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Government
of South Australia

Report

of the

Auditor-General

Annual Report

for the

year ended 30 June 2011

Tabled in the House of Assembly and ordered to be published, 18 October 2011

First Session, Fifty-Second Parliament

Part A: Audit overview

By Authority: B. Morris, Government Printer, South Australia

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30 September 2011

The Hon R K Sneath, MLC
President
Legislative Council
Parliament House
ADELAIDE SA 5000

The Hon L R Breuer, MP
Speaker
House of Assembly
Parliament House
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Dear President and Speaker

Report of the Auditor-General: Annual Report for the year ended 30 June 2011

Pursuant to the provisions of the *Public Finance and Audit Act 1987*, I herewith provide to each of you a copy of my 2011 Annual Report. This Report includes the Honourable the Treasurer's Statements for the financial year ended 30 June 2011.

Content of the Report

This Report is in three parts – Part A, Part B and Part C.

Part A – Audit overview contains a summary of certain matters of importance regarding the audit program of work conducted at public sector agencies for 2010-11. More detailed comment on these matters is made in Part B – Agency audit reports.

Part B – Agency audit reports (Volumes 1 to 5) contains comment on the operations of individual public authorities, the financial reports of those public authorities, and the Treasurer's Statements. A number of matters in Part B of this Report that, in my opinion, are of administrative and/or financial management importance to the Government and the Parliament are listed separately under the heading 'References to matters of significance'. This list can be found immediately after the table of contents in the front of Volumes 1 to 5 of Part B.

Part C – State finances and related matters presents a general review, and report on the public finances of the State.

Auditor-General's Annual Report

In accordance with subsection 36(1)(a) of the *Public Finance and Audit Act 1987*, and subject to comments made within this Report, I state that in my opinion:

(i) the Treasurer's Statements reflect the financial transactions of the Treasurer as shown in the accounts and records of the Treasurer for the financial year ended 30 June 2011

(ii) the financial statements of each public authority reflect the financial transactions of the authority as shown in the accounts and records of the authority

(iii) the controls exercised by the Treasurer and public authorities in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities, is sufficient to provide reasonable assurance that the financial transactions of the Treasurer and public authorities have been conducted properly and in accordance with law.

Whilst I have not seen fit to express a qualified opinion with respect to matters referred to in subsection 36(1)(a)(i) above, I emphasise that there are agencies whose financial statements had not been finalised and the audits were continuing at time of preparing this Report. The agencies are:

- Attorney-General's Department
- Department of Health
- Land Management Corporation
- South Australian Country Fire Service
- South Australian Fire and Emergency Services Commission
- South Australian Metropolitan Fire Service
- South Australian State Emergency Service.

Each of the agencies has balances included in the Treasurer's Statements as at 30 June 2011. Should matters arise in finalising the audits of those agencies, there may be consequential affects to their balances reported in Treasurer's Statements.

Further, whilst I have not seen fit to express a qualified opinion with respect to matters referred to in subsection 36(1)(a)(iii) above, there have been cases where in some agencies, systems of internal controls have not, in my opinion, been of an acceptable standard. Where this has occurred I have, in accordance with the provisions of subsection 36(1) of the *Public Finance and Audit Act 1987*, drawn attention to this fact and included comment on my reason(s) in the report on the agency concerned in Part B of this Report.

Report and assessment of controls

As required by subsection 36(1)(a)(iii) of the *Public Finance and Audit Act 1987*, the audit included an assessment of the controls exercised by the Treasurer and public authorities in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities and also, where applicable, whether the controls in operation were consistent with the Treasurer's Instructions with particular focus on TIs 2 and 28. The overall aim of that assessment was to establish whether those controls were sufficient to provide reasonable assurance that the financial transactions have been conducted properly and in accordance with the law.

It is not practical in any such assessment to review each and every control in respect of each and every transaction. Whilst every effort is made to test the sufficiency of controls across a representative range of transactions, it must be remembered that no system of control is 'fail-safe'.

The Parliament has recognised this in stating that the controls need only be sufficient to provide, at the time of audit, 'reasonable assurance' of the matters set out in subsection 36(1)(a)(iii).

The audit assessment has been made by reviewing the adequacy of procedures and testing a number of control components against a range of financial transactions conducted at various levels of the organisation.

In assessing the sufficiency of these controls, particular regard has been had to the organisation's structure, risk and the interrelation of policies, procedures, people, management's philosophy and operating style, demonstrated competence, and overall organisational ethics and culture. All of these matters serve as interrelated elements of control.

The standard by which I have judged the sufficiency of controls is whether and how well those controls provide reasonable assurance that financial transactions of the Treasurer and public authorities have been 'conducted properly and in accordance with law'. This concept requires the organisation to meet the standards of financial probity and propriety expected of a public authority and, at all times, discharge its responsibilities within the letter and spirit of the law, both in terms of its own charter and as an instrumentality of government discharging public functions.

Except for the matters detailed for each agency in Part B of my Report under the section 'Audit findings and comments', I formed the opinion that the controls exercised in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities were sufficient to provide reasonable assurance that the financial transactions were conducted properly and in accordance with the law. In respect of those matters where the controls exercised were not sufficient to provide that level of assurance, I have made recommendations as to where improvements are required.

Modified Independent Auditor's Reports

For the financial year ended 30 June 2011 modified opinions were expressed on the financial report of the following agencies:

- Adelaide Festival Centre Trust
- Department of Environment and Natural Resourcese
- The Legislature
- Local Government Finance Authority of South Australia
- South Australian Motor Sport Board
- Department for Transport, Energy and Infrastructure
- University of South Australia
- Department for Water.

In addition, without qualification to the WorkCover Corporation of South Australia's Independent Auditor's Report, the report drew attention to the inherent uncertainty associated with the outstanding claims liability reported at 30 June 2011.

In all cases where a modified opinion is given, the Independent Auditor's Report includes explanatory paragraphs clearly describing the reason for issuing a modified opinion. Further the reason for issuing a modified opinion is described in the commentary on each of those agencies in Part B of this Report.

Acknowledgments

I would again like to sincerely thank my staff for their dedicated efforts throughout the year. Their professionalism and dedication have been of the highest order and is reflected in the content of this Report.

In addition I extend my thanks to the Under Treasurer, Government Publishing SA, and their staff, and the report printing coordinator, Mr D O'Keefe, for their efforts which have assisted materially in the production of this Report. The cooperation of all public authorities with my staff during the financial year is also acknowledged.

Yours sincerely

S O'NEILL
AUDITOR-GENERAL

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Audit overview

Introduction

The 2011-12 Budget reinforces the requirement for public sector agencies to realise the significant budget savings measures set in the 2010-11 Budget.

In last year's Report I mentioned that public sector agency chief executives and senior management will need to ensure that their respective agency governance and accountability structures meet the responsibilities of focus on service delivery for the public and the prudent and accountable use of resources. This is a real and continuing challenge particularly when central administration and support areas are required to achieve a greater proportion of the savings to reduce the impact on the provision of government frontline services.

The annual audits of agencies are planned and conducted in the knowledge of the budget settings and their implications for agencies while at the same time, meeting the statutory audit responsibilities of the *Public Finance and Audit Act 1987*. Certain important observations that have resulted from the 2010-11 audits of the public accounts, including the financial accounts and operations of public sector agencies, are principally provided in this audit overview and in the agency reports in Part B of this Report.

The audit program and process

New audit methodology

This has been a year of major change for our audit practice. For some time the Auditor-General's Department has been working towards the implementation of a new audit methodology and associated software. After extensive research, testing and planning the new audit methodology IPSAM (Integrated Public Sector Audit Methodology), developed by the Victorian and Queensland state audit offices, was implemented across the Department's auditee agency portfolio (approximately 150 auditee agencies).

IPSAM is integral to the performance of the annual audit process applied to agencies, in particular the conduct of the financial and compliance audits (control and financial statement audits) of public sector agencies. It is widely used by public sector audit offices across Australia, which provides the Department with a long-term commitment to the product and its development.

The implementation task was significant, requiring priority resource effort and commitment from all staff members of the Auditor-General's Department. They demonstrated their true professionalism and I am grateful for their efforts. The last full methodology replacement occurred 10 years ago and the implementation took two years to apply to all agency audits. This year IPSAM was applied to all audits in the first year of implementation.

The priority focus on IPSAM implementation limited scope of progress in 2010-11 towards increasing audit activity on special focus reviews. Having successfully implemented IPSAM for the 2010-11 interim and year end audits, certain reviews are now underway.

Audit management letters

Last year's Report referred to the important matter of audit management letter communications to agencies advising the results of audits of agencies' operations. The audit management letter is provided to the officers charged with governance responsibility for the particular agency (Board Chair, Chief Executive, senior executives).

As stated last year, these letters raise with the agencies weaknesses in financial management, accounting and control identified during the audit process, and include recommendations for consideration and improvement in agency systems, processes and controls. These letters also request a responses from the agencies with advice of remedial action proposed or to be taken in relation to the matters raised by Audit.

It is my expectation that should an agency's response indicate remedial actions for matters raised by Audit, then those actions would be implemented and reviewed periodically within the agency for operating effectiveness.

I advised last year that agencies were generally responding in a satisfactory manner to the audit management letters. However, there was an upward trend of instances where some responses in agencies' letters indicating corrective action had not in fact been taken or was delayed.

That upward trend noted last year has not diminished. Audit commentaries for agencies in Part B of this Report evidence instances of intended corrective actions to matters identified in 2009-10 noted as unresolved during the 2010-11 audit.

It is my intention during 2011-12 audits to gain an understanding of the factors giving rise to this situation (for example, staff resourcing, staff turnover, system changes).

The public finances

Estimated results for 2010-11

The 2010-11 Budget was based on a partial recovery of the previously predicted decline in revenues following the global financial crisis, due to improved economic conditions and upward revisions to Commonwealth grants. A deficit was forecast for 2010-11, primarily due to the nature and timing of Commonwealth grants and expenditure carryovers into 2010-11. The budget was then expected to return to operating surpluses for the remainder of the forward estimates.

The 2011-12 Budget Papers show the operating result for 2010-11 is estimated as a net operating balance deficit of $427 million compared to the budgeted deficit of $389 million. The variation is principally due to lower than budgeted grant revenues and higher than estimated interest expenses.

The net lending deficit is estimated to be $1821 million, compared to the budgeted $1791 million, the difference being due to the decline in the net operating balance result. The general government sector is estimated to have net debt of $3217 million at the end of 2010-11, $118 million lower than was budgeted.

Investment market conditions through 2010-11 contributed to increases in the market value of investment assets. The Superannuation Funds Management Corporation of South Australia, which manages the majority of the Government's financial assets, reported net income of $1.6 billion compared to $1.5 billion in 2009-10. As the managed funds include superannuation assets, this result will contribute to managing the unfunded superannuation liability.

Unfunded superannuation liabilities are estimated to be $8.7 billion for the year to 30 June 2011, an improvement on the 2010-11 budgeted expectation of $9.4 billion. The improvement is mainly due to the following:

- Unfunded superannuation liabilities are valued at points in time by discounting future superannuation benefit payments by the prevailing discount rate that reflects the risk-free interest rate. As the rate rises the value of the liability reduces. A discount rate of 5.6 percent was used for the estimate as at the 2011-12 Budget, compared with 5.3 percent for the 2010-11 Budget.

- Improvement in returns from investment markets. The assumed earnings rate for 2010-11 of 12.9 percent compares to the long-term assumption of 7 percent used in the 2010-11 Budget.

The Government reports that it remains committed to fully fund the superannuation liability by 2034.

Positive market returns and an improved underwriting result contributed to the Motor Accident Commission reporting a comprehensive profit result for the year of $193 million, up from $168 million. The Commission's statutory solvency level, calculated in accordance with a formula determined by the Treasurer, improved to 103.6 percent (97.1 percent) of the target level of solvency. As at 30 June 2011 the Commission had net assets of $431 million ($239 million). WorkCover Corporation of South Australia (WorkCoverSA), which manages its own investments, reported a profit in 2010-11 of $30 million ($77 million). This contributed to an improvement in its funding ratio to 64.8 percent from 61.5 percent, compared to its approved target funding range of 90 to 110 percent. As at 30 June 2011 WorkCoverSA had a net liability position of $952 million ($982 million).

Budget forecasts 2010-11 to 2013-14

An operating deficit of $263 million is now budgeted for 2011-12 compared to a surplus of $55 million estimated at the time of the 2010-11 Budget. Operating surpluses are projected from 2012-13 although at lower levels than in the previous budget.

The elements that have changed and cause the budgeted deficit for 2011-12 are:

- total revenue is budgeted to be $200 million more than previously estimated for 2011-12, essentially from increased Commonwealth grants

- total expenses are $522 million higher than estimated in the previous budget. Employee expenses, up $84 million, other operating expenses, up $173 million, and grants, up $200 million, are the key changes.

The 2011-12 Budget contains new expenditure and offsetting savings initiatives in the general government sector totalling $477 million over the next four years. This comprises new operating and investing initiatives of $515 million and operating savings of $38 million.

Setting large savings targets is a feature of past Budgets. The 2010-11 Budget consolidated savings announced in earlier budgets (of over $700 million per annum by 2013-14) and new savings totalling $1.5 billion over the four years to 2013-14 arising from the recommendations of the Sustainable Budget Commission.

For 2010-11, the Department of Treasury and Finance (DTF) advised that generally agencies achieved their allocated savings targets. The largest exception was in Health which had a $10.9 million shortfall relating to an unachieved outpatient services reforms measure. A range of methods were applied to achieve savings. Agencies utilised the Government's target voluntary package separation (TVSP) scheme to achieve 381 full-time equivalent (FTE) reductions during the period 1 November 2010 to 30 June 2011. Agencies also held vacant positions to offset budget pressures while others managed through reductions in other expenditure lines rather than FTE numbers. Actual FTEs of 77 808 were reported as at 30 June 2011 for all portfolios, which was within the cap of 78 596.

There remains in excess of $1.8 billion of new and existing savings to be achieved for the three years to 2013-14 together with savings measures announced in the 2011-12 Budget. The Department of Health (DoH) has the largest individual agency savings target with remaining 2010-11 new savings for the three years to 2013-14 of $298 million.

As noted last year an inherent risk of the savings strategy is its sheer size and breadth. Achieving the task will require significant discipline. Agencies have developed experience with implementing savings strategies over recent years but the savings targets are not always achievable by all agencies. As indicated, DTF has reported that agencies achieved most of the 2010-11 targets. The remaining savings task is of a much greater scale with savings in the order of $430 million expected in 2011-12. It presents risks including industrial action and public demand to maintain services. Implementing savings tends to be directed at administrative and support areas for services. Care needs to be taken that where this occurs, relevant changes to systems and procedures within a risk management context are addressed, to ensure the public interest is continually served by efficient and effective administrative performance and failures avoided.

Net lending

A net lending deficit of $1.3 billion is budgeted for 2011-12 and the budget is not projected to return to net lending surplus until 2014-15, a year later than previously forecast. The 2011-12 Budget continues a large capital spending program estimated to be $2.1 billion in 2011-12. Capital projects are being delivered through both direct publically delivered projects but also in partnership with the private sector.

In June 2011 the Government announced financial close on a public private partnership contract to build, operate and maintain the new Royal Adelaide Hospital (RAH). The total capital cost of the new hospital at contractual close was $2.09 billion. The current forward estimates to 2014-15 do not recognise the completion of the new RAH and the commencement of its annual service payments as they are scheduled to occur in 2015-16. The Government has also committed grant expenditure of $535 million to redevelop the Adelaide Oval. The size and complexity of the capital program presents a continuing heightened risk to the proper management and control of capital projects.

Asset sales are also a prominent feature of the 2011-12 Budget. Total budgeted asset sales for the non-financial public sector exceed $1.3 billion in 2011-12 and are estimated at $871 million in 2012-13. The budget now incorporates two significant asset realisation processes. These are the forward sale of up to three harvest rotations for South Australian Forestry Corporation plantations and a proposed sublicence giving the right to operate the Lotteries Commission of South Australian's brands and business for a defined period of time. Both sales will need appropriate competitive sale processes incorporating relevant expertise to maximise the realised value of these public assets.

Net debt

To support the net operating deficits for 2010-11 and 2011-12, and to fund the Government's capital investment program across the forward estimates, net debt is budgeted to climb to $4213 million by 2013-14. If the aims of this budget are achieved over the next four years, the estimated result for 2014-15 is an operating surplus of $655 million, the highest result reported since the Government Financial Statistics (GFS) budget methodology was adopted in 2002-03. The Government is seeking the significant operating surplus forecast for 2014-15 to provide an essential buffer for the impact of the new RAH lease liability which will be recognised for the first time in 2015-16 when it is expected to add $2.8 billion to net debt.

Budget monitoring and reporting

Audit has expressed a view of the fundamental importance of budget monitoring and reporting processes in past Reports. Audit made inquiries of specific monitoring measures for the 2011-12 Budget. DTF advised that, in addition to a regular monitoring regime, given the magnitude of the budget improvement measures and the importance of achieving the measures, an enhanced monitoring process was introduced in 2010-11 to monitor the progress of agencies in achieving their budget improvement measures and FTE reductions. DTF indicated both regular and enhanced monitoring processes will continue in 2011-12.

Concluding comments

There are a number of significant challenges to achieving the 2011-12 Budget. There is continuing and significant uncertainty in global economic climate which may threaten revenue projections. Budgeted expenditure restraint has risks both in the size and by its nature. There is an ongoing large and diverse capital projects program.

These circumstances emphasise the importance of a high degree of government management discipline supported by effective reporting and monitoring. Audit intends to review certain aspects of the budget monitoring and reporting process, in 2011-12.

Part C of this Report

More detailed commentary and audit observations on aspects of the State's finances are presented in Part C of this Report. That commentary includes observations on the Treasurer's Financial Statements, prepared pursuant to the *Public Finance and Audit Act 1987* to report on transactions and balances in the public accounts.

The main public accounts are the Consolidated Account, Special Deposit Accounts and Deposit Accounts established pursuant to the *Public Finance and Audit Act 1987*.

Financial reporting obligations of government agencies: The important requirements of timely and quality preparation of financial statements

The *Public Finance and Audit Act 1987* requires public authorities to submit their financial statements to the Auditor-General within 42 days of the end of the financial year. I am, in turn, required to deliver my Report, including agencies' audited financial statements, to the President of the Legislative Council and the Speaker of the House of Assembly by 30 September annually.

The timeframe for delivery of my Report imposes tight time constraints on the completion of the audit of agencies' financial statements and the compilation of the Report. While statutory financial reporting time frames have remained unchanged since 1987, the volume of reporting has increased markedly over the years, mainly due to changes in accounting standard reporting requirements but also reflecting an increase in reporting of audit findings and analysis of financial statement information.

In June each year, I write to all chief executives of agencies that have a 30 June financial reporting year. In that letter I set out the statutory timeframes and other requirements for financial reporting. I also set out a range of areas where Audit has identified risks to agencies preparing financial statements of an appropriate standard.

Financial statements of quality to be presented for audit

In my letter for June 2011, I indicated that it was important that chief executives and chief financial officers have processes in place to review the quality of their agency's financial statements prior to their certification and submission to the Auditor-General, to ensure they:

- present information that is consistent with their understanding and expectations
- have notes that are meaningful and succinct
- will assist users to understand the financial status and operations of the agency
- are substantially complete and reliable.

The letter conveyed that where there are issues with the quality of the financial statements, Audit would consider whether the audit of the financial statements could be completed within the strict timeframes for inclusion in this Auditor-General's Annual Report to Parliament. If it was not possible, I would advise the chief executive of this matter and the financial statements would be included in a Supplementary Report to Parliament. I also stated I would comment in this Auditor-General's Annual Report on the status of the statements and that they were to be presented in a Supplementary Report.

Good financial statement preparation and practice

My letter for June 2011 highlighted critical matters that, in Audit's experience, contribute to the preparation of quality financial statements that are readily auditable. They include:

- a planned and structured approach to preparing financial statements

- the officers who prepare the financial statements have appropriate experience and a good understanding of the agency

- officers are available at the time of audit

- supporting documentation is prepared and checked including reconciliations and explanations for major variances.

Over recent years the following recurring factors have caused difficulty to both agencies and Audit staff:

- Draft financial statements submitted within the required timeframe were incomplete or unreliable and were significantly amended during the audit.
- Information required to support the financial statements and complete the audit was not prepared.
- Draft financial statements incorporated errors or misstatements which would have been identified had the statements been quality reviewed before submission.

In the past, where one or more of these factors was evident, the audit of the financial statements was not always completed in time for inclusion in the Auditor-General's Annual Report.

Status of financial statements for 2010-11

The 2010-11 audits of agencies' financial statements gave rise to issues that were similar to past years and included degrees of changes to financial statements from original versions and the availability of timely and quality supporting documentation. This again resulted in significant demands on Audit staff to complete audits and meet reporting deadlines.

This Auditor-General's Annual Report excludes the financial statements and related commentary of a number of agencies that were planned to be included so that Parliament has that information on a timely basis. In each case the audit could either not commence or be completed as scheduled to allow for the inclusion of the financial report in this Auditor-General's Annual Report to Parliament. The audited financial reports for the year ended 30 June 2011 and related commentary for those agencies will be included in a Supplementary Report to Parliament. This has occurred for a range of reasons including:

- the financial report of an agency did not meet the expected quality standard
- issues arising through the implementation of a new financial system and centralising previously regional finance functions while concurrently using existing systems in regional areas
- matters arising during the course of the audit of an agency's financial report that require further work by the agency and Audit
- records and information supporting the financial report not meeting the expected quality standard.

After completing this Report, my Department continues with audits of other agencies, funds and grant certificates not included in the Report. A consequence of unnecessarily prolonged audits of the agencies that would otherwise be included in the Auditor-General's Annual Report is to delay completing these other audits. In turn, delays to the remaining audits reduce the Auditor-General's Department's ability to consider other areas of possible audit risk and risk not meeting statutory timeframes. Each year involves continual assessment of the application of limited audit resources to complete audit responsibilities in the most efficient and effective manner.

It is unavoidable that under current circumstances not all financial reports will be included in the Auditor-General's Annual Report or will meet other statutory timeframes. The quality of financial statements forwarded for audit is integral to the Auditor-General's Department's ability to meet the statutory timeframes with reasonable access to audit resources. I will continue to exercise my judgment where there are issues with the quality of the financial statements of agencies as to whether an audit of the financial statements can be completed within the strict timeframes for inclusion in the Auditor-General's Annual Report.

Financial statements will only be included in the Auditor-General's Annual Report on the basis that Audit has received all necessary information, records and explanations supporting an entity's financial statements.

In my view there continues to be a risk that without improvements in the way some agencies prepare their financial statements, audits will not be completed in time to meet statutory reporting time limits.

Audit will continue to relate with agencies and Shared Services SA (SSSA) in 2011-12 to seek further improvements in processes to support the preparation and audit of public authorities' financial statements.

Agency financial statement disclosures: Employee remuneration: A significant change in disclosure effective from 2010-11

Agency financial statements are general purpose financial statements that are prepared in accordance with relevant Australian Accounting Standards and Treasurer's Instructions and Accounting Policy Statements (APSs) promulgated under the provisions of the *Public Finance and Audit Act 1987*.

In the interest of public accountability and transparency the APSs require that a number of specific note disclosures are included in an agency's financial statements. One of these disclosures relates to the number of employees whose normal remuneration is equal to or greater than a specific amount (within $10 000 bandwidths). Since 1994-95, this specific amount has been set at $100 000.

Amendments to the APSs, effective from 1 July 2010, changed the disclosure threshold for South Australian public sector employee remuneration from $100 000 to the base executive remuneration level. For the 2010-11 financial year, this equated to $130 700. Agencies were also required to update the comparable figures for 2009-10 to reflect the base executive remuneration level applicable for 2009-10 ($127 500).

As a result of the amendments to the APSs, there has been a significant reduction in the number of employees disclosed in the specific note of each agency's financial statements. The impact of the change of accounting policy for each agency is disclosed in the individual agency financial statements contained in Part B of this Report.

Governance and financial control and accountability practices: Improvement always required

Introduction

Previous Reports have included comment on the importance of agency having in place effective governance and financial control and accountability elements and practices for the adequate management and control of public resources.

Important elements and practices for effective governance and financial control and accountability include:

- sound organisational structures
- clearly stated responsibility and authority relationship
- policy and planning
- adequate financial management and accounting systems and records
- risk profiling and assessment and effective control strategies
- monitoring and reporting systems.

Because agencies are continually subject to change (structures, program delivery, staffing, systems) the abovementioned elements and practices need to be often revisited and subject to agency internal review for appropriateness and adequacy.

A properly constructed and the ongoing application of a financial management compliance program (FMCP) can assist an agency's internal assessment of its core financial policies and material areas of financial operation, including systems and processes. An FMCP is a requirement of Treasurer's Instruction 28 which became effective from the 2008-09 financial year.

Agency audits

The Auditor-General is required by the *Public Finance and Audit Act 1987* to assess and give an opinion on the adequacy of internal controls of auditee agencies. Any deficiencies or shortcomings in the abovementioned governance and financial control and accountability elements and practices can result in a qualification (exception) comment to the 'assessment of controls' opinion given for each agency in Part B of this Report.

The 2010-11 'assessment of controls' opinion for many agencies include a qualifying exception comment, that reflects a weakness or control gap, or inappropriate process, or a significant shortcoming, in one or more areas of the abovementioned elements and practices.

A notable matter is that some agencies still have not implemented an effective FMCP.

Concluding comments

Agencies must always commit to revisit their governance and financial control and accountability elements and practices, and make the appropriate changes, so that they are adequate for the management of public resources and delivery of public services.

Audit communications in agency reports in Part B of this Report highlight where practices fall short and need to be addressed by the respective agencies.

In relation to the requirement for agencies to have in operation an adequate FMCP, Audit will include this as a matter of review focus in the financial audit programs for agencies in 2011-12.

The Government shared services initiative: Audit comment on progress of initiative and savings

Introduction

This government initiative has been in operation for three years. Since commencement of the initiative my reports to Parliament have included specific comment on the progress of reform activity and savings associated with the initiative. This section of the Report provides a further update on the initiative.

Nature of the initiative

The initiative involves transferring high volume administrative functions such as payroll, accounts payable, accounts receivable and other services and the related staff to a central service provider, SSSA. The underlying principle for the initiative is to streamline and simplify administrative and technology services bringing significant efficiencies and savings across all government agencies.

The shared services model adopted involves transitioning services from agencies 'as is', with review, reform and improvement of services to follow. The 'as is' transition involves services transitioned in their current state with the current agency employees and systems. Under this model the bulk of service reform and improvement happens after SSSA assumes ownership and responsibility for service provision to agencies.

2010-11 reform activity

During 2010-11 e-Procurement was implemented for agencies (excluding SA Health). This system initiative involved the automation of the purchasing and accounts payable process and is discussed further below under the heading 'e-Procurement reform'.

In December 2010 Cabinet approved:

- proceeding with the transition of information and communications technology (ICT) services (Tranche 4). This tranche includes transition of functions such as ICT user support and client equipment for most agencies; as well as communication, hosting, data and network services for some smaller agencies. Detailed discovery began in 2011 and transitions are expected to take at least 18 months to complete. Once the discovery process is completed further Cabinet approval will be sought for the transition of specific services and resources
- the deferral of the transition of human resource administration (Tranche 3). This tranche has been deferred until after the e-Recruitment initiatives, already under consideration or being progressed in agencies, have been delivered.

SSSA advised that the FTE employees as at 30 June 2011 were 61 in shared services reform and 638 in shared services operations.

Future reform activity

Payroll reform strategy

SSSA has commenced development of a payroll reform strategy and is presently undertaking a business process review. The primary objective of this review is to identify opportunities to improve the functionality, usability and effectiveness of the CHRIS payroll system, which should lead to improved efficiency and effectiveness across payroll teams.

Payroll processes will also be process mapped, with specific recommendations to improve process efficiency. Opportunities for process simplification, improvement and standardisation will be identified.

This project is in the early implementation phase with completion expected in the first quarter of 2012.

Financial services reform strategy

The goals of this project are:

- to establish a clear strategic direction and approach for the reform of the Government's financial services and systems
- developing a high level understanding of agency and internal business requirements in the area of financial services
- determining SSSA's preferred financial system for use in the medium term, based on the extent to which the business requirements can be satisfied and improved efficiency delivered
- to identify a program of initiatives (including a high level benefits analysis) that could be pursued to improve the efficiency of financial services provided by SSSA and potentially the Government as a whole.

This project commenced in March 2011 and SSSA anticipate that a draft strategy will be completed before the end of 2012.

Cost of implementation

On a number of occasions in past years Cabinet was advised that funding provided for the implementation of shared services was not sufficient to allow the full range of business and corporate services, identified as potentially in-scope in October 2007, to be transitioned to SSSA.

Audit has previously reported that significant additional funds in excess of the original $60 million implementation budget would be required to transition all in-scope activities.

The following notable matters have been commented on in previous reports:

- As part of the 2010-11 Budget process, additional implementation funding would be provided to finalise the savings realisation for Tranches 1 and 2. Additional funding of $8.3 million above the original $60 million was budgeted.
- In addition to the implementation funding, SSSA has received funding in past years for the use of Wakefield House and funding has been allocated for every year up to 2013-14. The total of this funding is $15.4 million.

- The cost of implementing the e-Procurement solution by SSSA was estimated to be $23 million over six years. This is additional funding that is not included in the $60 million implementation budget.

SSSA has estimated that the implementation costs to complete the approved implementation activities will be:

	$'million
Implementation funding	60.0
2010-11 budget additional funding	8.3
Wakefield House appropriation	5.0
e-Procurement	30.4
Tranche 4 implementation	10.5
Other	0.2
Total	114.4

Achievement of savings

The shared services initiative was announced in September 2006 in the 2006-07 Budget.

At the time of the 2006-07 Budget, the implementation of shared services arrangements aimed to save $130 million (including savings from Future ICT and associated changes) over four years to 2009-10 offset by implementation costs of $60 million over the same period.

In response to my request to provide details of all savings amounts included in the Budget for the shared services initiative since its announcement, DTF provided the following information.

	*Up to 2009-10 $'000	2010-11 Actual $'000	2011-12 Budget $'000	2012-13 Budget $'000	2013-14 Budget $'000	2014-15 Budget $'000	**Total $'000**
Savings budgeted 2006-07	130 000	60 000	60 000	60 000	60 000	61 500	**431 500**
Less: Savings allocated:							
Future ICT savings	74 120	25 952	26 601	27 266	27 948	28 647	**210 534**
Supply SA warehouses	2 551	1 811	1 417	1 004	1 029	1 055	**8 867**
ICT mobile carriage services	4 786	2 216	2 272	2 329	2 387	2 447	**16 437**
Future ICT implementation cost offset	386	-	-	-	-	-	**386**
Balance of savings	48 157	30 021	29 710	29 401	28 636	29 351	**195 276**
Less: Savings allocated to reform initiatives:							
Tranche 1 services	4 825	2 540	2 629	2 721	2 816	2 886	**18 417**
Financial systems savings	-	700	869	890	912	935	**4 306**
e-Procurement	509	4 507	12 429	16 219	16 589	17 004	**67 257**
Procurement savings	-	2 300	1 333	1 366	1 400	1 435	**7 834**
Tranche 4 savings	-	-	-	-	1 000	3 000	**4 000**
Current balance of savings - shortfall	42 823	19 974	12 450	8 205	5 919	4 091	**93 462**

* Cumulative

As conveyed in my previous Reports, Cabinet has been advised that various factors have meant that savings from shared services will be lower than the original savings factored into the Budget. These factors related to transition delays, reduced employees, accommodation 'dead rent' and potential redeployment costs.

The 'current balance of savings - shortfall' in the table represents the shortfall against original savings budgeted. For example, cumulative savings up to 2009-10 fell $42.8 million short of the original budgeted savings of $130 million. The expectation that savings would not meet original targets was reflected in the 2010-11 Budget, where savings were revised downwards from $60 million for each of the three years 2010-11, 2011-12, and 2012-13. The changed savings targets are:

- 2010-11 – $40.026 million
- 2011-12 – $50.348 million
- 2012-13 – $56.539 million.

A major element of the total savings target is ICT. Agency expenditure budgets were reduced overall by $25 million each year in the 2007-08 Budget to achieve these savings.

Similarly, significant savings estimated to be achieved through the implementation of e-Procurement will be realised through agency budget adjustments.

Audit is advised that the Budget continues to include a contingency to allow for the possibility that savings from shared services are not achieved. This contingency would be an offset to any savings shortfall and would prevent, or at least limit, any adverse impact on the Budget bottom line.

e-Procurement reform

This development represents the first major information systems reform initiative to be undertaken by SSSA to achieve across-government savings. Cabinet approved in August 2009 the acquisition and development of an across-government e-Procurement solution by SSSA at a cost of approximately $23 million over six years. The funding for this project is not included in the $60 million implementation budget.

The e-Procurement solution involves automating the purchasing and accounts payable process and is expected to realise savings in four areas:

- FTE reductions from accounts payable efficiency
- SSSA and agency avoided costs
- sourcing and purchase ordering efficiency
- savings in the cost of goods and services.

Cabinet was advised that from 2012-13 annual savings are expected to be $16 million. A significant proportion of these savings ($10.8 million per annum) is expected to be realised by agencies through savings in the cost of goods and services.

It is noted that the proposal is to phase in the full recoup of these agency savings through agency budget adjustments over a three year period commencing in 2010-11 and then fully on an ongoing basis.

During 2010-11 e-Procurement was implemented for all agencies other than SA Health. SSSA advised that there are now approximately 12 000 users across 28 government agencies accessing e-Procurement.

The achievement of a significant part of the savings each year was dependent on SA Health interfacing e-Procurement with its new Oracle corporate system. The e-Procurement system was scheduled for implementation in Health in July 2010. However, due to changes in the implementation of the Oracle system by SA Health this implementation was delayed. SSSA have advised that there is currently no agreed timeframe for the implementation of e-Procurement in SA Health.

Concluding comments

The expected cost ($60 million) to transition the in-scope activities of agencies to SSSA, as identified in the original Cabinet submission, was significantly underestimated. Further, the revised expected cost of implementing the approved shared services initiatives of $114.4 million does not include all the original in-scope activities (for example human resource administration). SSSA advised that future additional reform activities would be put forward for funding on a business case basis (such as e-Procurement).

The original savings targets will not be met and this was recognised through the downward revision of these targets in the 2010-11 Budget. A significant part of the savings will be realised through agency budget adjustments.

SSSA is at the initial stages of potentially significant reform changes in the payroll and financial services and systems areas. These are the core areas that process the main financial transactions of government. It is important that any changes to systems and processes include the integration of robust and sound internal controls.

Shared Services SA: Some specific comments on the systems and control environment

Introduction

The audit mandate under the *Public Finance and Audit Act 1987* requires an assessment to be made annually of the control environment and specific controls of government agencies. The focus of audit is on the core business (financial) cycles that generate information for inclusion in the financial statements of agencies. The audit, therefore, involves the assessment of controls and testing of financial records and transactions relevant to the core financial cycles.

As the core business cycles were transitioned from agencies to SSSA on an ‘as is’ basis, the services provided by SSSA to agencies form an integral part of the financial records and controls pertaining to the agencies. Due to the differing range of systems, processes and procedures undertaken by SSSA and agencies, the annual audit requires an assessment of these matters (with particular emphasis on controls) at the agency as well as at SSSA.

It is critical that SSSA maintains a strong internal control environment and business cycle system and process controls to ensure the integrity of the daily processing of the financial transactions for around 50 government agencies. In doing so it also needs to ensure that any system and process changes (new or revised) for each core business cycle incorporates sound control attributes.

The following discusses certain matters relevant to SSSA's responsibility of ensuring the soundness of its business cycles and associated systems and processes and control environment to ensure effective and controlled delivery of its service obligations.

Review of the e-Procurement control environment

Cabinet approved the implementation of the across government e-Procurement solution in August 2009. The progressive roll out to other agencies (excluding SA Health) started in April 2010 and was largely completed by the end of February 2011.

The 2010-11 audit of SSSA included coverage of the e-Procurement control environment. The audit focused on the Readsoft (optical invoice and voucher scanning) and Basware (purchase order and invoice processing) processes at SSSA.

Control findings

The review revealed the following important aspects of the control environment had not been fully established:

- Service level determinations were not finalised and signed.
- A number of draft e-Procurement policies and procedures were not finalised, approved and distributed to staff for use.
- Controls to manage user access and delegation profiles for Basware were not implemented.
- Procedures and system reports to enable the regular and timely review of special and super delegations were not implemented.
- Payment data can be altered in Basware after certification and approval by agencies without any (independent) check.
- There was no independent check of the validity of transactions processed by SSSA that bypass the electronic approval by the agencies.

Audit noted at the time of review that SSSA was aware of most of the matters raised and had commenced, or was planning to commence, remedial action.

Further details about the e-Procurement review and related internal audit reviews are provided in the Department of Treasury and Finance section of Part B of this Report to Parliament.

Treasurer's Instruction 8 compliance

In the course of the audit of e-Procurement a matter has come to Audit's attention about the interpretation and application of Treasurer's Instruction 8 'Financial authorisations' (TI 8). TI 8 sets out the financial authorisation provisions that are to be complied with by public authorities. It requires prior financial authorisation (approval) by a person authorised pursuant to TI 8, before the public authority can:

- enter into agreements that have the potential to lead to expenditure or enter into contractual arrangements (including purchases) that incur expenditure

- make a payment or disbursement.

Audit noted some practical difficulties in meeting and evidencing the requirements of TI 8 for separate prior approval at two points in the expenditure (purchase and payment) cycle:

- the incurring of expenditure (commitment of expenditure)
- the making of a payment or disbursement.

The new e-Procurement system arrangement (now involving more automated change in the purchase and payment transaction cycle) has directly influenced the key control activity of financial authorisations (approvals) applied to the purchase and payment transactions of SSSA agencies.

Given the implementation of e-Procurement across government Audit considered it an opportune time for a revisit and review of the specific provisions and operation of TI 8 to:

- clarify the overall intent of the instruction and the separate approvals required

- clarify the application of specific paragraphs

- assess and resolve the practical compliance issues for the new electronic purchasing and payment environment.

Audit is currently addressing this matter with the Under Treasurer and DTF.

Review of electronic funds transfer arrangements

Last year Audit undertook focused reviews of the SSSA electronic funds transfer (EFT) arrangements for selected government agencies.

A number of significant control weaknesses were identified that necessitated remedial action.

Specific details regarding the Audit review and remediation actions taken by SSSA in 2010-11 are provided in the following section of this Report.

Concluding comments

The operations of SSSA are a significant part of the control environment over financial transactions of government agencies. It is important that there is ongoing review and confirmation of the soundness of the control environment.

The processing of payments is a critical component of government operations. It is therefore important that the control environment over e-Procurement is robust at both agencies and SSSA.

The e-Procurement solution was rolled out to most agencies during 2010-11 resulting in a significant change in the way procurement transactions are processed at both SSSA and agencies. Audit review indicates that significant further work was required to achieve a robust control environment. A recent update from SSSA indicated that the majority of audit issues raised had been addressed or would be completed by the end of September 2011.

Electronic funds transfer (payment) systems: An update status: Government exposure to adverse events still remains

Introduction

My last Report made specific comments on significant weaknesses in controls for EFT systems within government agencies. The comments reflected the outcome of a specific program of audit undertaken of these systems for SSSA and other government agencies in 2009-10.

EFT systems have the financial transaction processing capability that enables instantaneous transfer of monies, both in small and large amounts. Without sufficient and continuously maintained controls over EFT systems government is exposed to immediate loss of monies, including through fraudulent activity and malicious behaviour.

The majority of financial processing is now undertaken by SSSA. This results from the transition in recent years of the core financial accounting processing functions of most government agencies to SSSA. As mentioned above, a specific program of audit of EFT systems was undertaken last year. This included testing the strength of controls of EFT payment processing within the SSSA common processing environment. As stated in last year's Report, SSSA did not pass the test, and there were significant weaknesses found that exposed the Government and agencies to loss of monies.

Given the significance of the weaknesses identified and reported to agencies and the Parliament last year, Audit conducted follow-up reviews of remediation action taken by SSSA and agencies to address the weaknesses arising out of the 2009-10 audits.

The following commentary provides the follow-up position status for SSSA and agencies.

Shared Services SA

Electronic funds transfer payment processing environment

SSSA is a business unit of DTF. As noted previously, the majority of EFT financial payment transactions are processed by SSSA on behalf of government agencies.

The EFT payment processing arrangements with agencies were put in place over the last three years and are documented in formal service level determinations between SSSA and the agencies.

The principal common systems used by SSSA for EFT payment processing are the:

- Masterpiece financial system for accounts receivable, accounts payable and general ledger
- CHRIS human resource management system (HRMS)
- EmpowerHR human resource and payroll system
- e-Procurement Basware system for automated payments
- Westpac Corporate Online for EFT.

Last year's review

In 2009-10 Audit completed focused reviews of the SSSA EFT payment processing arrangements for DTF Corporate, the Department of Further Education, Employment, Science and Technology (DFEEST) and the DoH Corporate for the payment of accounts and payroll expenses.

The outcome of these reviews had revealed common weaknesses across the EFT payment processing arrangements, which could be grouped into six general themes, namely:

- user access was insufficiently controlled
- segregation of duties was insufficient
- understanding of user access profiles needed improving
- processing and reconciliation controls needed to be improved
- logging and log monitoring needed to be increased
- policies and processes needed to be updated and/or documented.

In response, SSSA advised that the EFT matters raised would be addressed through an organisational review. The SSSA's remediation approach and remediation status are discussed below.

Shared Services SA remediation approach

SSSA formally advised Audit of its remediation plans in August 2010. SSSA indicated that the majority of matters raised would be addressed by an organisational review to be conducted in two stages.

- Stage one would be to confirm the systems in-scope, document the manner in which access is provided and develop a project plan for Stage two. Finalisation of Stage one was advised as 31 October 2010.

- Stage two was to make change recommendations, including appropriate procedures for access, appropriateness of user profiles, segregation of duties and a review of system administrator activities. Remedial actions would be put in place after the recommendations had been formally considered.

For some other matters raised by Audit, separate completion dates were provided by SSSA.

This year's follow-up review

During 2010-11 Audit maintained regular contact with SSSA on both their remediation approach and progress.

SSSA has altered its initially advised remediation approach and completion timeframes. Reasons provided by SSSA in February 2011 included:

- The remediation project was much broader in its requirements than originally anticipated, which not only impacted SSSA but also a number of other government agencies and external service providers.

- The original user access model was to be re-engineered to a standard user profile/role based approach.

- Some of original timelines proposed in relation to completing formal procedures, revised service level determinations were found not to be achievable.

- There were some initial resourcing issues in recruiting the most appropriate personnel to conduct the remediation project.

In addition, for the CHRIS HRMS, multiple separate databases exist, each with individual system settings and user profiles. Issues like these have added to the complexity of the remediation approach.

Revised Shared Services SA remediation approach

Given the challenges to remediate the EFT issues, SSSA has revisited its remediation approach and resourcing. This has meant that the original remediation timeframes, such as 31 October 2011 for Stage one, will not be achieved.

Remediation of the EFT issues will be now addressed primarily through an internal project called the 'User Access and Controls Project' (the Project). The SSSA Project scope document highlights remediation activities for the previously mentioned SSSA systems. These remediation activities include all user access issues raised in past reports from the Auditor-General, from internal audit reviews and from external reviews contracted by SSSA.

A Project Governance Board, involving the Executive Director, SSSA, will oversee all remediation activities related to the EFT user and access control matters. This includes payroll related issues being separately addressed by the SSSA Payroll Services team.

The revised remediation approach anticipates that all remediation work from matters raised by Audit's 2009-10 specific program of EFT reviews will not be completed until April 2012.

Shared Services SA remediation status underway

In August 2011, SSSA provided Audit with a status update on both the full range of the Project remediation activities, and those activities related to Audit's specific 2009-10 EFT review findings. The latter update related to DTF Corporate, DoH Corporate and DFEEST.

SSSA has categorised the full range of remediation activities raised by SSSA's reviews and reviews by Audit into approximately 80 user access issues. They advised that a significant number of these issues have been fully or partly remediated.

SSSA has categorised issues raised by Audit's specific 2009-10 EFT reviews into over 40 issues. In a general context approximately one half of the issues raised for DTF Corporate and DFEEST have been fully remediated. The other issues have been partially remediated. For DoH Corporate the majority of issues raised have been partially remediated.

As stated above, all remediation activity to adequately address the EFT risks is not expected to be completed until April 2012.

Agency audit reviews

Last year's Report also included specific comment on some individual agency EFT processing arrangements. The Public Trustee was one such agency reviewed.

The 2009-10 review of the Public Trustee identified some issues of a similar nature to those found in the SSSA reviews. The Public Trustee review also identified certain controls in place to reduce the potential for unintentional errors or fraudulent activity.

Audit's follow-up review in 2010-11 indicated that remediation activities proposed by the Public Trustee had been completed. For issues where the Public Trustee did not propose remedial action, Audit was of the opinion that some associated EFT control risks still existed and recommended that these residual risks be considered for inclusion in the corporate risk register. The Public Trustee agreed with Audit's observations and will implement the recommended approach.

Reviews of other agency EFT arrangements during 2010-11 have again identified weaknesses in EFT control arrangements. These weaknesses have been reported on in individual agency commentaries in Part B of this Report.

Concluding comments

The 2009-10 Report raised the matter of significant weaknesses in EFT processing arrangements for agencies, including SSSA. Those weaknesses exposed the Government and agencies to loss of monies.

The 2010-11 follow-up audit review of EFT arrangements has identified that many weaknesses still remain. SSSA does not anticipate its proposed remediation activities will be completed until April 2012.

Until all remediation has been completed and its effectiveness in operation has been verified, significant risks continue. These include information security risks and the risk of immediate loss of monies, including through fraudulent activity and malicious behaviour. SSSA confirmed that its EFT remediation program would remain a key priority during 2011-12.

The priority for remediation of EFT control weaknesses applies to all agencies. This is demonstrated by continuing issues being identified by in Audit reviews of agencies during 2010-11

Given the importance of these issues Audit intends to continue monitoring the remediation activities of SSSA and undertake further specific reviews and verification of the corrective actions implemented by agencies.

Goods and services procurement capability and practice: Securing value for money or avoiding losses and liability exposure: A matter for continuing attention within government

Introduction

State public sector agencies collectively spend billions of dollars on goods and services procurement.

The 2009-10 Report provided detailed commentary on a number of matters regarding the roles and responsibilities of the State Procurement Board (SPB) and agencies under the *State Procurement Act 2004* (the Act) for goods and services procurement. The commentary highlighted shortcomings in agency procurement capability and practice, giving rise to risks of not achieving value for money outcomes or liability exposure due to inadequate practice and process. The Report also advised of actions being taken by the SPB, including proposed actions in response to Audit's suggestions made to the SPB, to meet the challenges of improving the overall procurement capability and practice of agencies.

The following provides an update on developments in this area since the last Report and also makes specific comment on the matter of market competition and testing as an important matter for consideration by agencies to achieve effective procurement outcomes for government.

Responsibilities of the State Procurement Board and agencies

Responsibilities of the SPB and the public sector agencies (including their principal [chief executive] officers) are set out in the Act.

The responsibilities of the SPB, include setting the strategic direction of procurement practices across government; developing policies, principles, guidelines and training programs relevant to procurement operations of public sector agencies; and reviewing agencies' compliance with SPB policies, principles and guidelines.

Chief executive officers and their public sector agencies are responsible for the efficient and cost effective management of the procurement operations of their agencies in compliance with SPB policies, principles and guidelines.

The SPB policy and guidance framework is not overly prescriptive (by interstate comparison), but emphasises certain requirements, principles and elements of process that should be followed in procurement practice. For example, the framework emphasises the need for a competitive tender process for high risk/high value procurements, adhering to international free trade obligations (AUSFTA[1]), and applying certain elements of process for procurement stages of acquisition planning, market selection approach, supplier evaluation and contract management. The SPB framework should be supplemented by agency local policies and guidelines.

The adherence to SPB requirements and principles will facilitate the achievement of the objectives of the Act for procurements, that of value for money, fair treatment for suppliers, and probity and accountability of procurement practice. Alternatively, overlooking these matters can result in costly procurement outcomes, including abandonment or a repeat of a procurement process with liability exposure due to assessed improper process.

Procurement capability and practice

Section 12 (1) (e) of the Act requires the SPB 'to investigate and keep under review levels of compliance with the Board's procurement policies, principles, guidelines, standards and directions'. Consistent with this responsibility the SPB has a compliance review program of public sector agencies to monitor compliance with its framework and to assess general procurement capability of the agencies.
My 2009-10 Report provided detailed comment on the SPB compliance review program. To recap, it was designed to extend over a three year cycle 2009 to 2011, had been applied to six

1 Australia-United States Free Trade Agreement.

mainline agencies of government, and the reports emanating from these compliance reviews identified shortcomings in the procurement capability and/or policies and practices of the agencies.

The shortcomings covered the spectrum of procurement practice and process, involving acquisition planning, probity considerations, proponent evaluation, and documentation and record maintenance to evidence procurement decision-making. The 2009-10 Report described the specific nature of the shortcomings. It was also noted in the Report that certain of the shortcomings were matters that had been identified in annual statutory audits of agencies.

Finally, the 2009-10 Report referred to my communication to the Chair of the Board in August 2010, and the Chair's constructive response of the same month, to two matters raised by Audit for consideration in addressing the challenges of raising the procurement standards of public sector agencies. The matters related to the acceleration of the SPB's compliance review program and development and training.

Developments have occurred in relation to these two matters in 2010-11 and are briefly described below.

Acceleration of the State Procurement Board compliance review program

As stated in last year's Report, Audit views the SPB compliance review program as proactive and positive.

The compliance reviews of agencies are comprehensive in nature and bring to the attention of the SPB and the relevant agency important matters for improvement in procurement capability and process. The reviews and resultant reports should be seen as procurement improvement instruments.

In October 2010 the SPB approved an accelerated approach to completing the 2009 to 2011 compliance review program of mainline and some other agencies. The program was completed by June 2011. Also, during 2011-12, the SPB will be seeking updates from agencies that have been subject to a compliance review regarding their remedial action items and responses to their compliance review report.

It should be noted the agency compliance reviews undertaken in 2010-11 have raised similar shortcomings to those identified in previous reviews. This emphasises the importance of some form of continuance program of review and compliance of procurement policy and practice of agencies.

In addition, the SPB received a report from an independent accounting firm that it engaged to review and assess the SPB's review and compliance program. The report received by the SPB in July 2011 is being used by the SPB to further improve its review and compliance strategy and approach.

Audit places certain reliance on the SPB's review and compliance program of agency procurement operations. To reinforce the importance of this program, the 2011-12 statutory audits of agencies by the Auditor-General will look at how agencies are responding to the issues raised through the SPB compliance reviews.

Development and training

It is generally accepted that development training in procurement is a key driver in improving procurement capability and practice. As noted in last year's Report, Audit considered that the SPB should re-assess the extent and type of development and training that needs to be in place to facilitate improvement of procurement capability and practice in agencies.

In October 2010 the SPB approved its Capability Development Work Plan. The Plan directed development to three elemental streams of compliance and target training, formal training and education and professional development.

The SPB was also successful in securing funding to train and qualify over 100 government procurement officers in TAFE SA accredited Certificate and Diploma Courses. In addition, the SPB completed its strategic plan for 2011-13. The plan reinforces capability improvement as a primary focus.

Market competition and testing

The SPB policy and guidance framework emphasises the importance of formulating procurement decisions that achieve the best possible outcomes in both financial and non-financial terms for government.

For many procurements (particularly of high value/high complexity and risk) open and competitive tendering would seem to optimise the opportunity for government to achieve the key procurement principles of value for money, ethical and fair treatment of participants and probity, accountability and transparency. In addition, that the open and competitive tender process is undertaken in a timely manner, particularly for goods and services contracts that expire after a certain term.

Audit has noted that some major contracts of significance that have been extended (sometimes on more than one occasion) as the agency had not allowed sufficient time prior to the expiry of the contract to plan for an open and competitive tender. The extension(s) may result in lost opportunity to achieve value for money and other benefits that can come with a refreshed open tender process. Audit is now reviewing this matter in more detail in relation to certain goods and services procurement and contractual arrangements.

In the section of this Report titled 'Whole-of-government telecommunication services and agency management arrangements: benefits/cost savings missed', Audit comments on the dilution (change) of the telecommunication services panel (TSP) competition arrangements associated with customer agreements (CAs) for the provision of telecommunication services to agencies. Audit considers that the dilution of the competition arrangements for the TSP can have significant potential to reduce the competitive tender environment and the associated benefits, including value for money, that open competition can provide.

Concluding comments

The SPB is implementing positive and proactive strategies and programs, including compliance monitoring and development and training programs, aimed at enhancing the procurement capability and practice of agencies for goods and services procurement.

Audit has noted the use of extensions for some significant goods and services contractual arrangements that have expired. There may be valid reasons for such extensions without going to open and competitive tender process before expiry of the contractual arrangements. Audit is reviewing this matter in relation to some contractual arrangements that have been subject to extensions.

Effective delivery of major information and communications technology projects to mitigate risks of delays, costs and loss of benefits: Ongoing audit concern

Introduction

Previous Audit Reports have included commentary on some major ICT project developments. This has been done to highlight commonly occurring problems that arise during their development and implementation.

The problems encountered, if not managed in a timely and proper manner, can result in increased costs, and time/benefit realisation delays or material loss through project abandonment. The adverse consequences can sometimes not only affect the agency, but can also affect cross agency operations.

The commentary that follows provides an overview of some current ICT projects that have encountered certain problems in meeting approved planned outcomes. The experience in these matters reinforces the importance of effective independent quality assurance and regular reporting on progress of these projects to Cabinet.

Taxation revenue management system project

Project background

Initial comment was made on the taxation revenue management system (RISTEC) project in the 2005-06 Auditor-General’s Annual Report to Parliament. In that Report, Audit conveyed that initially envisaged project completion timeframes of around 2006 or 2007 would not be achieved.

The RISTEC project is to develop a replacement integrated taxation system for DTF, RevenueSA existing legacy taxation systems. It is being implemented in stages. RevenueSA collects in excess of $3 billion per annum in state taxes, including payroll tax, land tax, the fixed property component of the Emergency Services levy and stamp duties. The legacy taxation systems have been in operation for nearly 20 years.

Audit’s last comment on the progress of the project was made in the Supplementary Report of December 2009. That Report noted that in December 2008 Cabinet was advised of an overall cost for the project of $44.3 million with full implementation expected by September 2011. It also mentioned that there was a delay in achievement of revenue/taxation benefits of $15 million.

Project delays

Since that time, Audit has monitored and kept informed of key developments for the project. In June 2010 Audit was provided with a report to the RISTEC Project Board for completion of Stage 1 of the project (design).

The report highlighted two significant events that delayed the completion of Stage 1. These were the unavailability of the Queensland Office of State Revenue intellectual property documentation and the lack of required functionality in the new SAP Pty Ltd Taxpayer Online Services System (SAP). It also meant that the timeframe for Stage 2 (build, test and deploy) would be extended by five months. That is, an overall project extension from September 2011 to July 2012. Notwithstanding the delays, the project cost remained within the approved budget.

Stage 2 involves the following component releases:

- Release 1 base SAP system and payroll tax
- Release 2 Land tax and emergency service levy
- Release 3 Stamp duties and sundry taxes.

In December 2010 the Stage 2 timelines were further extended to:

- Release 1 - August 2011
- Release 2 - March 2012
- Release 3 - remained July 2012.

This also took into account delays in resolving quality issues with certain SAP ‘enhancement’ software.

Health check and shortcomings

Within the context of the replanned Stage 2 timelines, the Project Board initiated a project health check to be undertaken by an external party. Audit communicated certain observations on the planned project health check and other matters to DTF in January 2011.

Audit conveyed that the present replanned Stage 2 Release 2 timeline of March 2012 would necessitate the extension of the arrangements with an external service provider for support of the current emergency service levy system for an additional 12 months. Audit further conveyed that the health check needed to be very objective and clinical in its project execution, reporting of review conclusions, and in putting forward recommendations to secure effective delivery of the project within the planned timeframes.

The external health check was completed and DTF provided Audit with a copy of the report in August 2011. Also in July 2011 the Stage 2 timelines were further extended to:

- Release - 1 October 2011
- Release - 2 July 2012.

In August 2011 the Project Board approved the Release 3 timeframe of November 2012.

The health check made important observations on the project governance/management arrangements and recommended key priority actions for its future management. It found that clearer project governance and more robust vendor management and oversight may have reduced the impact of issues experienced by the project.

Further, the health check identified a number of issues and risks that may impede the successful and timely delivery of Release 1 and future releases and delay the realisation or reduce the amount of expected project benefits.

In essence it found that successful implementation of the required improvements will depend on the project's ability to promptly optimise its governance structure and project management processes. It would also depend on the introduction of an independent project quality assurance function with strong experience in similar complex and high risk IT projects.

Actual costs expended on the project to 30 June 2011 were in the vicinity of $29 million with system functionality to commence with Release 1 in October 2011 (base SAP system and payroll tax).

Department of Treasury and Finance action

As a result of the health check recommendations the Project Board approved the engagement of a quality assurance provider for the project through to its planned completion. At the time of Audit's review, DTF was preparing a report on the remaining health check findings and recommendations for the Project Board's consideration.

DTF advised it intends to prepare a report for Cabinet on completion of consideration of the health check review.

Land Services Business Reform Program

The progress with respect to this ICT project development has been subject to comment in previous Reports to Parliament, as early as 2005-06.

The Department for Transport, Energy and Infrastructure (DTEI) Land Services Group is responsible for the Land Services Business Reform Program (LSBRP). This is for the replacement of the core legacy land administration system and implementation of electronic services for land administration in the State. Although enhancements and system modifications have been made, existing land administration systems have been in operation for over 30 years, including the existing land ownership and tenure system (LOTS).

As with the RISTEC project, Audit comment on the progress of this project was made in the Supplementary Report of December 2009. The Report noted that the LSBRP development is progressing at the same time as the RISTEC project of DTF. It was further noted that these two major government ICT system developments have important interdependencies, including in relation to future data and information requirements.

Since the Supplementary Report, the issue of the National Electronic Conveyancing System also has implications for the direction/development of the LSBRP and the implementation of electronic services.

During December 2010, the Government approved a contract with an external software provider for the replacement land administration system. The contract was signed in March 2011 for a total value of $30 million. The LSBRP is anticipated to be operational in early 2014. Customisation requirements of the LSBRP system will require the existing legacy land administration systems to be retained for a further three years.

As the new land administration system will not be implemented until early 2014, Audit considers it critical that the interdependency requirements between the two systems are adequately addressed by the LSBRP due to its later development/implementation timeframe.

DTEI has recognised the importance of the interdependencies between the LSBRP and RISTEC projects and will continue to liaise with RevenueSA.

Projects with an eventual aim to replace the existing legacy land administration systems have been in progress for a number of years. The risk to the provision of services from the legacy systems will remain until achievement of the planned implementation of the new system in early 2014.

Health Oracle Corporate Systems project

Project background

The project is to replace DoH and health unit legacy general ledger and financial systems with a whole-of-health integrated system.

In June 2008, an external firm completed a business case for the replacement of patient administration and financial and materials management systems for DoH. Recommendations of the business case included separating the projects for replacement of patient administration and the replacement of financial and materials management systems. DoH advised Cabinet in November 2008 of the outcomes from the business case and proceeded with its recommendations.

The extent of the cost of the project necessitated financial approvals from both Cabinet and the SPB. Approvals were received from these bodies in November 2009 (Cabinet and SPB) and December 2009 (SPB).

The DoH implemented components of its new financial management system, Oracle Corporate Systems (OCS) from 1 July 2010.

Given the size and importance of the OCS to DoH and all health units, Audit undertook a review of some important aspects of the implementation of the OCS. This was also in recognition of difficulties being experienced in the implementation of the OCS by DoH.

Nature of the project

Implementation of the OCS in DoH and health units was being undertaken in two phases.

- Phase 1 (financials – principally some accounts payable and accounts receivable functions, general ledger maintenance and reporting, budgeting and forecasting).

- Phase 2 (supply chain and some financials – principally inventory management, product information management, iProcurement, purchasing, order management, warehouse management, accounts payable and cash management).

Phase 1 was expected to be fully operational by 1 July 2010. Phase 2 was to be implemented through a number of separate releases to hospitals and health units and expected to be fully operational by November 2010.

Audit review

As mentioned, Audit's review addressed aspects of the implementation of the DoH's new financial management system, OCS. This included examining DoH project governance arrangements, OCS project reporting and control, submissions made to the Cabinet and SPB, contract arrangements and independent project 'health checks' undertaken by external consultants.

The following commentary provides a summary of Audit's key findings from the review. These and other findings were communicated to the DoH in August 2011 and a response received in September 2011.

Key findings and Department of Health responses

Audit's review found that the OCS project had achieved some objectives of rollout of certain financial management functionality to all sites within planned timeframes. However, problems and difficulties were being experienced and the rollout of full functionality remains incomplete.

Whilst the project operates under governance and stakeholder oversight arrangements, certain concerns were identified with the project's implementation. These are summarised below.

Inconsistencies in approvals

Approval was given by Cabinet in November 2009 to incur investing expenditure of $21.14 million. This was to enter into specific contracts with Oracle and an external system integrator.

The Cabinet approval differed from SPB approvals of November 2009 and December 2009 which totalled $33.6 million. This was also for the establishment of a contract with Oracle for the supply, annual support and maintenance of the OCS and a contract with an external system integrator.

In essence the Cabinet submission did not include cost estimates beyond a five year life of the system. The SPB approval recognised a contract period of five years ($10.2 million) and a further two five-year extension options (estimated $10.8 million) at DoH's discretion. This reflected a realistic system life of 15 years which was beyond the five year system life costing approved by Cabinet.

The response by DoH took the view that the optional 10 year support and maintenance for the system was only a potential contract and as such the related estimated costs were not included in the Cabinet submission. DoH has also advised that the support and maintenance agreement entered into with Oracle was for a five year period consistent with that advised to Cabinet.

Audit considers the significant investment in the OCS would indicate that the system would operate and be supported in excess of five years. Therefore, consistent with the SPB approval the 15 year whole-of-life costs should have been included in the Cabinet submission.

Significant delays in implementation

There have been delays in implementation in a significant number of hospitals and health units with full functionality still to be implemented.

Phase 1 was implemented on 1 July 2010 to all locations identified in the Project Plan, initially with a low user base. Release 1 of Phase 2 implementation was implemented in December 2010 but only to five sites.

Although it was originally intended for all subsequent Phase 2 releases to be implemented by November 2010, this did not happen.

Given the number of hospitals and health units to still have Phase 2 functionality implemented, there is doubt about the ability of the project to be completed within the original financial approval.

DoH advised the Phase 2 remaining rollouts were currently being scoped, planned and costed and Cabinet would be updated as to any impacts that may be involved and how these will be managed. Continuation of Phase 2 rollout is planned to recommence in the second half of 2011-12. DoH further advised that as part of the completed development of the Phase 2 rollout, which will include the related benefits realisation plan, DoH will provide Cabinet with a formal update on the current status of the project and proposed completion.

No benefits realisation plans

Benefits realisation plans and strategies for the OCS project have not been undertaken.

A revised business case of October 2009 indicated that a benefits realisation plan would be prepared and finalised. Furthermore, two reports (March 2010 and June 2010) from an external firm engaged to conduct independent health checks on the project recommended that a benefits realisation plan be developed.

Audit considered that DoH should immediately identify the costs and benefits attributable to the OCS project and that it should as soon as practicable reappraise Cabinet of the current status of the project, including all costs and benefits attributable to the project.

In response, as mentioned above, DoH advised that a benefits realisation plan would be developed as part of the completed development of the Phase 2 rollout. Further, DoH advised it would provide Cabinet with a formal update on the current status of the project and proposed completion.

Non-replacement of legacy systems

Significant costs continue to be incurred, and benefits remain deferred. This is due to the inability to decommission legacy systems and the unfinished implementation of full system functionality. The legacy systems cannot be decommissioned until the completion of the remaining implementation to the majority of hospitals and health units. At the time of the review the remaining Phase 2 releases implementation plan was yet to be finalised.

Also resources are being used to support the mapping of data between the remaining legacy systems and the OCS financial systems.

DoH acknowledged the inability to decommission legacy systems.

Other matters

Audits of hospitals and health units and certain documentation sighted during 2010-11 have indicated dissatisfaction by users with aspects of training and ongoing support and with current reporting functionality.

DoH advised that training and rollout has been tightly controlled to limited numbers as the Health finance restructure was occurring at the same time so the changes had to be managed carefully. In addition, DoH advised of the intended implementation of DoH's long-term reporting solution that will be rolled out across the Health entities. DoH expects this reporting solution to provide significantly enhanced reporting functionality.

Health Enterprise Patient Administration System program

In addition to the significant project for the implementation of the Health-wide integrated financial system, OCS, DoH is also progressing the development and implementation of a major Health-wide Enterprise Patient Administration System (EPAS).

The EPAS is a platform for delivery of a state-wide electronic health record.

Audit has recently commenced a review of aspects of this significant ICT program development.

Concluding comments

The matters stated above are significant observations. Essentially, Cabinet has not been fully informed of whole-of-life costs and benefits, no benefits realisation plans have been prepared, the systems are not fully implemented and the legacy systems have not been decommissioned.

In addition to these matters, problems are being experienced with certain functionality/ reporting at health services. Lastly, training rollout and ongoing support for the implementation of the system has not been considered satisfactory by certain users at hospitals and health units.

There is also doubt about the ability of the project to be completed within the original financial approval for the capital spend for the development.

Overall concluding comments

The major ICT projects commented on in this Report are significant in terms of size, complexity and cost. They are intended to replace ageing legacy systems implemented many years ago and have long development and implementation timeframes.

Audit's review of three selected major ICT projects during 2010-11 has again identified weaknesses in project governance, delays in implementation timeframes, lower or non-achievement of expected benefits and inadequacies in reporting to Cabinet for certain projects. In addition, the legacy systems that these projects were to replace continue to operate in the agencies concerned.

Previous Reports have included comment on the need for strong project governance and control and the need for periodic reports to Cabinet on project progress, costs and achievement of benefits.

One important control being adopted for the RISTEC project of DTF is the appointment of an independent quality assurance provider for the project through to its planned completion.

It is Audit's view that all major ICT projects of government and its agencies should include an independent quality assurance function/external provider and that Cabinet should be provided with regular formal updates on project progress, costs and achievement of benefits.

Whole-of-government telecommunication services and agency management arrangements: Benefits/Cost savings missed

Introduction

In January 2008 Cabinet approved the Government entering into whole-of-government agreements for the supply of voice carriage services[2] and data carriage services[3] to agencies through a TSP. The TSP was to replace existing agency contracts for voice and data carriage services and the Government telecommunication services agreement (TSA).

The Government (through its agencies and statutory authorities) has an estimated expenditure of $41 million per annum through the TSP for voice and data carriage services from external third party suppliers. This excludes service costs for other telecommunication related services, such as mobile carriage services, the Government radio network and managed network services.

Given the importance and complexity of telecommunication services within the Government, Audit saw it important to review the implementation process of the TSP at both a whole-of-government and agency level.

This review activity is part of a larger and continuing review focus by Audit of assessing the overall governance and management of telecommunication services for government agencies. As a consequence, Audit will be conducting other telecommunication related reviews in 2011-12. In particular many agencies receive and are billed for voice and data carriage services through DTEI's Office of the Chief Information Officer (OCIO) – StateNet Services. This is one such related area that will be subject to review.

The immediate commentary that follows presents a summary of the Audit review. It provides background information to the TSP, scope of the audit and key matters arising from the audit. The immediate commentary is then followed by two sectional commentaries which provide more detailed information relating to the results of the review at the whole-of-government and selected agency levels.

2 Voice carriage services – provides the means to enable the State's personnel to make and receive local, national and international calls from fixed line telephones.

3 Data carriage services – provides the means for the carriage of the State's data in electronic form between Government sites and from the State's data networks to the internet.

Summary of audit review

Perceived benefits and challenges of the telecommunication services panel

The perceived benefits of the new TSP were outlined in the January 2008 Cabinet submission. Some of the key benefits were:

- there was a possible reduction in costs to the State. Although the overall expenditure estimates could not be confirmed until all CAs were finalised the initial cost saving estimate was $5 million per annum
- a panel of suppliers (TSP) would drive competition leading to better pricing outcomes
- changes to technology could be adopted more quickly due to the diverse service offerings of the TSP suppliers
- the TSP would provide a more streamlined, responsive and timesaving process for agencies
- the TSP would ensure a significant choice of suppliers for voice and data carriage services that would minimise the risk of an agency not being able to satisfy its requirements.

Notwithstanding these potential benefits, the wide ranging nature and complexity of the telecommunications arrangements and requirements within government, presented (and continue to present) a number of challenges. Audit was advised that the initial implementation of telecommunication services into the TSP involved the migration of approximately 24 000 voice and data services. Performing this task required appropriate resourcing, communication and management support from not only the OCIO but just as importantly from the affected agencies and the TSP suppliers.

Implementation of the telecommunication services panel

During the period April to September 2008, six TSP purchase agreements were executed with telecommunication suppliers. At the time of preparation of this Report approximately 50 CAs have been entered into by government agencies with the TSP suppliers. Of these 50 CAs, one telecommunication supplier has approximately 70 percent of the total market share.

Each TSP purchase agreement has a contract term of approximately six years. To help maintain the competitiveness of the TSP the Cabinet submission indicated individual CAs between agencies and the TSP suppliers would be no longer than three years and would then be subject to TSP competition.

The management and administration of the whole-of-government telecommunication contracts is the responsibility of the OCIO.

Scope of telecommunication services panel audit

In 2011 Audit performed a review of some important aspects of telecommunications management and arrangements in relation to the TSP (whole-of-government and selected agencies).

The audit included examining the OCIO governance arrangements and responsibilities in the management of the TSP. It also included reviewing the governance arrangements of selected agencies in their initial procurement and ongoing management of their TSP CAs for both voice and data.

Agencies selected for review were DoH, Courts Administration Authority, South Australian Water Corporation and the Attorney-General's Department (AGD).

Key matters arising from the audit

The following provides a description of the key matters arising from the review of whole-of-government and agency arrangements.

Whole-of-government

- There were significant delays in agencies transitioning to the TSP arrangements, thus reducing the perceived benefits of the TSP.
- There was a subsequent dilution (change) of the original TSP re-compete process. Under the change while the agency is required to engage with each TSP provider at the end of their CA (three year term), if value for money cannot be guaranteed then the agency is not required to adopt an extensive TSP competition approach for their next three year CA. This can have significant potential to reduce the competitive tender environment and the associated benefits that this can provide.
- The estimated TSP costs supplied to Cabinet were incorrect.

Agency

- Many agencies had weaknesses in their invoice verification process and were reliant on the accuracy of the vendor invoice and supporting reports.
- Some procedures were not documented or current.
- Deficiencies existed in the original TSP selection evaluation.
- The AGD in particular had a slow transition to the TSP arrangements.

These matters are discussed in more detail in the following sections of the report.

Overall concluding comments

Cabinet's approval in January 2008 for the implementation of a whole-of-government TSP agreement for both voice and data carriage services envisaged a number of perceived benefits. These benefits included costs savings and increased supplier competition.

Audit's review of the implementation and management of the TSP has highlighted a number of matters. In particular, significant implementation delays by agencies to the TSP arrangements have occurred and there has been a dilution of the TSP re-compete arrangements. These matters have reduced the anticipated costs savings and have the potential to weaken competition within the tender environment.

The OCIO project approach to transition voice and data services from the previous TSA to the TSP panel was classified as a 'light touch' transition project. Under this approach the agencies (not the OCIO) were ultimately responsible for managing the transition of their service arrangements with their TSP suppliers. Audit considers that the OCIO will need to take a harder and more authoritative approach in the implementation of future whole-of-government telecommunications arrangements to ensure optimal benefits are achieved. This approach should also be adopted in any other whole-of-government initiatives undertaken by the OCIO.

In relation to the implementation and ongoing management of the TSP arrangements within government agencies Audit has raised a number of common weaknesses. In particular, many agencies had weaknesses in their invoice verification process. This meant that agencies were reliant on the accuracy of the vendor invoice and supporting reports. To help with the invoice verification process agencies need to maintain accurate internal telecommunication asset listings and on forward copies of invoices to all applicable business units. At the moment government agencies are at risk of being overcharged for telecommunication service provision or of paying for telecommunication services not provided.

Other common weaknesses related to agency telecommunications procedure documentation and the initial CA TSP selection evaluation processes of agencies. For the selected agencies reviewed it was noted that the AGD had a very slow transition to the TSP arrangements.

As a result of the review findings, Audit recommended that the OCIO formally update Cabinet on the TSP arrangements, notably matters concerning agency transition delays, changed re-compete conditions, and cost benefits. The OCIO has advised that this is to occur.

Against this background, focused follow-up reviews of key remedial actions proposed by the OCIO and individual agencies will form a component of the 2011-12 program of audit. Audit also intends to undertake a more detailed assessment of the governance and billing arrangements for agency voice and data carriage services.

Whole-of-government implementation of voice and data services

Preface

The TSP consists of a panel of suppliers for the provision of voice and data carriage services for government agencies. The aim of this panel arrangement is to drive competition, thus leading to better pricing outcomes.

The OCIO Contract Management Group is responsible for the implementation and ongoing management of the whole-of-government TSP contract arrangements.

As mentioned previously, aspects of the OCIO's responsibilities and accountabilities for these arrangements were subject to Audit review. The following commentary discusses in detail the results of the review, including the response from the OCIO.

Summary of findings

The review revealed certain positive governance arrangements. There were however, a number of serious shortcomings requiring attention. Importantly, the nature of these shortcomings has adversely affected the savings and benefits initially envisaged under the TSP arrangements.

In particular, Audit noted significant transition delays to the TSP arrangements for a number of agencies. These transition delays have reduced expected cost savings. Also in cases where an agency has yet to transition, the agency can potentially be exposed to contractual non-performance liabilities.

Another matter of concern has been the change in the original re-compete process. The term of any agency CA or any individual service was to be restricted to three years and then be subject to TSP competition. Under the change while the agency is required to engage with each TSP provider at the end of their CA (three year term), if value for money cannot be guaranteed then the agency is not required to adopt an extensive TSP competition approach for their next three year CA.

The OCIO sought advice from the Crown Solicitor's Office and notified the TSP suppliers of the amended re-compete arrangements. Audit considers that the change to the TSP re-compete arrangements can have significant potential to reduce both cost savings and the timely adoption of new technologies. TSP suppliers expressed concern over the change indicating that it can reduce goodwill and a cooperative business relationship between government and supplier.

In terms of the expected costs associated with voice and data services the initial cost estimates supplied in the January 2008 Cabinet submission were incorrect. Total per annum spend was overestimated by $19.8 million, with an associated overestimate of cost savings of $1 million. These discrepancies were attributed to double counting, the inclusion of other internal management costs and a lack of accurate knowledge about agency voice and data spend prior to the TSP.

In communicating the results of the audit to the OCIO, Audit recommended that the OCIO formally update Cabinet on the transition delays and the amended TSP re-compete arrangements. It was conveyed that particular emphasis should be placed on the agencies that have not transitioned to the TSP. In addition, Audit indicated that the matter of assessment of budget savings achievable should also be addressed in an update to Cabinet.

Whilst the resolution of most issues requires the joint involvement of the OCIO, government agency and TSP supplier, Audit indicated that the OCIO should take the initiative in addressing the issues raised.

The following lists audit findings arising from the review of the whole-of-government TSP implementation for the provision voice and data services.

Findings of a positive nature

Audit noted a number of positive governance arrangements within the OCIO. These were:

- The OCIO was able to provide detailed and easy to read process documentation relating to ICT governance within the OCIO.
- The Contract Management Group within the OCIO has regular contact with the TSP suppliers in formal minuted meetings. Action points are recorded with responsibilities allocated.

- Many deliverables relating to TSP were recorded with nominated timeframes.
- Contract issues were recorded and managed in a Contract Management database.
- An OCIO commissioned external review in 2008 highlighted a number of proactive controls within the Contract Management Group.
- TSP progress and issues have been raised and minuted in ICT Steering Committee and ICT Board meetings.
- Escalation letters were sent to agencies by the OCIO on a number of occasions to prompt transition to TSP and reduce the associated risks of remaining under the former TSA contract arrangements.

Notable shortcomings requiring attention

Audit identified a number of notable matters requiring attention. They adversely affected the achievement of the intended savings and benefits of the TSP arrangements. The matters were:

- significant agency delays in the transition to the TSP
- some agencies were still using the old TSA arrangements
- costings supplied in the January 2008 Cabinet submission were incorrect
- insufficient OCIO authority to transition agencies to the TSP
- agencies experienced resource issues with the TSP
- inadequate agency telecommunication records management
- deficiencies in agency understanding of the TSP
- support limitations from TSA supplier for TSP transition
- initial TSP supplier support difficulties
- limitations on TSP service scope
- dilution of TSP re-compete conditions
- supplier concerns regarding the amended TSP re-compete arrangements.

Audit understands that many of the findings relate to agencies and the suppliers of which the OCIO may have limited responsibility/authority. Audit suggested a reassessment of the domains of responsibility/authority for the OCIO and agencies be undertaken in determining how the particular findings are to be addressed.

Audit comment on shortcomings

The notable shortcomings identified by Audit for attention are commented in more detail hereunder.

Significant agency delays in whole-of-government transition to telecommunication services panel

It was estimated that the whole-of-government implementation of TSP required the transition of 24 000 voice and data services from the former TSA. Although classifying and transitioning all services would be a complex task, the January 2008 Cabinet submission envisaged that the transition would only take up to seven months, between the period of January 2008 and July 2008. This was not achieved.

The majority of agencies have now transitioned to the TSP. There had been considerable implementation delays. At the time of preparation of this Report some agencies had yet to transition.

These delays required repeated TSA extensions to be negotiated with the final extension taking the interim disengagement arrangements up to two years after the TSA contract had finished. Despite the TSA contract extensions, the delays had resulted in some agencies' telecommunication services being out of contract. Those agencies out of contract would have been subject to some potential risk of higher telecommunications costs and uncertainty of terms and conditions of service provisions.

Some agencies were still using the old telecommunication services agreement arrangements

At the time of initial Audit inquiry in February 2011 the following agencies had yet to transition to the TSP and were using telecommunication services under the old TSA conditions:

- the AGD Department[4]
- the South Australian Fire and Emergency Services Commission (SAFECOM) (this includes telecommunication services for the Metropolitan Fire Service, Country Fire Service and the State Emergency Service).

Audit understands that agencies that had not moved to the TSP from the old TSA arrangements had no formal service contract in place and did not receive the TSP service rates. Audit was advised that the OCIO communicated to these agencies on a number of occasions the need to move to the TSP for the provision of voice and data services.

Costings supplied in Cabinet submission were incorrect

The Cabinet submission approved in January 2008 stated that the cost of delivering telecommunication services under the TSA contract was approximately $49.8 million per annum for voice and $15 million per annum for data (total cost $64.8 million).

The Cabinet submission provided an estimated cost savings of $5 million per annum under the new TSP arrangements. It was stated however that a definitive figure could not be supplied until all CAs were finalised.

The OCIO advised that the first reliable 12 month TSP reporting period was from October 2009 to September 2010. This was due to both lengthy delays in agencies transitioning to the TSP and early reporting problems experienced with suppliers. In this period the OCIO was able to take into account costings from the majority of agencies, excluding the AGD and SAFECOM.

In assessing the TSP reporting period (October 2009 to September 2010) an OCIO mid-term review indicated in March 2011 that there was an overestimate of the initial TSP per annum spend against the actual per annum spend. This overestimate amounted to $19.8 million.

[4] Audit has since been advised by the Attorney-General's Department that a TSP customer agreement was signed in June 2011 with a TSP supplier.

Revised estimated savings based on the actual expenditure of around $41 million per annum were approximately $4 million per annum (against the original envisaged $5 million per annum). Audit understands that no detailed analysis has been performed on the actual cost savings beyond approximate figures.

This discrepancy could be attributed to double counting, the inclusion of other internal management costs and a lack of accurate knowledge about agency voice and data spend prior to the TSP.

Insufficient Office of the Chief Information Officer authority to transition agencies to the telecommunication services panel

The OCIO project approach to transition voice and data services from the previous TSA to the TSP Panel was classified as a 'light touch' transition project.

Under this arrangement agencies (not the OCIO) were ultimately responsible for managing the transition of their service arrangements with their TSP supplier(s) as well as managing any disengagement requirements and service continuity risks.

To assist the transition the OCIO provided a number of information sessions with agencies. The sessions were to explain the TSP implementation process. The OCIO also sent targeted formal letters to those agencies whose transition delays were deemed to be at high risk.

Despite this assistance, the 'light touch' approach used by the transition project did not have sufficient applied authority to ensure TSP implementation across agencies within the desired timeframes.

Sufficiency of agency resource application to the telecommunication services panel

The success of the TSP transition was reliant on not only the OCIO but the activities of the individual government agencies and the TSP suppliers. Information provided to Audit suggested that some agencies did not supply sufficient or have adequate resourcing to transition to the TSP arrangements.

Some of the reasons highlighted were that the focus and priority applied by some agencies to deliver the transition requirements was not consistent, key agency staff had moved on and agency telecommunications data was not kept up to date. Audit also noted difficulties in the OCIO project team engaging the right people in agencies.

Agency staff for example, that were responsible for paying the voice bills were often required to deal with the request for quote and CA process. These staff may not have had sufficient knowledge, authority or time to complete the transition process. This was particularly the case with smaller agencies.

Inadequate agency telecommunication records management

For an agency to satisfactorily complete the request for quote and CA processes, a complete and accurate record of telecommunication assets and service details was crucial.

Information supplied to Audit indicates that some agencies had incomplete and /or incorrect telecommunication records. This was compounded by some agencies separating voice and data management and responsibilities into different areas.

Deficiencies in agency understanding of telecommunication services panel

Given the complexity of telecommunication services, it was important that agencies had an understanding of their telecommunication service requirements and were aware of the contractual responsibilities of their suppliers. It was also important that agencies were familiar and utilised the reporting mechanisms available to highlight any real and potential support issues and to verify the accuracy of telecommunication billing.

Information provided to Audit indicated that there were instances of agency knowledge deficiencies relating to the TSP transition requirements and ongoing contract management.

The OCIO Contract Management Group reported that there was some early confusion around the definition between fixed data services and mobile data services. Also feedback provided indicated that some agencies did not have an understanding of all OCIO resources available for assistance.

The OCIO had in the past tried to resolve these knowledge deficiencies within agencies by the proactive provision of information sessions and kits. The OCIO is in the process of developing online tutorials and plans to conduct briefings sessions to improve contract knowledge within agencies.

Telecommunication services agreement supplier support limitations for transition to telecommunication services panel

The incumbent TSA supplier needed to provide critical input in an agency's transition from TSA to the TSP. This included reporting of TSA telecommunication assets and disengagement support.

In the OCIO information provided to Audit, it was indicated that some transition delays could be attributed to a lack of TSA supplier resourcing and accuracy of their reports to agencies.

Initial telecommunication services panel supplier support difficulties experienced

In general, feedback provided regarding TSP suppliers was that the suppliers were responsive, provided adequate communication and were generally professional. This was apart from some teething issues in the initial implementation of the TSP. The OCIO Contract Management Group also had regular formal meetings with the suppliers to discuss and resolve any issues.

Despite this positive feedback some agencies raised a number of matters to the OCIO with certain matters resolved during the TSP transition. These included suppliers being reluctant to implement government reporting and process requirements outlined in the contracts and not all transition deadlines were met by suppliers. In addition, some agencies experienced problems with suppliers providing accurate invoicing and billing information. There were also instances of suppliers not responding (or delaying responses) to request for quotes.

Limitations on telecommunication services panel service scope

A benchmarking review, performed by an external consulting firm indicated that the TSP generally gave agencies a cost effective voice and data service arrangement, using a range of potential service suppliers.

Despite these benefits agency feedback indicated potential limitations. These included the TSP being inflexible in relation to 'specialist services' or non-standard voice or data services. In addition not all suppliers could compete equally, especially in regional and remote areas, where they had to include infrastructure costs in their quotes.

Dilution of telecommunication services panel re-compete conditions

The January 2008 Cabinet submission for TSP advised that the term of any associated agency CA or any individual service will be restricted to three years. This time restriction was to ensure the panel was used effectively to maintain price competitiveness as well as avoiding the risk of long-term lock-in to legacy technological solutions. The aim was to have all CAs subject to ongoing competition via the panel.

Since the Cabinet submission, some agencies expressed concerns with the TSP requirement to re-contest all services at the expiry of their CAs. Many agencies wanted to seek an exemption from the TSP re-compete process.

Some agencies for example stated that the cost in agency resource effort to conduct a full re-compete was high, potentially meaning that any cost savings from the re-compete would be lost. In addition feedback to the OCIO indicated that many agencies were happy with their current supplier in terms of service and price and hence would remain with their incumbent supplier.

For some agencies delays in establishing initial CAs has meant that a number will not be due to re-contest services until late 2012. This means pricing from suppliers will be for less than three years, thus potentially resulting in less than optimal pricing.

As a consequence the OCIO mid-term review in March 2011 recommended that agencies will be required to engage with each TSP provider at the end of their CA agreement term to review their current arrangements against those offered by alternative TSP members. However, if improved value for money cannot be guaranteed then the agency will not be required to undergo an extensive market approach.

Although Audit understands that the OCIO has stated a number of reasons behind changing the re-compete arrangements Audit considered that this will dilute the re-compete requirements. This dilution potentially reduces the overall integrity of the price and service objective of the TSP panel. Suppliers also stated that a reduced re-compete arrangement may result in agencies not assessing new voice and data technologies and service offerings that may provide further benefits.

In essence, Audit considers that the changes to the TSP re-compete arrangements can have significant potential to reduce both cost savings and the timely adoption of new technologies.

Supplier concerns regarding amended telecommunication services panel re-compete arrangements

A proposal to alter the re-compete arrangements was initially communicated to the TSP suppliers in December 2010.

In response the TSP suppliers, with the exception of the dominant TSP supplier, expressed concern over the proposed alterations to the re-compete arrangements. In particular suppliers have expressed concerns regarding potential implications to any future agency business under the new TSP re-compete requirements. These changes potentially reduce goodwill and a cooperative business relationship between government and the supplier.

Office of the Chief Information Officer response

In July 2011 the results of the audit were formally communicated to the OCIO. The OCIO provided a detailed response in August 2011.

In particular, for the following main concerns the OCIO response indicated:

- Transition delays – The OCIO agreed that the agency transition delays had reduced the extent of the anticipated TSP benefits. The OCIO stated that during the TSP implementation period they had made an extensive effort to assist agencies to both prepare and implement the TSP arrangements. An example listing of the regular OCIO communications to SAFECOM to encourage transition to the TSP was provided.

  The OCIO emphasised that it was ultimately the individual agency Chief Executive who was responsible for their agencies' implementation and ongoing management.

  To help reduce future transition delays in ICT procurements OCIO will make allowances, where possible, for appropriate transition-in periods prior to the formal commencement of new arrangements. This should allow more time for agencies to prepare and hence reduce transition delays.

  Audit notes however, that ongoing participation by the OCIO in providing valuable transition assistance to agencies will be challenged due to budget constraints. These budget constraints have resulted in a reduction in dedicated OCIO transition and procurement staff.

- Re-compete dilution – The change to the re-compete arrangements means that the agency no longer must re-compete their TSP business at the end of their initial customer agreement terms. The OCIO has indicated that agencies should still consider undertaking the re-compete process. A recent notification to agencies stated that before a CA expires an agency is expected to engage with all TSP suppliers to discuss requirements.

  The OCIO has stated that the dilution of re-compete arrangements was in response to the concern of several agencies that the re-compete process would take significant resourcing and time. In addition, because of the shorter time left, some agencies also had concerns that a fresh re-compete may result in price increases in voice and data service costs.

- TSP costing errors – OCIO advised that an update to the Cabinet is being developed on certain TSP matters, such as agencies yet to transition and cost amendments for the TSP.

Concluding comments

The implementation of voice and data carriage services under the TSP agreement had a number of perceived benefits. These were not achieved to the extent envisaged.

There were a number of matters highlighted by Audit that have reduced the extent of such benefits being realised. Importantly, implementation delays and the dilution of the re-compete arrangements have reduced the anticipated costs savings and have the potential to weaken competition within the tender environment. Also costings in the January 2008 Cabinet submission for the TSP were in error.

Audit recommended that the OCIO formally update Cabinet on the agency transition delays to the TSP, the amended TSP re-compete arrangements and TSP cost benefits. The OCIO has advised that this is to occur.

Audit also considers that the OCIO will need to take a harder and more authoritative approach in the implementation of future whole-of-government telecommunications arrangements to ensure optimal benefits are achieved. This approach should also be adopted in any other whole-of-government initiative undertaken by the OCIO.

As mentioned previously, aspects of the OCIO whole-of-government telecommunications arrangements will form a principal component of the 2011-12 program of audit.

Agency telecommunication management arrangements

Preface

Government agencies were required under the whole-of-government TSP arrangements to transition the provision of their voice and data carriage service requirements to the TSP. The responsibility and accountability for transitioning to the TSP arrangements and the subsequent management of the services received under the TSP rests with the chief executives of agencies.

As previously mentioned, certain agencies were selected for review of their governance arrangements for their initial procurement and ongoing management of their TSP CAs for both voice and data carriage services. The agencies selected for review were DoH, Courts Administration Authority, South Australian Water Corporation and the AGD.

The following commentary discusses the details of the results of the review, including responses received from the agencies that were selected for review.

Summary of findings

Department of Health

The review examined the initial procurement and ongoing management of their CAs with two separate TSP service providers. Although not assessed in this review DoH can incur other telecommunication related costs from other government departments and third party service providers. An example is mobile carriage services which were excluded in this review component.

Given the diversity of TSP service provisions and the associated complexity of charges, Audit considered that there is the potential for errors to occur in both supplier invoices and internal department recharging. Despite this risk the audit revealed that minimal checking of TSP invoices and internal recharge billing for TSP services occurred within DoH. DoH was reliant on the accuracy of the telecommunication vendor invoices and their supporting reports.

The key matters raised in the TSP review and formally communicated to DoH are summarised below:

- Not all of DoH's documentation relating to the initial TSP supplier evaluation process was readily available.

- Estimated cost savings in adopting the TSP could not be confirmed.

- There were deficiencies in the supporting invoice process documentation and reports used to manage the billing verification.

- DoH was reliant on the billing accuracy of the telecommunication supplier managed reports.

- DoH was reliant on the telecommunication supplier for voice carriage service asset listings.

In response DoH accepted Audit's findings and recommendations. DoH stated that for the individual TSP related matters raised they have either been remediated, have an action plan in place to address the matter or will address the matter during the next contract review cycle.

DoH has also commenced a review of TSP related processes using a third party audit firm specialising in telecommunication related services. This review was expected to be completed by the end of August 2011.

South Australian Water Corporation

The South Australian Water Corporation (SA Water) uses multiple suppliers for both voice and data carriage services.

In relation to the TSP, SA Water has four separate contracts with different suppliers. SA Water also uses another telecommunication provider arrangement that was in place before the TSP. This arrangement is expected to migrate to the TSP shortly.

The review for SA Water assessed the initial procurement and ongoing management of the two main TSP telecommunication arrangements. It also looked at the ongoing management for the telecommunication provider arrangement in operation before the TSP.

The key matters arising from the review and formally communicated to SA Water are summarised below:

- SA Water TSP evaluation did not produce information that would allow an informed decision on pricing.

- SA Water had a supplier classification regime that potentially did not include all major telecommunications contracts, which may have implications for the way in which particular contracts are managed.

- There were opportunities for improvement identified concerning the verification of telecommunications invoices.

- SA Water needed to develop procedural documentation that covers the key essential areas concerning the verification of supplier telecommunication invoices and their reconciliation.

In response SA Water accepted the matters raised by Audit and the associated recommendations.

In particular a new telecommunication acquisition strategy is currently under development and a supplier management framework has recently been instituted. SA Water will examine methods of enhancing invoice verification along with performing annual audits of data services and utilising active monitoring of fixed voice services. Procedural documentation is also to be enhanced.

Attorney-General's Department

The focus of the review of the AGD was slightly different to the other agency reviews as the AGD had not transitioned to the TSP arrangements at the commencement of the review. The 2011 review is the first phase of a two phase review process.

The first phase of the review examined aspects of governance and billing management of voice and data services for the AGD under the original TSA and the transition in June 2011 to TSP CAs. The AGD's estimated annual spend for the June 2011 implemented TSP service is under $100 000.

It is planned that the phase two review will commence early in the 2011-12 financial year. This review will examine the governance and billing management of other voice and data services supplied to the AGD. These services are primarily billed OCIO – StateNet Services and Justice Technology Services and represent a significant cost outlay.

The key matters arising from the first phase review are summarised below.

- The AGD failed to comply with the Government directive for transitioning to the TSP by September 2009. The AGD acknowledged that the delay in transitioning to the TSP contract was the consequence of an administrative error. During this period the AGD had relied upon the expired conditions of the original TSA agreement.

- The TSP purchase recommendations and evaluations of preferred telecommunication service providers, dated September 2009, were not actioned until April 2011.

- Ongoing management and governance surrounding the TSA agreement with the third party supplier was irregular, informal and lacked supporting documentation.

- Weaknesses existed surrounding the invoice verification process relating to the TSA agreement. These included:

  — some invoices not on-forwarded to business units for confirmation of accuracy
  — business units unaware of appropriate charges for some services provided.

- The level of supporting invoice processes, documentation and reports relating to the administration of the TSA agreement by business units was deficient and in some instances misunderstood.

Whilst AGD business units examined undertook reasonableness checks on billing invoices, they were not performing comprehensive reviews for both voice and data. The AGD will seek the provision of more detailed monthly billing from OCIO – StateNet Services that are by business unit.

In relation to telecommunication charging by Justice Technology Services, the AGD have advised that these costs are currently apportioned to the AGD on an agreed pro-rata basis and use an agreed formula. Hence, rather than trying to verify individual data volumes used as part of the invoice verification process the AGD will conduct a formal annual review of the formula and data links used to determine the billing formula.

In response the AGD accepted Audit's findings and recommendations and have provided their remediation approach.

Courts Administration Authority

The review of the Courts Administration Authority (the Authority) covered not only the billing arrangements of voice and data service by the TSP service providers but also the billing arrangements of separate voice and data services through OCIO – StateNet Services and the AGD.

The review concluded that the Authority had processes to manage voice and data related invoices and also request changes to required service offerings within the TSP CAs. Although business units were reliant on the telecommunication supplier's produced usage reports for cost verification (if required) it was expected that any major invoice discrepancies and redundant service charges could still be highlighted by the individual business units within the Authority.

Despite these controls Audit highlighted certain findings to further improve the Authority's governance of telecommunication charging. The key matters are summarised below:

- Although the Authority considered that all TSP suppliers were evaluated in the initial TSP procurement process this was not evident in the final business case.

- Not all cost centres' contacts were sent a copy or extract of the external TSP supplier and OCIO – StateNet Services invoices for verification checking.

- The invoice details were not sent out to the respective cost centre owner(s) for certain charged services.

- The monthly data invoice from the AGD and also the external TSP supplier invoice for electronic messaging had no formal scheduled inventory review process against the invoice detail listings. For both invoices however the device list and hence associated charges were reasonably static.

In response the Authority accepted Audit's suggested improvements and has put in place an action plan for this to occur. The Authority advised that many of the actions have been completed, with the remainder expected to be finalised by the end of 2011-12, apart from those relating to a new contract cycle.

Concluding comments

Each selected agency reviewed had variances in how voice and data services were supplied. Notwithstanding, there were a number of common weaknesses noted.

In particular, many agencies had weaknesses in their invoice verification process. This meant that agencies were reliant on the accuracy of the vendor invoice and supporting reports. To help with the invoice verification process agencies need to maintain accurate internal telecommunication asset listings and on forward copies of invoices to all applicable business units.

Other common matters raised were deficiencies in telecommunications procedure documentation and the initial TSP selection evaluation process. The AGD in particular also had a slow transition to the TSP arrangements.

The audit findings arising from the review of selected agencies indicate generally that government agencies are at risk of being overcharged for telecommunications service provision or of paying for telecommunication services that have not been provided.

As mentioned previously, I intend to undertake further review work at agencies in 2011-12.