financial audits – *continued*

Report	Description
Public Hospitals: Interim Results of the 2009–10 Audits	The report will provide the interim results of audits of approximately 110 agencies in the sector. It will examine the effectiveness of internal control supporting the preparation of the financial reports and aspects of how they manage leave and creditors. *Proposed to be tabled in Parliament in September 2010.*
Auditor-General's Report on the Annual Financial Report of the State of Victoria, 2009–10	The report will provide the result of the audit of the state's annual financial report. It will examine the quality and timeliness of financial reporting, explain significant financial results for the state and make observations on the status and financial implications of significant issues. *Proposed to be tabled in Parliament in October 2010.*
Acquittal Report: Results of the 2009–10 Audits	The report will provide the results of the annual financial statement audits of approximately 420 agencies across the portfolio departments and associated entities, and all other sectors including local government, water entities and public hospitals. The report will include comment on the timeliness of their financial reporting and financial sustainability. *Proposed to be tabled in parliament in February 2011.*
Tertiary Education and Other Entities: Results of the 2010 Audits	This report will provide the results of the annual financial audits of approximately 110 entities that end their financial year other than on 30 June 2010. It will examine timeliness of their financial and performance reporting, the effectiveness of their internal control, their financial sustainability and aspects of how they manage creditors, employee costs and student fee revenue. *Proposed to be tabled in Parliament in May 2011.*

Source: Victorian Auditor-General's Office.

1.2 Financial audit framework

An annual financial audit has two aims:

- to give an opinion consistent with Section 9 of the *Audit Act 1994*, about whether financial reports are fairly stated
- to consider whether there has been any wastage of public resources or any lack of probity or financial prudence in the management or application of public resources, consistent with Section 3A(2) of the *Audit Act 1994*.

Figure 1B shows the three phases of a financial audit and details how the 2009–10 interim audit of the 11 portfolio departments was conducted.

Figure 1B
Financial audit framework

Planning

Planning is not a discrete phase of a financial audit, rather it continues throughout the engagement. However, initial audit planning is conducted at two levels:

- At a high or entity level, planning involves obtaining an understanding of the entity and its environment, including its internal controls. The auditor identifies and assesses: the key risks facing the entity; the entity's risk mitigation strategies; any significant recent developments; and the entity's governance and management control framework.
- At a low or financial reports line item level, planning involves the identification, documentation and initial assessment of processes and controls over management, accounting and information technology systems.

The output from the initial audit planning process is a detailed audit plan and a client strategy document, which outlines the proposed approach to the audit. This strategy document is issued to the client after initial audit planning and includes an estimate of the audit fee.

Conduct

The conduct phase involves the performance of audit procedures aimed at testing whether or not financial statement balances and transactions are free of material error. There are two types of tests undertaken during this phase:

- Tests of controls, which determine whether controls identified during planning were effective throughout the period of the audit and can be relied upon to reduce the risk of material error.
- Substantive tests, which involve: detailed examination of balances and underlying transactions; assessment of the reasonableness of balances using analytical procedures; and a review of the presentation and disclosure in the financial reports, for compliance with the applicable reporting framework.

The output from this phase is a final (and possibly an interim) management letter which details significant findings along with value-adding recommendations on improving controls and processes. These documents are issued to the client after any interim audit work and during the reporting phase.

Reporting

The reporting phase involves the formal presentation and discussion of audit findings with client management, and / or the audit committee. The key outputs from this process are:

- A signed audit opinion, which is presented in the client's annual report alongside the certified financial reports.
- A report to Parliament on significant issues arising from audits either for the individual entity or for the sector as a whole.

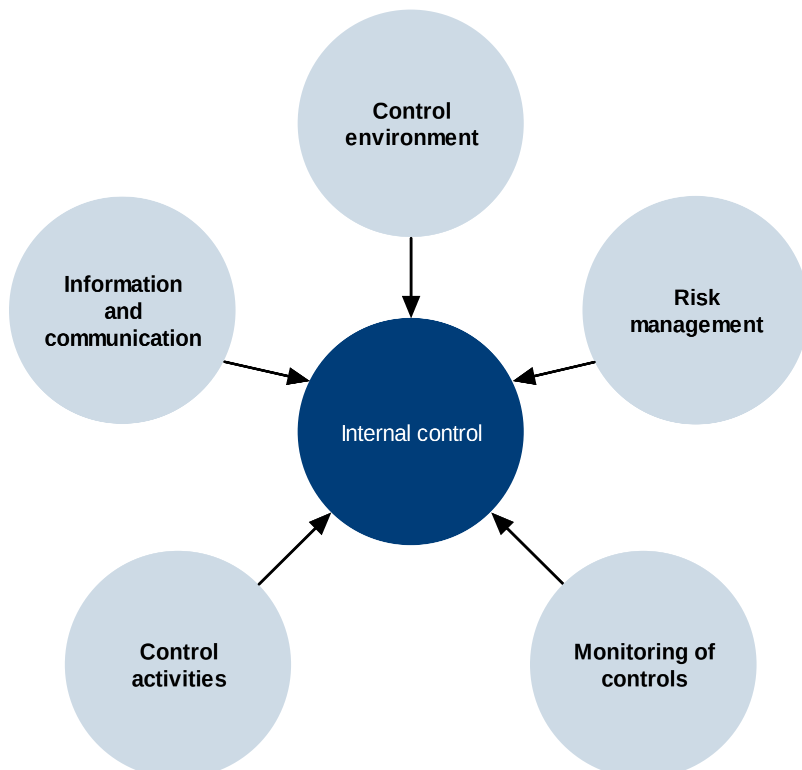
Source: Victorian Auditor-General's Office.

1.2.1 Audit of internal control

Assessment of an agency's internal controls is part of a financial audit. Internal control is how an organisation or entity can reasonably assure that its financial reporting is reliable, its operations are effective and efficient and that it is complying with laws and regulations.

Figure 1C shows diagrammatically the main components of an effective internal control framework.

Figure 1C
Internal control framework



Source: Victorian Auditor-General's Office.

In the diagram**:**

- the **control environment** provides the fundamental discipline and structure for controls and includes governance and management functions and the attitudes, awareness, and actions of those charged with governance and management
- **risk management** involves identifying, analysing and mitigating risks
- **monitoring of controls** assess the effectiveness of internal controls in practise
- **control activities** are the policies, procedures and practices that management prescribes to help meet entity objectives
- **information and communication** involves communicating control responsibilities throughout the portfolio department and providing information in a form and time frame that allows officers to discharge their responsibilities.

The annual financial audit enables the Auditor-General to form an opinion on an agency's financial report. An integral part of this process, and a requirement of Australian Auditing Standard 315 *Understanding the Entity and its Environment and Assessing the Risk of Material Misstatement*, is to assess the adequacy of the agency's internal control framework and governance processes as they relate to the accuracy, completeness and reliability of their financial reporting.

Internal control weaknesses we identify during an audit will usually not result in a qualified audit opinion. A qualification is usually only warranted if weaknesses cause significant uncertainty about the financial information being reported. Often, an agency will have other compensating controls to mitigate the risk of material error. We bring weaknesses we find during an audit of a portfolio department to the attention of its secretary and audit committee.

Section 16 of the *Audit Act 1994* empowers the Auditor-General to report to Parliament on the results of audits. This report includes the results of our review of internal controls related to the financial reporting responsibilities of the 11 portfolio departments.

1.3 Financial reporting framework

The main legislation governing financial reporting of portfolio departments is the *Financial Management Act 1994* (FMA).

The FMA requires annual reports to be given to the relevant minister and tabled in Parliament within four months of the end of the financial year. The annual report must include the financial report of the portfolio department. The financial report must be provided for audit within eight weeks of year end, and an audit opinion issued within four weeks of the financial report being received.

All portfolio departments prepare their financial reports in accordance with the Australian Accounting Standards, including the Australian accounting interpretations.

Independent audit opinions add credibility to financial reports by providing assurance that the information is reliable. A clear audit opinion confirms that the financial report has been prepared according to the requirements of relevant accounting standards and legislation.

If the report has not been prepared in accordance with the relevant reporting framework it is issued with a qualified audit opinion. A qualified audit opinion means that the financial report is materially deficient and is therefore less reliable and useful as an accountability document.

2 Common internal control weaknesses

At a glance

Background

As part of our financial audits we assess internal controls that affect the reliability of financial reporting. This year, information technology (IT) issues were commonly reported to the relevant departmental secretary and audit committee.

Findings

- Three portfolio departments were not adequately monitoring the performance of outsourced IT providers and service level agreements were not in place for the outsourced IT functions in a further two portfolio departments.
- Portfolio departments had poor IT system security controls over password and remote system access, with limited monitoring of the integrity of the operation of security systems. This situation increases the risk of unauthorised access to departmental information.
- The confidentiality of personal information is not adequately recognised as a risk in the risk register of three portfolio departments. Also, in one shared services environment affecting three portfolio departments, actual personal information was used when conducting systems development and testing. This situation heightens the risk of misuse of personal information, identity theft and fraud.

Recommendation

Portfolio departments should assess their policies and procedures against the commonly identified internal control weaknesses to assure they are operating in a reliable and cost effective manner.

2.1 Introduction

All portfolio departments operate adequate internal controls to maintain the reliability of financial reporting, the efficiency and effectiveness of their operations and compliance with all relevant laws and regulations. In our annual financial audits, we focus on the internal controls relating to financial reporting and assess whether portfolio departments have managed the risks that their financial statements will not be complete and accurate. Poor controls diminish management's ability to achieve their portfolio department's objectives and comply with relevant legislation, and increase the risk of fraud.

Our interim audit of the 11 portfolio departments found instances where internal controls should be strengthened. We reported these to departmental secretaries and audit committees.

Three information technology (IT) issues commonly arose:

- oversight of outsourced IT provision
- IT system security
- confidentiality and security of personal information.

2.2 Oversight of outsourced IT provision

At the time of our interim audits, six portfolio departments had outsourced their IT hardware and operating environments to CenITex, the Victorian government IT shared services agency. Subsequently, a further three portfolio departments completed outsourcing to CenITex while the remaining two portfolio departments are planning to do so as required by government policy.

Portfolio departments also outsource financial applications such as payroll to both third party government and private providers.

The *Financial Management Act* 1994 (FMA) requires portfolio departments to 'ensure effective management of outsourced financial functions to obtain the required level of service and maintain compliance with the FMA'.

When portfolio departments outsource functions, they remain accountable for the performance and quality of information in outsourced systems. This is particularly important when preparing financial statements as portfolio departments need to have confidence in the reliability and completeness of financial system information. The performance of outsourced functions therefore needs to be monitored by portfolio departments so that they can detect and manage any performance risks.

Without comfort that outsourced providers have adequate controls, portfolio departments can be exposed to additional risks and may not fully comply with the FMA.

We noted weaknesses in departmental oversight of outsourced IT provision including:

- five of the six portfolio departments using CenITex services had not sought a letter of comfort to adequately assure themselves about the effectiveness of CenITex controls
- three portfolio departments did not monitor the performance of their IT service providers using pre-determined key performance indicators and targets
- two portfolio departments did not have service level agreements with their IT service providers.

In *Portfolio Departments and Associated Entities: Results of the 2008–09 Audits* tabled in December 2009 it was recommended that arrangements be put in place to manage outsourced service providers, with timely monitoring of performance against these arrangements. It is disappointing that at the time of this report those recommendations had not been fully implemented.

2.3 IT system security

Portfolio departments process, store and communicate huge volumes of information in electronic format. Effective IT security controls mitigate the risks that information will be inappropriately released and that information will be incomplete, unreliable or inaccurate. IT systems should be supported by security policies and procedures that control user access, and monitor and report compliance with these policies and procedures.

IT system security weaknesses were reported to portfolio departments, including:

- six portfolio departments had password settings with no complexity or length requirements, no history set to prevent repeating passwords, and no expiration time frame
- remote log in controls at CenITex, impacting four portfolio departments, were not configured to log user activity and stop users from unlimited failed attempts to access systems
- three portfolio departments had weaknesses in the policies and procedures governing information security
- information security policies and procedures were not approved by senior management in one portfolio department
- one portfolio department did not log and monitor compliance with security policies and procedures.

Without appropriate security controls there is an increased risk of unauthorised access to information.

2.4 Confidentiality and integrity of personal information

To maintain the confidentiality and integrity of personal information, portfolio departments should restrict access to people who need it to perform their duties. This is also a requirement of the *Information Privacy Act 2000*.

Controlling access to personal information reduces the risks that information is used inappropriately, corrupted or lost, either intentionally or inadvertently. Failure to maintain the confidentiality of personal information exposes individuals and public sector agencies to the risks of reputational damage, identity theft, non compliance with legislative requirements and fraud.

Portfolio departments should better protect the confidentiality and integrity of personal information in their IT systems. We found:

- actual personal information in the human resource system and payroll system was used during development and testing of applications for one shared services environment affecting three portfolio departments
- three portfolio departments did not identify confidentiality and integrity of personal data as a risk, nor was it evident that it was being appropriately monitored and managed as part of the portfolio department's risk management activities.

Recommendation

1. Portfolio departments should assess their policies and procedures against the commonly identified internal control weaknesses to assure they are operating in a reliable and cost effective manner.

3 Controls over declarations of interest

At a glance

Background

A cyclical approach to reviewing internal controls relating to significant annual financial report balances and disclosures consistent with Australian Auditing Standards is used. This year we reviewed management controls over declarations of interest at all 11 portfolio departments.

Findings

- Seven portfolio departments did not take a systematic approach to gathering, recording and managing declarations of interest. This makes conflicts more difficult to manage and less transparent.
- Five portfolio departments did not have a consolidated conflicts of interest policy. Therefore, departmental officers do not have a central source of information outlining their responsibilities and procedures to follow if they have, or might have, a conflict.
- Six portfolio departments had separate conflicts of interest policies. However, these could be improved by including the actions required to manage conflicts, consequences for non compliance, and procedures for maintaining the privacy of information.
- Nine portfolio departments provide conflicts of interest training upon commencement, but no portfolio department conducted regular training to keep staff aware of their conflicts of interest responsibilities. This issue was also raised by the Ombudsman in his June 2010 report, *Ombudsman investigation into the probity of the Kew Residential Services and St Kilda Triangle developments.*

Recommendations

- Portfolio departments should establish a consolidated conflicts of interest policy.
- Portfolio departments should provide regular refresher training to all staff about their responsibilities to identify and declare conflicts, and the consequence for failing to do so.
- Portfolio departments should take a systematic approach to gathering, recording and managing declarations of interest.

3.1 Introduction

A cyclical approach to reviewing internal controls relating to significant annual financial report balances and disclosures consistent with Australian Auditing Standards is used. This year we reviewed management controls over declarations of interest at all 11 portfolio departments.

The *Public Administration Act 2004* and the *Code of Conduct for Victorian Public Sector Employees* require officers of public sector agencies to avoid any real or perceived conflicts of interest. Conflicts of interest are conflicts between the personal interests of the officer and the officer's duty to act in the public interest.

The State Services Authority (SSA), in its *Conflicts of interest policy framework,* identifies three kinds of conflicts:

- **actual** conflicts of interest where there is a direct conflict between an officer's public duties and responsibilities, and their existing private interests
- **perceived** or **apparent** conflicts of interest where a third party could form the view that an officer's private interests could improperly influence how they perform their duties, whether or not the officer has actually been improperly influenced
- **potential** conflicts of interest where an officer has private interests that could conflict with their public duties and responsibilities.

Conflicts of interest are important issues for portfolio departments as the 'business of government' relies on its employees acting or being seen to act honestly and impartially at all times. Portfolio departments are required to operate in a manner which either avoids any conflict of interest or, when they arise or can be perceived to arise, manages them with integrity. Failure to do so gives rise to risks of:

- non compliance with legal requirements
- misconduct, abuse of office or corruption, which can result in inaccurate financial information being disclosed in financial reports
- reputational damage.

The integrity of departmental staff and the existence of a sound system for identifying and managing conflicts of interest are also important to protect public interests.

Overall we found that portfolio departments could improve their policies and procedures over the identification, declaration, and management of conflicts of interest.

3.2 Policy

The SSA's framework applies to all portfolio departments and requires them to develop detailed policies and procedures to identify and manage conflicts of interest.

Figure 3A shows the good practice elements of a conflicts of interest policy as set out in the joint publication, *Managing Conflicts of Interest in the Public Sector,* by the New South Wales (NSW) Independent Commission Against Corruption and the Queensland (QLD) Crime and Misconduct Commission. This joint publication was used as a primary source by the SSA to develop its policy framework.

Figure 3A
Good practice elements of a conflicts of interest policy

Key area	Content
Introduction	The policy should explain: • its purpose—why it was drafted and what it intends to achieve • its application—who it applies to and the range of possible conflicts of interest (which depends on the work and function of the department) • relevant legislation—any laws or regulations that oblige officers to disclose and/or manage conflicts of interest.
Definitions	The policy should define and explain the different types of conflicts of interest and give examples of situations which may give rise to conflicts.
Responsibilities	The policy should name the officer responsible for overseeing its implementation and should define the officer's functions. The officer should have sufficient authority to make the decisions necessary to implement the policy.
Procedures	The policy should describe the process that officers must follow if they think they have or might have a conflict of interest. It should include procedures for declaring and managing interests, and the record keeping required for each type of conflict.
Breaches	The policy should explain the consequences of breaching it.
Privacy	The policy should detail how the privacy of information disclosed under the policy will be handled in line with the department's privacy policy.

Source: Managing Conflicts of Interest in the Public Sector, jointly published by the NSW Independent Commission Against Corruption and the QLD Crime and Misconduct Commission.

The policies of all 11 portfolio departments were assessed against Figure 3A and we found that:

- five portfolio departments did not have a consolidated conflicts of interest policy but included the principles within other policies such as hospitality, entertainment and procurement
- six have developed a separate conflicts of interest policy.

Without a consolidated conflicts of interest policy, departmental officers do not have one central authoritative explanation of their responsibilities and what to do if they have, or think they might have, a conflict. This increases the risk that conflicts will not be identified, reported or managed.

A review of the content of departmental policies against the principles in Figure 3A found that the policies consistently included:

- details about to whom they apply
- reference to relevant legislative requirements
- the name of the officer responsible for overseeing and implementing the policy
- definitions and examples of conflicts of interest
- statements of the responsibilities of managers, other officers and the portfolio department itself
- reporting procedures if an officer thinks that they have or might have a conflict.

The policies of portfolio departments should be improved by including:

- how conflicts will be managed once notified by an officer
- the consequences of not complying with the policy
- procedures to protect the privacy of information.

Recommendation

2. Portfolio departments should establish a consolidated conflicts of interest policy.

3.3 Implementation

If conflicts of interest policies and procedures are to be effective:

- they need to be easily accessible
- officers need to know that they exist and what they cover
- officers need to know what their responsibilities are
- officers need training and support to discharge their responsibilities
- they need to be regularly reviewed so they stay current and achieve their intended outcomes.

Of the 11 portfolio departments, nine provide training and education about conflicts of interest to staff upon commencement. However, no portfolio department provided regular training to remind staff of their responsibility to identify and manage conflicts.

Without regular training there is a heightened risk that staff will overlook their conflicts of interest responsibilities over time.

The issue of training and staff knowledge of conflicts of interest was also raised by the Ombudsman in his June 2010 report, *Ombudsman investigation into the probity of the Kew Residential Services and St Kilda Triangle developments*. In these instances, the Ombudsman's findings are consistent with our assessment of the departmental conflict of interest framework, and point to a pervasive problem. In particular, the Ombudsman found a 'lack of adequate training and policy advice on conflict of interest issues'. This meant that public sector staff could not demonstrate an understanding of the principles of conflict of interest.

Recommendation

3. Portfolio departments should provide regular refresher training to all staff about their responsibilities to identify and declare conflicts, and the consequence for failing to do so.

3.4 Recording of declarations

Portfolio departments vary considerably in how they gather and record declarations of conflicts of interest.

Four portfolio departments take a systematic approach to gathering and recording declarations. These portfolio departments continually update their records and information is handled in line with their privacy policies. Three of the four portfolio departments use the information gathered to make the disclosures required in their annual financial report. The fourth is planning to use the information for reporting this financial year.

The other seven portfolio departments do not take a systematic approach but store declarations in various areas, such as on personnel files and procurement files. This makes it more difficult for them to reliably manage conflicts and impairs transparency. It also makes preparation of the related party disclosure notes in the financial statements less efficient and increases the risk that the disclosures will not be complete and accurate.

Recommendation

4. Portfolio departments should take a systematic approach to gathering, recording and managing declarations of interest.

4 Controls over procurement

At a glance

Background

In 2009–10 the general government sector was expected to procure goods and services of $13 885 million and spend $5 228 million on fixed assets.

To protect the public interest, portfolio departments are required to implement and maintain an effective internal control framework for procurement.

Findings

- Officers need written guidance about exactly what is 'high risk', 'high value' or 'complex' so that there is consistency within and between portfolio departments as to when a strategic procurement plan is required.
- In four of the five contracts that required the appointment of a probity advisor and probity auditor, both functions were performed by the same person.
- The contract value thresholds at which contract details are recorded on registers varies between portfolio departments.
- Penetration testing of information technology (IT) networks had occurred at four portfolio departments.

Recommendations

- The Victorian Government Purchasing Board should develop guidance on the criteria for identifying 'high risk', 'high value' and 'complex' procurement.
- The procurement policies of all portfolio departments should define 'high risk', 'high value' and 'complex' procurement.
- The probity advisor and probity auditor functions should be conducted by different parties.
- Portfolio departments should record all contract data in a register.
- Portfolio departments should undertake penetration testing of their critical IT networks at least annually.

4.1 Introduction

In 2009–10 the general government sector was expected to procure goods and services of $13 885 million and spend $5 228 million on fixed assets. To protect the public interest, the Minister for Finance’s standing directions under the *Financial Management Act 1994* (FMA) require portfolio departments to implement and maintain an effective internal control framework for procurement.

The FMA may be replaced by the *Public Finance and Accountability Bill* which was introduced into Parliament in December 2009 and at the time of finalising this report had not yet been passed. The bill establishes a new legislative framework for the management of public finances including procurement.

An internal control framework should assure that procurements satisfy business needs, are suitably authorised, are in line with policies and procedures and are consistent with the principles of value for money, open and fair competition, accountability, risk management, probity and transparency. These principles should guide the procurement process from needs identification through to contract evaluation and management.

Poor procurement practices give rise to risks of:

- the procurement process being unfair or not transparent
- inadequate competition resulting in reduced value-for-money
- suppliers and portfolio departments facing unnecessary costs
- portfolio departments purchasing inferior goods, services or assets that do not meet their objectives.

Effective internal controls mitigate these risks, increase accuracy of financial reporting, help portfolio departments achieve value for money and improve the probity of the procurement process.

We found that while all portfolio departments have adequate procurement policies, some divergence from good procurement practice was noted, and portfolio departments should improve contract recording and controls over payments.

4.2 Policy

An effective procurement policy needs to clearly articulate the principles, processes and procedures that will apply to all purchases. In addition, the staff involved in the procurement process need to be appropriately trained and supported to carry out their responsibilities effectively.

Section 54L of the FMA empowers the Victorian Government Purchasing Board (VGPB) to make supply policies that must be complied with by all portfolio departments. The VGPB requirements are outlined in Figure 4A.

Figure 4A
Victorian Government Purchasing Board requirements

Key area	Requirement
Accredited purchasing unit	The VGPB requires portfolio departments to establish an accredited purchasing unit. Once a unit is established, the portfolio department applies to the VGPB for an accreditation level that suits the portfolio department's needs and risk environment.
Management plan	Applications for accreditation or changes in accreditation level must include a management plan and an implementation timetable. The VGPB considers and approves the plan and timetable, and reviews them within 36 months of approval.
Training	Officers involved in procurement should undertake training consistent with the Procurement and Contracting Centre for Education & Research (PACCER) training framework.
Policy	Portfolio departments must comply with VGPB policy for the purchase of goods and services.

Source: Victorian Government Purchasing Board.

The procurement policies of all 11 portfolio departments were assessed against the VGPB requirements outlined in Figure 4A and no exceptions were noted.

We found that all portfolio departments:

- have accredited purchasing units with three to 13 full time equivalent employees
- included management plans in their applications for accreditation
- provided staff training consistent with the PACCER framework.

Additional policies and procedures are required under the standing directions of the FMA for the following expenditure types:

- capital expenditure
- gifts
- hospitality
- *Purchasing Card Rules for Use and Administration* issued by the Department of Treasury and Finance
- travel
- personal expense reimbursement
- employee advances
- petty cash.

The standing directions require portfolio departments to review their policies and procedures at least every two years so they remain current and reflect business and operational needs. All 11 portfolio departments have fulfilled these requirements.

4.3 The procurement process

Sound management of procurement assists the effective delivery of government programs and services, and the achievement of government outcomes.

Figure 4B outlines good practice procurement criteria, drawing on the Victorian Auditor-General's Office (VAGO) *Public Sector Procurement: Turning Principles into Practice* guidance and VGPB policies.

The process to be applied for each procurement will vary depending on the value and complexity of the goods or services being purchased. Where the goods or services are expected to be in excess of $150 000 a tender must be undertaken in the open market.

Figure 4B
Procurement good practice criteria

Key area	Good practice criteria
Detailing the procurement process	The items being procured should be clearly specified and documented before going to tender. A procurement conduct plan should be developed and apply to all officers involved in the procurement process. It should document the minimum standard of conduct required of officers. A strategic procurement plan should also be developed to bring together all activities during the procurement process. A procurement conduct plan and strategic procurement plan should be developed for all high value and/or high risk or complex procurements.
Receiving and recording tender submissions	The process of receiving and recording tender submissions must be conducted with integrity, fairness and impartiality. At least two officers should be responsible for managing an electronic tender system or physical tender box and its contents. At the close of the tender submission period, all tenders should be opened in the presence of two officers. Details should be recorded in a register which identifies the number of tenders received at the time tenders closed, and is signed by both officers.
Evaluating tender submissions	All tender submissions should be treated fairly and evaluated against the same criteria, which should be clearly documented in an evaluation plan. The evaluation plan should specify the members of the evaluation panel and each member's responsibility. Each member of the evaluation panel should have relevant skills and knowledge of the goods or services being procured. Each should declare any conflicts of interest. The most capable tenderer delivering value-for-money should be selected, avoiding any actual or perceived bias or preferential treatment.

Figure 4B
Procurement good practice criteria – *continued*

Key area	Good practice criteria
Recommending the preferred submission	A clear audit trail should be maintained to provide evidence that the tender process was fair and transparent. The evaluation panel should prepare a report including who was on the panel, what procedures and criteria it used to select the preferred submission, and its reasons for preferring that submission.
Finalising a contract	A contract, signed by an officer with delegated authority, should be prepared before any work starts, or goods or assets change hands. The contract should include detailed specifications of requirements, including service expectations.
Assuring the quality of the procurement process	A probity plan should be developed for all high value and/or high risk or complex procurement. A probity auditor should be engaged for all high value and/or high risk or complex procurement. The probity auditor provides independent assurance that probity has been observed throughout the procurement process. A separate probity advisor should also be engaged for all high value and/or high risk or complex procurement. The advisor helps prepare the probity plan and provides probity advice during the procurement process.

Source: Victorian Auditor-General's Office and the Victorian Government Purchasing Board.

We assessed the process to award 22 contracts across the 11 portfolio departments against the criteria in Figure 4B. Contracts were selected from departmental records for goods and services, which included construction projects and services.

For 20 of the 22 contracts examined, good practice was evident at all stages of the procurement process. In particular:

- a procurement conduct plan and a strategic procurement plan were developed for all contracts greater than $10 million
- submissions were evaluated by panels consisting of staff with relevant skills and knowledge of the procurement
- members of evaluation panels declared all potential, perceived and actual conflicts of interest
- some portfolio departments prepared strategic procurement plans and probity plans even when they were not required to do so. This strengthened the governance of the procurement process.

VGPB policies require portfolio departments to develop strategic procurement plans and procedures only for high value and/or high risk or complex procurement of goods and services. Two portfolio departments provide written guidance to staff about what is 'high risk', 'high value' and 'complex'. The VGPB does not define these terms and as a result, staff must decide their own interpretations. This risks inconsistencies within and between portfolio departments, and of staff underestimating the need for strategic procurement plans in some cases.

We found that the Department of Transport (DOT) and the Department of Treasury and Finance (DTF) need to improve their procurement processes because:

- there was no probity advisor or probity auditor engaged for one DOT contract with a value of $23.8 million
- there was no tender evaluation plan and no tender evaluation report for one DTF contract with a value of $200 000 even though there were two tenderers.

The 22 contracts subject to review included six with a value in excess of $10 million, and therefore requiring the appointment of a probity advisor and probity auditor in accordance with good practice. Five contracts had a probity advisor and probity auditor appointed. In four of the five contracts, the probity advisor and probity auditor functions were performed by the same person. The need to improve probity over contracts by separating the two probity functions continues not to be adequately recognised and addressed by portfolio departments. This issue was previously reported in our October 2007 report, *New Ticketing System Tender*, and the Public Accounts and Estimates Committee's November 2009 report, *Review of the Findings and Recommendations of the Auditor-General's Reports tabled in July 2006–February 2007*. Recently, the Ombudsman also reported this issue in his June 2010 report, *Ombudsman investigation into the probity of the Kew Residential Services and St Kilda Triangle developments*.

The review of contracts identified a number of information technology (IT) consultancy contracts awarded by the Department of Innovation Industry and Regional Development (DIIRD) through the IT & Administration Staffing Services Panel. Although the procurements occurred within VGPB guidelines, the department's 2008-09 report of operations did not include details of the contracts. The FMA requires disclosure of consultancy contracts in excess of $100 000 in a department's annual report. The contracts meet the definition of a consultancy within the FMA and therefore should have been disclosed. It is expected that DIIRD's consultancy payments including commissions to recruitment firms will be $5 million in 2009–10.

Recommendations

5. The Victorian Government Purchasing Board should develop guidance on the criteria for identifying 'high risk', 'high value' and 'complex' procurement.
6. The procurement policies of all portfolio departments should define 'high risk', 'high value' and 'complex' procurement.
7. The probity advisor and probity auditor functions should be conducted by different parties.

4.4 Recording and managing contracts

Once a contract has been signed, portfolio departments need systems and processes to support the oversight and management of contracts. Contract registers can be an effective means of managing contracts if they are kept current and responsibility for management of the register is assigned. Contract registers can be used as the primary source of reporting commitments in annual financial reports.

We found all portfolio departments maintain one or more contract registers with details of their contracts. A procurement unit or contract manager is responsible for the completeness and accuracy of the contract registers.

Portfolio departments differed in the number of registers they have, what information is recorded in registers, and what use is made of the information.

The Department of Primary Industries and the Department of Education and Early Childhood Development record all contracts in a register regardless of their type or value. The Department of Health (DOH) records all capital contracts on a capital management system. The remaining eight departments, and for goods and services contracts at DOH, record only contracts above a threshold in a register. The usual threshold applied is $100 000.

Recommendation

8. Portfolio departments should record all contract data in a register.

4.5 Making payments

A final step in any procurement process is paying for the contracted goods or services. These days, portfolio departments make most of their payments using electronic funds transfer (EFT).

We reviewed each of the 11 portfolio departments' controls over the security of accounts payable EFT files. While all portfolio departments stored the EFT file on a secure network, four portfolio departments did not protect the file so that changes could not be made.

As a compensating control all 11 portfolio departments reconcile the EFT file totals to the accounts payable system reports. This control should detect any unauthorised changes, but not until after a payment has been made.

The Whole of Victorian Government Information and Communications Technology standard on penetration testing came into effect on 13 November 2009 and requires critical internal systems to be independently penetration-tested at least annually. Penetration testing assesses the ability of a system or network to withstand unauthorised external entry.

Penetration testing of IT networks had occurred at four portfolio departments. Given the susceptibility of EFT files to fraud, all portfolio departments should conduct this testing at least annually.

Recommendation

9. Portfolio departments should undertake penetration testing of their critical IT networks at least annually.

5 Financial reporting framework

At a glance

Findings

- For the 2009–10 financial year, there were three significant changes to the financial reporting framework affecting public sector agencies.
    - The presentation of financial statements has changed with a new format for the operating statement and more disclosure required when the comparative information from prior periods is restated.
    - A staggered approach to adopting fair value for infrastructure assets means that port and metropolitan water agencies will report infrastructure assets at fair value in 2009–10 while rail and regional water agencies will do so in 2010–11. This is notwithstanding the fair value requirement in AASB 1049, at the whole of government level, was first foreshadowed in May 2007.
    - All land under roads will be recognised as an asset and reported at fair value by VicRoads for the first time in 2009–10.
- The *Public Finance and Accountability Bill* (the bill) classifies public sector entities into four categories with differential reporting requirements whereas the Australian Accounting Standards Board (AASB) has introduced a differential reporting framework with two tiers. It is important that these two differential frameworks reconcile so that the accountability for, and transparency of, the use of taxpayer funds is maintained.
- As the bill was not passed before 1 July 2010, the shortened annual reporting time frames proposed in the bill, and which are consistent with those adopted for 2009–10, may not be mandatory for the year ending 30 June 2011.

Recommendation

The Department of Treasury and Finance should require all public sector entities to adopt the shortened annual reporting time frames proposed in the *Public Finance and Accountability Bill* for the year ending 30 June 2011.

5.1 Changes to the financial reporting framework

For the 2009–10 financial year, there were three significant changes to the financial reporting framework:

- revised Australian Accounting Standard AASB 101 *Presentation of Financial Statements*
- the implementation of Financial Reporting Direction (FRD) 121 *Infrastructure Assets (Water/Rail)*
- the issue of Financial Reporting Direction 118B *Land Under Declared Roads*.

5.1.1 Presentation of financial statements

AASB 101 *Presentation of Financial Statements* includes a new concept 'total comprehensive income' in the operating statement. This represents the changes in equity during a period, other than changes resulting from transactions with owners. This means that income and expense items previously recognised directly in equity will now be shown on the comprehensive operating statement. An example of this is when asset revaluation increments and decrements occur.

Other changes in AASB 101 include:

- the statement of changes in equity is now required to be a separate financial statement, rather than a note to the financial report
- a statement of financial position (that is, a balance sheet) is now required at the beginning of the earliest comparative period following a change in accounting policy, the correction of an error or the reclassification of items in the financial statements. In these circumstances, an entity must present three columns in the balance sheet and related notes.

This standard was mandatory for all entities preparing general purpose financial reports for 30 June 2010.

5.1.2 Measurement of infrastructure assets

At 30 June 2009, there was a $15 billion difference between the value of infrastructure assets in the state's Annual Financial Report (AFR) and in the financial reports of individual agencies. All water and rail, and some port agencies were required to measure their infrastructure assets at cost in their statutory financial statements. However, the AFR measured these assets at fair value so that the state complied with the requirements of AASB 1049 *Whole of Government and General Government Sector Financial Reporting*.

To eliminate this difference, FRD 121 required water, ports and rail entities to adopt fair value in their statutory financial statements in either 2009–10 or 2010–11.

The Minister for Finance has allowed agencies to take a staggered approach to adopting fair value for infrastructure assets and to align their accounting policies with those applicable to the whole of government financial statements. Recognising the high number of assets to be valued, the Minister accepted it was impracticable and costly to conduct fair value assessments for all infrastructure assets by 30 June 2010.

For 2009–10 the four metropolitan water entities (Melbourne Water, City West Water, South East Water and Yarra Valley Water) will report their infrastructure assets at fair value. Consistent with other port agencies, the Port of Melbourne will also report infrastructure assets at fair value for 2009–10.

The regional water entities and the Victorian Rail Track Corporation (Victrack) will report their infrastructure assets at fair value for 2010–11.

Compared with the valuation policies and practices of other states and territories, Victoria is one of four Australian jurisdictions yet to require water infrastructure assets to be measured at fair value in entity financial statements. This is notwithstanding that the fair value requirement in AASB 1049, at the whole of government level, was first foreshadowed when the accounting standard was exposed as a draft in May 2007.

In our reports *Water Entities: Results of the 2008–09 Audits* and *Portfolio Departments and Associated Entities: Results of the 2008–09 Audits* tabled last year, we recommended the adoption of consistent recognition and valuation policies for whole-of-government reporting and entity level reporting for 2009–10. We note that the differences will not be fully eliminated this financial year but should be eliminated for the 2010–11 year. The preparation for the fair valuation of infrastructure assets should have commenced earlier given the October 2007 release of AASB 1049 requiring such assets be measured at fair value in the whole of government financial statements.

5.1.3 Recognition of land under declared roads

AASB 1049 *Whole of Government and General Government Sector Financial Reporting* became mandatory for 2008–09 reporting and required the state to recognise all infrastructure assets at fair value. As a result, $18.6 billion of land under roads was recognised at the whole of government level for the first time at 30 June 2009.

The Minister for Finance issued FRD 118 *Land Under Roads* in March 2009 to require the Roads Corporation (VicRoads) in its own statutory financial statements to:

- recognise and measure at cost land under roads acquired after 1 July 2008
- not recognise as an asset land under roads acquired prior to 1 July 2008.

Consequently, VicRoads only recognised land under roads acquired after 1 July 2008 in its financial statements, as permitted under AASB 1051 *Land Under Roads*. However, neither the relief in AASB 1051 nor the requirements of FRD 118 were applicable to the state's AFR, which meant the recognition of land under road was treated differently between VicRoads' financial statements and the state's AFR.

In April 2010, the Minister for Finance released FRD 118B *Land Under Declared Roads* which required all land under roads controlled by VicRoads to be recognised as an asset and measured at fair value. Consequently, VicRoads will recognise land under roads acquired before 1 July 2008 for the first time in 2009–10. The financial impact on the VicRoads financial report is expected to be an increase in assets of around $15 billion.

5.2 Developments in financial reporting

5.2.1 Public Finance and Accountability Bill

The *Public Finance and Accountability Bill* (the bill) was introduced into Parliament in December 2009. At the time of finalising this report the bill had not been passed.

The bill is proposed to replace the *Financial Management Act 1994* and other related legislation to establish a new legislative framework for public finance, including financial reporting. The Department of Treasury and Finance (DTF) advises that the new requirements are expected to be implemented gradually over three years with effect from 1 July 2010.

The bill covers key elements of public finance, including planning, reporting, procurement, borrowing and investment, and appropriations. The changes to the financial reporting framework are significant. The bill establishes a differential financial reporting framework for public sector agencies according to their size, complexity and risk profile. The time lines for annual reporting will also be shortened by one month to bring Victoria in line with the better practice established in Queensland and Western Australia.

Figure 5A shows the different reporting requirements and time lines for reporting.

Figure 5A
Reporting requirements under the
Public Finance and Accountability Bill 2009

Criteria for classification	Form and time lines for reporting	Required to submit financial statements to the Auditor-General
Category 1 and departments		
All departments, public financial corporations, and public bodies with: • assets equal to or greater than $100 million; and • expenses equal to or greater than $25 million; and • liabilities as a percentage of total assets equal to or greater than 20 per cent.	Draft financial statements to be submitted to the Auditor-General within eight weeks of the end of the financial year. Report of operations and audited financial statements to be transmitted to Parliament by 30 September each year (previously 31 October).	Yes
Category 2		
Public bodies with: • assets equal to or greater than $5 million; and • expenses equal to or greater than $5 million.	Draft financial statements to be submitted to the Auditor-General within eight weeks of the end of the financial year. Report of operations and audited financial statements to be transmitted to Parliament by 30 September each year (previously 31 October).	Yes
Category 3 and 4	**Category 3**	
All public bodies that do not meet Category 1 or Category 2 criteria. The relevant minister of the agency is responsible for categorising the agency as either Category 3 or Category 4, drawing on financial considerations and any non-financial considerations established in ministerial directions.	Draft financial statements to be submitted to the Auditor-General within eight weeks of the end of the financial year. Report of operations and audited financial statements to be submitted to Parliament by a ‘prescribed date’ each year.	Yes
	Category 4	
	Category 4 public bodies must provide their annual reports to the relevant minister. The relevant minister must inform the Parliament of the receipt of those reports, and make them available to any Parliamentarian who requests them.	No

Source: Public Finance and Accountability Bill 2009.

The bill allows the Minister for Finance to:

- move public sector agencies to a higher category having regard to financial and non-financial factors
- direct a university, university company or denominational hospital to prepare, submit for audit, and transmit to Parliament an annual report, as if it were a Category 1 agency.

It is proposed that:

- Category 1 and Category 2 agencies will continue to prepare general purpose financial statements in accordance with Australian Accounting Standards
- Category 3 agencies will prepare financial statements with reduced note disclosures
- Category 4 agencies will prepare financial reports in a simplified form.

In June 2010, the AASB issued amending standards introducing a differential financial reporting framework. It is important that the AASB framework and the requirements of the bill reconcile so that the accountability for, and transparency of, the use of taxpayer funds is maintained.

As the bill was not passed before 1 July 2010, the shortened reporting time frames proposed in the bill may not be mandatory for the year ending 30 June 2011. However, the timeliness of annual reporting by public sector agencies would be improved if the shortened time frames proposed in the bill, and which are consistent with those adopted for 2009–10, were adopted for the year ending 30 June 2011.

Recommendation

10. The Department of Treasury and Finance should require all public sector entities to adopt the shortened annual reporting time frames proposed in the *Public Finance and Accountability Bill* for the year ending 30 June 2011.

5.2.2 Differential reporting

At present, agencies preparing general purpose financial statements must apply the recognition, measurement and disclosure requirements of all applicable Australian Accounting Standards, which are based on International Financial Reporting Standards (IFRS).

IFRSs are developed primarily for profit-oriented entities and entities that require access to capital markets and therefore drive extensive disclosure. While public sector agencies must comply with the same accounting standards when preparing general purpose financial statements, their circumstances are different to the private sector. This means that public sector agencies spend much time and money preparing mandatory disclosures that are relevant to capital markets but are of little use to the users of public sector financial statements.

In June 2010 the AASB issued amending standards that introduced a revised differential reporting framework with two tiers of reporting requirements:

- tier 1, full IFRS as adopted in Australia
- tier 2, a reduced disclosure regime.

The standards have mandatory application dates of periods beginning on or after 1 July 2013, but entities may early adopt the standards for the 2009–10 reporting period.

Under the new standards, only the nature and extent of disclosures would vary between the tiers: entities applying the reduced disclosure regime would apply the same recognition and measurement requirements as those applying full IFRS as adopted in Australia.

The standards will require federal, state and territory governments and local governments to apply the tier 1 requirements. Public sector agencies that are not categorised as tier 1 will be able to apply the reduced disclosure regime subject to the relevant legislative reporting framework, such as the proposed *Public Finance and Accountability Bill* referred to in the above section.

While eligible entities may early adopt the standards, DTF has not mandated early adoption of the reduced disclosure requirements for 30 June 2010 reporting. DTF should engage with the AASB in determining the reduced disclosures that would benefit the public sector.

In determining the reduced disclosures, the AASB is applying the overarching principle that the reduced disclosure regime should satisfy the objective of general purpose financial statements, which is ‘to provide information about the financial position, financial performance and cash flows of an entity that is useful to a wide range of users in making economic decisions’.

The AASB has decided that the international standard *IFRS for Small and Medium-Sized Entities* (*IFRS for SMEs*) will not be available for use in Australia as part of the reduced disclosure regime. There are concerns about adopting *IFRS for SMEs* in Australia because:

- some of the accounting policy options that have been removed would be the preferred accounting policy for many Australian entities
- *IFRS for SMEs* will only be updated every three years so entities applying that standard would not have access to improvements and simplifications as they become available at the full IFRS level
- the absence of some accounting policy options in *IFRS for SMEs* would force subsidiaries to adjust accounting policies for consolidation purposes when parent entities apply full IFRS
- having different streams of recognition and measurement requirements would increase the cost of tertiary level education and training in the accounting profession.

Instead, the AASB has applied an approach for determining the reduced disclosures that:

- draws on the international standard *IFRS for SMEs* where the recognition and measurement requirements align with those in full IFRS
- applies the user needs and cost-benefit principles to determine reduced disclosure requirements where the recognition and measurement requirements in full IFRS differ from those under *IFRS for SMEs*.

This approach will benchmark the disclosures under the reduced disclosure regime to those under *IFRS for SMEs*, which are seen as the minimum disclosures required to satisfy the objective of general purpose financial statements.

The issue of the amending standards in June 2010 concludes the first stage of the AASB's differential reporting project. The AASB is now commencing the second stage of the project which relates to the change of application focus from 'reporting entity' to 'general purpose financial statements'. The AASB has commissioned research into the effect of their proposals on preparers of special purpose financial statements, which may include Category 4 agencies under the *Public Finance and Accountability Bill*.

As differential reporting is a key feature of the *Public Finance and Accountability Bill,* the AASB framework clearly has implications for Category 3 and Category 4 public sector agencies.

5.3 Emerging accounting standards

The International Accounting Standards Board (IASB) and the AASB are working on several projects as a result of:

- the review of accounting standards at an international level following the global financial crisis
- the IASB and the United States' Financial Accounting Standards Board (FASB) focus on converging the requirements of international financial reporting standards and US generally accepted accounting principles
- the AASB's renewed focus on developing and improving the relevance of financial reporting standards for the public sector
- the AASB's proposals for differential financial reporting.

The International Public Sector Accounting Standards Board (IPSASB) has also issued standards and exposure drafts on topics of relevance to public sector agencies which are not addressed in the current standards.

Below we outline the proposed changes to the financial reporting framework that we expect to have the greatest impact on public sector reporting.

5.3.1 Income from non-exchange transactions

Income from non-exchange transactions such as grants, donations, bequests, appropriations and taxes often dominate the income streams of public sector and not-for-profit agencies.

The definition and accounting treatment of non-exchange transactions has been a contentious issue for a number of years. In a non-exchange transaction, an entity either:

- receives value from another entity without directly giving approximately equal value in exchange, or
- gives value to another entity without directly receiving approximately equal value in exchange.

The current requirements in AASB 1004 *Contributions* can result in volatility in reported financial performance driven by the timing of when funds are received, notwithstanding that the ongoing operations are steady over time. This reduces the usefulness of public sector financial statements for users making decisions about resource allocation and management accountability.

In response, the AASB and the New Zealand Financial Reporting Standards Board (FRSB) issued a joint exposure draft (ED) 180 *Income from Non-exchange Transactions (Taxes and Transfers)* in June 2009, to replace AASB 1004.

The proposals in the exposure draft are likely to generally result in the deferral of the recognition of income and an increase in the recognition of liabilities, which will reduce year on year volatility in agencies' net results and financial positions.

5.3.2 GAAP/GFS harmonisation of entities in the general government sector

Since June 1999, governments in Australia have been required by AAS 31 *Financial Reporting by Governments* to prepare their annual financial statements based on generally accepted accounting principles (GAAP), but used different reporting frameworks for budgets. This results in a lack of comparability across jurisdictions. There were also concerns that statisticians, economists and accountants were applying accrual principles but reporting different results for the same public sector agency.

In response to these concerns, the AASB addressed the harmonisation of government finance statistics (GFS) and GAAP in two phases.

Phase 1 resulted in the issue of AASB 1049 *Whole of Government and General Government Sector Financial Reporting* in September 2008. AASB 1049 harmonises the GFS and GAAP reporting frameworks to achieve a single set of government reports. Government reports are now comparable between jurisdictions, and directly comparable with budget statements.

Phase 2 is the development of financial reporting requirements for entities within the general government sector, including government departments. Following its issue of ED 174 *Amendments to Australian Accounting Standards to facilitate GAAP/GFS Harmonisation for Entities within the GGS*, the AASB is developing a further exposure draft that improves the quality of financial reporting by not-for-profit entities within the general government sector. This is expected to be issued in late 2010.

Notwithstanding the absence of an accounting standard, portfolio departments were required to early adopt the revised AASB 101 *Presentation of Financial Statements* when preparing their 2008–09 financial statements because it aligns with the presentation requirements of AASB 1049 at whole of government level. This revised presentation format was also applied in the 2008–09 *Model Report for Victorian Government Departments* issued by the Minister for Finance.

All public sector entities were encouraged to adopt the presentation format outlined in the model report, but this was not mandatory. In 2008–09, 58 of the 105 entities in the general government sector chose to adopt the new presentation format. This resulted in financial statements being presented differently across the general government sector, limiting comparability.

5.3.3 Reporting on the long-term sustainability of public finances

The long-term sustainability of public finances means the ability of government to meet its service delivery and financial commitments now and in the future. Information about long term sustainability can enhance accountability and be useful for assessing how public resources are applied.

In November 2009, the International Public Sector Accounting Standards Board (IPSASB) released for comment a consultation paper titled *Reporting on the Long-Term Sustainability of Public Finances*. The IPSASB intends to recommend reporting by governments on the long-term sustainability of public finances. The reporting would be a statement additional to the financial statements or narrative disclosures in the general purpose financial report.

Although the IPSASB is currently presenting a preliminary view, we have raised with DTF the need to consider the proposals in this consultation paper when developing ministerial directions to underpin the *Public Finance and Accountability Bill*.

5.3.4 Financial instruments

In the wake of the recent global financial crisis, the spotlight has focussed on accounting for financial instruments. In early 2009, a meeting of the Group of Twenty (G20) finance ministers and central bank governors called on international standard-setters to improve accounting standards on valuation and impairment, and to reduce the complexity of accounting standards for financial instruments.

Since 2005, the IASB and the FASB have had a long-term aim to improve and simplify the reporting for financial instruments. In response to the G20 recommendations, the two boards have announced an accelerated timetable for replacing their financial instruments standards.

The project to replace the current financial instruments standard (IAS 39/AASB 139 *Financial Instruments: Recognition and Measurement)* has been split into three phases.

- Classification and measurement: AASB 9 *Financial Instruments* was issued in Australia in December 2009 and deals with the classification and measurement of financial assets only. For financial liabilities, the standard setters decided to retain the existing requirements for classifying and measuring financial liabilities, except those that are measured under the fair value option. An exposure draft containing proposals for how gains and losses on liabilities designated under the fair value option should be presented in the statement of comprehensive income was released in May 2010, with comment period closing in July 2010.
- Impairment of financial assets: ED 189 *Financial Instruments: Amortised Cost and Impairment* was released in November 2009 and was closed for comment in June 2010.
- Hedge accounting: the standard setters expect to issue an exposure draft on hedge accounting in the second half of 2010.

AASB 9, as issued in December 2009, will be expanded with additional chapters as each phase is completed. It is expected that by mid 2011, AASB 9 will be a complete replacement of AASB 139 *Financial Instruments: Recognition and Measurement*.

5.3.5 Accounting for leases

In March 2009, the IASB and the FASB released a discussion paper proposing to eliminate the distinction between finance and operating leases, and requiring all leases to be recognised on the balance sheet. If the proposals are implemented, the assets and liabilities on the AFR balance sheet would increase by around $10.5 billion.

Both the comprehensive operating statement and the balance sheet are likely to become more volatile following the introduction of the proposals, due to valuation adjustments to the leased assets and liabilities.

The proposal will also require agencies to review their controls and processes to facilitate proper management and accounting of all lease agreements, including the periodic reassessment and documentation of lease terms, contingent rentals and residual value guarantees at each reporting date.

The IASB intends to issue an exposure draft on lease accounting in the second half of 2010 and a final standard in 2011 for implementation in 2013.

Appendix A. Acronyms and glossary

Acronyms

AAS	Australian Accounting Standards
AASB	Australian Accounting Standards Board
AFR	Annual Financial Report for the State of Victoria
DIIRD	Department of Innovation, Industry and Regional Development
DOH	Department of Health
DOJ	Department of Justice
DOT	Department of Transport
DSE	Department of Sustainability and Environment
DTF	Department of Treasury and Finance
ED	Exposure Draft
EFT	Electronic Funds Transfer
FASB	United States Financial Accounting Standards Board
FMA	*Financial Management Act 1994*
FRD	Financial Reporting Direction
FRSB	New Zealand Financial Reporting Standards Board
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standards
IPSASB	International Public Sector Accounting Standards Board
GAAP	Generally accepted accounting principles
GFS	Government Finance Statistics
GGS	General Government Sector

IT	Information Technology
PACCER	Procurement and Contracting Centre for Education and Research
The bill	Public Finance and Accountability Bill
VAGO	Victorian Auditor-General's Office
VGPB	Victorian Government Purchasing Board
VicRoads	Roads Corporation
Victrack	Victorian Rail Track Corporation

Glossary

Accountability

Responsibility on public sector entities to achieve their objectives, with regard to reliability of financial reporting, effectiveness and efficiency of operations, compliance with applicable laws, and reporting to interested parties.

Asset

A resource controlled by an entity as a result of past events, and from which future economic benefits are expected to flow to the entity.

Asset useful life

An asset's useful life is the period over which it is expected to provide the entity with economic benefits. Depending on the nature of the asset, the useful life can be expressed in terms of time or output.

Auditor's opinion

Positive written expression within a specified framework indicating the auditor's overall conclusion on the financial report based on audit evidence obtained.

Capital expenditure

Amount capitalised to the balance sheet for contributions by a public sector entity to major assets owned by the entity, including expenditure on:

- capital renewal of existing assets that returns the service potential or the life of the asset to that which it had originally
- capital expansion which extends an existing asset at the same standard to a new group of users.

Depreciation

The apportionment of the capital value of an asset over its expected useful life. The amount of depreciation expensed takes account of normal usage, obsolescence or the passage of time.

Entity

Is a body whether corporate or unincorporated that has a public function to exercise on behalf of the state or is wholly owned by the state, including departments, statutory authorities, statutory corporations and government business enterprises.

Equity or net assets

Residual interest in the assets of an entity after deduction of its liabilities.

Expense

Outflows or other depletions of economic benefits in the form of liabilities incurred or depletion of assets of the entity, other than those relating to contributions by owners, that result in a decrease in equity during the reporting period.

Fair value

The amount for which a financial or non-financial asset could be exchanged between knowledgeable and willing parties in an arm's-length transaction.

Financial delegation

A schedule that specifies the level or approval required for each transaction category to facilitate the execution of functions necessary for the efficient operation of the entity.

Financial instrument

A contract that represents a financial asset of one party and a financial liability or equity instrument of another party.

Financial report

Structured representation of the financial information, which usually includes accompanying notes, derived from accounting records and intended to communicate an entity's economic resources or obligations at a point in time or the changes therein for a period in accordance with a financial reporting framework.

Financial sustainability

An entity's ability to manage financial resources so it can meet spending commitments, both at present and into the future.

Financial year

A period of 12 months for which a financial report is prepared.

General government sector

The GG sector comprises all government departments, offices and other bodies engaged in providing services free of charge or at prices significantly below their cost of production. General government services include those which are mainly non market in nature, those which are largely for collective consumption by the community, and those which involve the transfer or redistribution of income. These services are financed mainly through taxes, other compulsory levies and user charges.

Internal controls

Processes effected by an entity's structure, work and authority flows, people and management information systems, designed to assist the entity accomplish specific goals and objectives. Internal control is a means by which an entity's resources are directed, monitored and measured. It plays an important role in preventing and detecting error and fraud and protecting the entity's resources.

Liability

A present obligation of the entity, arising from past events, the settlement of which is expected to result in an outflow of resources from the entity.

Materiality

Information is material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial report. Materiality depends on the size of the item or error judged in the particular circumstances of its omission or misstatement. Thus, materiality provides a threshold or cut-off point rather than being a primary qualitative characteristic which information must have if it is to be useful.

Non-reciprocal

Transfers in which an entity receives assets without directly giving equal value in exchange to the other party to the transfer.

Public sector entity

A department; a local government; a statutory body; an entity controlled by one, or more than one, department, local government or statutory body or by a combination of departments, local governments and statutory bodies; or an entity controlled by an entity that is a public sector entity.

Qualification

A qualification is issued when the auditor concludes that an unqualified opinion cannot be expressed due to one of the following reasons:

- disagreement with those charged with governance
- conflict between applicable financial reporting frameworks
- limitation of scope.

A qualified opinion shall be expressed as being except for the effects of the matter to which the qualification relates.

Revenue

Inflows or other enhancements or savings in outflows of service potential, or future economic benefits in the form of increases in assets or reductions in liabilities of the entity, other than those relating to contributions by owners which results in an increase in equity during the reporting period.

Risk

The chance of a negative impact on the objectives, outputs or outcomes of the entity.

Unqualified audit opinion

An unqualified audit opinion is an expression by the auditor stating that the entity has followed all accounting rules appropriately and that the financial report is an accurate representation of the entity's financial condition. Also referred to as a clear audit opinion.

Appendix B.

Audit Act 1994 section 16—submissions and comments

Introduction

In accordance with section 16(3) of the *Audit Act 1994* a copy of this report, or relevant extracts from the report, was provided to all relevant entities with a request for comments or submissions.

Of the 11 portfolio departments and CenITex who were afforded the opportunity to provide comments or submissions, the departments of Health, Primary Industries, and Sustainability and Environment, did not consider it necessary to provide any comments or submissions. At the time of finalisation of the report, after expiration of the five day statutory time frame no response had been received from the departments of Education and Early Childhood Development, Human Services, and Premier and Cabinet.

The comments and submissions provided for publication by the other five departments and CenITex follow. These comments and submissions are not subject to audit nor the evidentiary standards required to reach an audit conclusion. Responsibility for the accuracy, fairness and balance of those comments rests solely with the agency head.

Submissions and comments received

RESPONSE provided by the Deputy Secretary, Corporate Services and Development, Department of Innovation, Industry and Regional Development

Department of
Innovation, Industry and Regional Development

121 Exhibition Street
Melbourne, Victoria 3000
GPO Box 4509
Melbourne, Victoria 3001
Australia
Telephone: (03) 9651 9999
Facsimile: (03) 9651 9129

Mr Pearson
Auditor-General
Victorian Auditor-General's Office
Level 24
35 Collins Street
Melbourne Vic 3000

Dear Mr Pearson,

RE: PORTFOLIO DEPARTMENTS: INTERIM RESULTS OF THE 2009-2010 AUDITS

The Department has reviewed the draft report into Portfolio Departments: Interim Results of the 2009-2010 Audits and takes the opportunity to make the following comments on the proposed audit report.

As there is no specific mention of this Department, I am unable to confirm the accuracy and fairness of the facts represented in the report.

However, the Department supports the recommendations listed on page viii of the report concerning internal control weaknesses, declarations of interest, procurement and the financial reporting framework.

Yours sincerely

ROB BARR
Deputy Secretary, Corporate Services and Development

Victoria
The Place To Be

RESPONSE provided by the Secretary, Department of Justice

Department of Justice

Secretary

121 Exhibition Street
Melbourne Victoria 3000
GPO Box 4356
Melbourne Victoria 3001
Telephone: (03) 8684 0500
Facsimile: (03) 8684 0525
penny.armytage@justice.vic.gov.au
www.justice.vic.gov.au
DX 210077

Our ref: CD/10/286767

Mr DDR Pearson
Auditor-General
Level 24 35 Collins Street
MELBOURNE VIC 3000

Des
Dear ~~Mr Pearson~~

PROPOSED AUDIT REPORT - *PORTFOLIO DEPARTMENTS: INTERIM RESULTS OF THE 2009-10 AUDITS*

Thank you for your letter of 9 July 2010 enclosing the above proposed audit report.

I can confirm that I am satisfied with the accuracy and fairness of the facts and context represented in the report and I welcome the recommendations contained within.

Yours sincerely

PENNY ARMYTAGE
Secretary

Victoria
The Place To Be

RESPONSE provided by the Secretary, Department of Planning and Community Development

Department of Planning and Community Development

1 Spring Street
Melbourne Victoria 3000
GPO 2392
Melbourne Victoria 3001
Telephone: (03) 9208 3333
Facsimile: (03) 9208 3680
DX 210292

Ref CSEC001895

Mr D D R Pearson
Auditor-General
Victorian Auditor-General's Office
Level 24, 35 Collins Street
MELBOURNE VIC 3000

Dear Mr Pearson

PROPOSED AUDIT REPORT - PORFOLIO DEPARTMENTS: INTERIM RESULTS OF THE 2009-10 AUDITS

Thank you for providing a copy of the proposed audit report *Portfolio Departments: Interim Results of the 2009-10 Audits* and an opportunity to provide formal comment.

The report offers useful findings for the portfolio departments and we agree with the accuracy and fairness of the facts and context represented in the audit report.

Should you require further information, please contact Simone Reichstein, Director Corporate Strategy on 9208 3718 or via email simone.reichstein@dpcd.vic.gov.au.

I look forward to receiving the final report.

Yours sincerely

Yehudi Blacher
SECRETARY

Victoria
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RESPONSE provided by the Secretary, Department of Transport

Department of Transport

PO Box 2797
Melbourne, Victoria 3001
Telephone: (03) 9655 6666
Facsimile: (03) 9095 4096
www.transport.vic.gov.au
DX 210410

Our Ref:

Mr DDR Pearson
Auditor-General
Victorian Auditor-General's Office
Level 24, 35 Collins Street
MELBOURNE VIC 3000

Dear Mr ~~Pearson~~ Des

PROPOSED AUDIT REPORT – 'PORTFOLIO DEPARTMENTS: INTERIM RESULTS OF THE 2009-10 AUDITS'

I refer to your letter dated 9 July 2010, requesting the Department of Transport's (DOT) response to the draft proposed audit report 'Portfolio Departments: Interim Results of the 2009-10 Audits'.

You requested that our response should indicate whether;

1. DOT is satisfied with the accuracy and fairness of the facts and context represented in the report.

   In relation to section 4.3 "The Procurement Process" and the VAGO finding regarding DOT and the probity auditor please see the following comments;

   Government Policy does not mandate the appointment of a probity auditor and advisor enabling departments to make a determination on a case by case basis on whether a probity auditor is required. While DOT appoints a probity auditor in practically all major procurements in this case the project team concluded that due to the lack of complexity a probity auditor was not required. This fact was not included in the findings and in our view would have presented a fairer representation of the situation.

   In section 2.2 "Oversight of outsourced IT provision" VAGO has noted weaknesses in departmental oversight of outsourced IT provision. However to provide the appropriate context in the section there should be a recognition of the fact that CenITex is the Government's mandated outsourced IT provider and while this does not reduce the department's obligations the relationship and management of the outsourcing contract will be different to the relationship with a commercial provider, who provides services on a profit incentive basis.

2. A succinct response for publication in your report, if deemed necessary. The following paragraph is suggested for inclusion in your report;

   In relation to the VAGO finding that DOT needs to improve its procurement process due to the lack of a probity auditor for a contract with a value of $23.8 million, DOT operated within Government guidelines that do not mandate the use of a probity auditor but require an assessment to be made as to whether a probity auditor is warranted considering the complexity and cost of the procurement. In this particular case it was determined that a probity auditor did not need to be engaged.

RESPONSE provided by the Secretary, Department of Transport – continued

Should you have any queries regarding this matter please contact Fred Cilia, Director Financial Operations at DOT on 9655 6657.

Yours sincerely

Jim Betts
Secretary

16 / 7 / 10

cc: Simon Bohan, Director, via email at PSAControls10@audit.vic.gov.au

RESPONSE provided by the Secretary, Department of Treasury and Finance

Department of Treasury and Finance

1 Treasury Place
GPO Box 4379
Melbourne Victoria 3001
Telephone: (03) 9651 5111
Facsimile: (03) 9651 2062
DX 210759

Mr Des Pearson
Auditor-General
Victorian Auditor-General's Office
Level 24, 35 Collins Street
MELBOURNE VIC 3000

Des
Dear ~~Mr Pearson~~

REPORT ON PORTFOLIO DEPARTMENTS: INTERIM RESULTS OF THE 2009-10 AUDITS

Thank you for the opportunity to provide formal comments on the proposed Auditor-General's Report *Portfolio Departments: Interim Results of the 2009-10 Audits*, prior to its finalisation and transmission to Parliament in late July 2010.

I would like to make the following formal response to 2 of the recommendations made in this proposed audit report, for inclusion in the final report to be tabled in Parliament.

I am pleased to note the Auditor-General's assessment that all portfolio departments operate adequate internal controls to assure the reliability of their financial reporting, the efficiency and effectiveness of their operations and their compliance with all relevant laws and regulations, However, there are a number of areas where more can be done to further strengthen controls. Further comment on these is provided below.

I am also pleased to advise that DTF has taken a proactive approach to strengthening policy and guidance, particularly in the areas where it has policy responsibility, such as procurement and IT security. We will continue to work to progress opportunities to improve current frameworks and guidance.

Recommendation:

The Victorian Government Purchasing Board should develop guidance on the criteria for identifying 'high risk', 'high value' and 'complex' procurement and all portfolio departments should adopt this in their procurement policies.

The Victorian Government Purchasing Board (VGPB) has committed to a program of implementing extensive procurement reform in 2010-11 across the whole-of-government sector. This reform program is based on the development of several key principles which includes assessing the complexity of the procurement activity.

To ensure that the application of this revised procurement process is undertaken consistently across the sector, it is intended that these principles will be prescribed within the proposed Ministerial Directions mandated by the Public Finance and Accountability Bill which is currently being considered by Parliament, and supported by detailed instructions and guidance material to aid in good practice.

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

Recommendation:

The Department of Treasury and Finance should require all public sector entities to adopt the shortened annual reporting time frames proposed in the Public Finance and Accountability Bill for the year ending 30 June 2011.

DTF has been a long term advocate of shortened annual reporting timeframes, as supported by the proposals in the Public Finance and Accountability Bill, which is currently being considered by Parliament. The timing for the adoption of such a reporting framework will be a decision for the Government of the day.

With regard to the broader content of the proposed report, I wish to seek your consideration of a number of amendments to improve the context and accuracy of the proposed report.

1. **Financial reporting framework**

   - The paragraph beginning *'While eligible entities may early adopt the standards...'* on page 31 should be amended to read as follows:

     'While eligible entities may early adopt the standards, DTF has not mandated early adoption as it is considering the implications of reduced disclosures within the context of the Public Finance and Accountability Bill'.

   - The last sentence of the second paragraph on page 32 should end at 'special purpose financial statements'. The remaining part of this sentence should be deleted as it implies that Category 4 bodies would be required to apply this financial reporting framework under the *Public Finance and Accountability Bill.*

2. **Chapter 5, page 29 – Figure 5A: Reporting requirements under the *Public Finance and Accountability Bill* 2009**

   - Departments are not deemed to be 'public bodies', and therefore should not be classed within the 'category framework' prescribed within the *Public Finance and Accountability Bill*. Therefore, the heading *'Category 1'* should read *'Departments and Category 1'* to better reflect this differential intent.

   - Furthermore, 2 references are made to the term *'public sector agencies'* in the body of this table. It is preferable that the term *'public bodies'* is used within this context, as it aligns with the definitions prescribed within the *Public Finance and Accountability Bill.* Consideration could also be given to making correct reference to this term throughout this proposed report.

If you require further information or would like to discuss the contents of this letter, please contact Mr Steve Mitsas, Director, Budget & Financial Management Division on 9651 2645.

Yours sincerely

Grant Hehir
Secretary

RESPONSE provided by the Chief Financial Officer, CenITex

CenITex
CENTRE FOR IT EXCELLENCE

PO Box 2750
Melbourne Victoria 3001
ABN 56 375 109 796

16 July 2010

Mr. DDR Pearson
Auditor-General
Victorian Auditor-General's Office
Level 24
35 Collins Street
Melbourne, Victoria 3000

Dear Mr Pearson,

With respect to the comments in your letter dated 9 July 2010 regarding CenITex and the management of outsourced arrangements I would like to provide the following response:

1. The second point in Section 2.3 should be changed from impacting six portfolio departments to only four. It should also be pointed out that these are customer applications hosted by CenITex and the relevant portfolio departments must request and approve the increased security controls prior to implementation. In this instance the relevant portfolio departments have subsequently deferred their decision to approve/reject the change order until 31 August 2010.
2. Excepting the above change I am satisfied with the accuracy and fairness of the remainder of the report.
3. Please also add the following response:

   CenITex provides hosting services for the business applications of our customers. This includes provision of advice and recommendations for appropriate security controls for the business applications but the customer ultimately decides on the level of security controls that will be configured and maintained.

Yours sincerely

Brett McKellar
Chief Financial Officer

CC: Simone Bohan (VAGO), Peter Blades, Graeme Bowker

CenITex
CENTRE FOR IT EXCELLENCE

Victoria
The Place To Be

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Auditor-General's reports

Reports tabled during 2010–11

Report title	Date tabled
Portfolio Departments: Interim Results of the 2009–10 Audits (2010–11:1)	July 2010

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VAGO

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